AFRICAN DEVELOPMENT BANK GROUP
GROUPE DE LA BANQUE AFRICAINE DE DÉVELOPPEMENT

AFRICAN ECONOMIC OUTLOOK 2024

Driving Africa's Transformation

The Reform of the Global Financial Architecture

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ISBN: 979-8-9893890-9-4

FOREWORD

Despite entrenched structural challenges and susceptibility to exogenous shocks, most African economies have shown remarkable resilience. Over the past four years, they have had to contend with multiple overlapping exogenous shocks, including persistently high food and energy prices on the back of the sustained impacts of Russia's invasion of Ukraine and other geopolitical tensions, climate change and extreme weather events on agricultural productivity and electricity generation, and pockets of political instability and conflicts. Against this backdrop, Africa's average growth in real GDP decelerated to an estimated 3.1 percent in 2023 from 4.1 percent in 2022, slowing the momentum of economic recovery, as successive shocks weakened post-pandemic gains.

The forecast for 2024–25 looks promising, as global economic conditions brighten, creating optimism for a rebound and sustained economic growth across Africa. Real GDP growth is projected to rise to 3.7 percent in 2024 and consolidate higher at 4.3 percent in 2025. The sustained increase in Africa's average GDP growth underscores its resilience and benefits of policies instituted to mitigate impacts of underlying shocks and put economies back on a higher growth trajectory. This resilience is broad-based, ensuring that Africa remains the second-fastest growing region in the world after developing Asia. To underscore this, 40 countries are set to post higher growth in 2024 relative to 2023, and 15 are projected to grow by more than 5 percent in 2024. Further, 10 African countries will be among the world's top 20 fastest growing economies, a trend sustained for more than a decade.

Whereas Africa's resilience amid global headwinds is a welcome development, challenges remain not only in strengthening the continent's growth, but in ensuring that growth brings about sustainable economic and social transformation in the lives and livelihoods of Africa's citizens. Therefore, there is much work to be done. Although Africa's real GDP grew on average at 3.8 percent annually across the four decades preceding the COVID-19 period, this growth has been too little to offset increases in population growth. Over the four decades, therefore, per capita real GDP growth rates have been consistently the lowest in the world.

This is partly because the pace of structural transformation has remained slow and uneven and the structure of most African economies has not changed much since the 1990s. Traditional sectors continue to drive Africa's growth and employment. The structural transformation that has been observed across the continent has lacked a marked level of industrialization. Instead, it reflects the reallocation of economic activities and employment from agriculture to other relatively low-productivity sectors, most notably in personal and retail services, rather than more productivity enhancing manufacturing. For instance, despite accounting for 42 percent of the continent's workforce, productivity in the agricultural sector is still 60 percent lower than the average productivity of the economy.

This transformation trajectory needs to change. Africa's governments and policymakers should reconfigure their policy tools to engender and accelerate Africa's structural transformation. One promising way to improve agricultural productivity is through establishing Special Agro-industrial Processing Zones, which the Bank has been pioneering across the continent. In addition to manufacturing, services-led growth can also play a critical role, providing a holistic approach to structural transformation. To support the continent's structural transformation, no economic sector should be left behind.

To fast-track its structural transformation and catch up with high-performing developing countries from other regions, Africa will need to prioritize investments in key areas of the Sustainable Development Goals—education, energy, productivity, and infrastructure. Mobilizing the resources to close the estimated annual financing gap of $402 billion for strategic investments in these areas will not be easy. Despite the recent recovery in revenues, Africa still has limited fiscal space, exacerbated by high debt-service payments. Expanding tax capacity and catalyzing private sector investments in critical sectors will be key to mobilizing the colossal resources for Africa's structural transformation.

However, domestic resources alone will not be sufficient to finance Africa's ambitious transformation agenda. That will require the international financial system to offer additional impetus by creating a sustainable pathway for Africa's meaningful participation in resource allocation decisions to unlock vital resources for these investments. This can be realized only through implementing pressing reforms that move the global financial architecture toward a fairer, inclusive, and more transparent system. Only such a system can help deliver resources at scale and on competitive terms—rather than consign developing countries, and indeed the continent, to a perpetual debt and poverty trap. Changes in financing models of multilateral development banks (MDBs) and international financial institutions should be a top priority of the reforms. The Bank Group has been leading proposals for the reforms of the MDBs and a rechanneling of the IMF's Special Drawing Rights from advanced countries to MDBs to boost lending to developing countries, especially those in Africa.

In making the call for reforms, governments across the continent need to take complementary measures. Africa is a rich continent with vast critical minerals and rare earth metals, and using these vast resources can fund its ascent to a higher income trajectory. Investing in institutional capacity to strengthen tax administrations —especially by expanding the use of digital technology, combat illicit financial flows, and reforming tax policies, as well as building a social contract between government and taxpayers to address implicit taxation—will be vital to enhancing domestic resource mobilization. In addition, making local institutional reforms responsive to emerging challenges will help unlock resources to drive inclusive economic development and accelerate structural transformation amid a fragile global environment.

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ACKNOWLEDGEMENTS

The African Economic Outlook (AEO) 2024 was prepared in the Vice Presidency for Economic Governance and Knowledge Management (ECVP), under the general direction and supervision of Prof. Kevin Chika Urama, Chief Economist and Vice President for the ECVP Complex, with support from Ferdinand Bakoup, Amadou Boly, and Amah Koffi.

Preparation of the chapters was supervised by Abdoulaye Coulibaly, Director (Governance and Economic Reforms Department) also serving as Director (Officer-in-Charge) for the Macroeconomic Policy, Forecasting, and Research (ECMR) Department, responsible for production of the report. The core team comprised Anthony Simpasa (Division Manager, ECMR.1), Hammed Amusa, Francis Leni Anguyo, Lacina Balma, Alexandre Kopoin, Adamon Mukasa, and Martin Wafula Nandelenga, all from ECMR.1. Chapter 1 was co-led by Hammed Amusa and Alexandre Kopoin, chapter 2 by Adamon Mukasa and Francis Leni Anguyo, while Lacina Balma led the preparation of chapter 3. Administrative support was provided by Felicie Zongo Kabore and Michael Abah.

The statistical information in the report was compiled by the Statistics Department, led by Louis Kouakou (Acting Director, Statistics Department, and Manager, Economic and Social Statistics Division) and supported by Anouar Chaouch, Soumaila Karambiri, Stephane Regis Hauhouot, Slim Jerbi, and Beejaye Kokil.

Valuable contributions to the three chapters were also received from several experts within and outside the African Development Bank. Within the Bank, experts were drawn from ECMR.1 and comprised Richard Dutu, Blaise Gnimassoun, and Zackary Seogo. From outside the Bank, inputs to Chapter 2 were received from Prof. Margaret McMillan (Tufts University), Solomon Owusu (Boston University), Emmanuel Mensah (Utrecht University), Gideon Ndubuisi (Delft University of Technology), and Ali Mansoor (Senior Advisor to Deputy Prime Minister, Mauritius). Chapter 3 benefited from contributions by Hafez Ghanem (Non-Resident Senior Fellow, Brookings Institution), Prof. Belinda Archibong (Columbia University), and Phyllis Papadavid (Overseas Development Institute).

The report was also enriched by review comments from Bank staff and external experts. Within the Bank, comments and suggestions were received from a team of economists in the Country Economics Department (ECCE) led by Desire J. M. Vencatachellum (Senior Director), and comprising Audrey Verdier-Chouchane, Marcellin Ndong Ntah, Edward Sennoga, George Kararach, Paul Mpuga, Antoine-Marie Tioye, Tilahun Temesgen, Duncan Ouma, Walter Odero, Peter Rasmussen, Khadiatou Gassama, Kaouther Abderrahim, Ameth Ndiaye, Hamacire Dicko, Rachidi Kotchoni, Wolassa Kumo, Admit Zerihun, Bashir Yousif Eltahir, Ibrahim Sawadogo, Iyad Dhaoui, Godwill Kan Tange, and Luba Bahosi Miguel. Comments and suggestions were also received from ECMR.2, led by Eugene Bempong Nyantakyi, Division Manager (Officer-in-Charge) and comprising Francis Kemeze and George Marbuah. Additional comments and suggestions were provided by

Densil Magume and Sijh Diagne (Vice-Presidency for Finance), Abimbola Temilade (Office of the Senior Vice President), a team from the Strategy Department comprising Victoria Chisala (Manager, Corporate Strategy and Policy Division) and Ronald Rateiwa as well as staff from the African Natural Resources Management and Investment Center (ECNR) comprising Fred Kabanda (Manager), Leontine Kanziemo, Innocent Onah, Jerry Ahadjie, and Koffi Kpognon.

External peer reviewers included Prof. Léonce Ndikumana (University of Massachusetts at Amherst), Prof. Christopher Adam (University of Oxford), Emmanuel Owusu-Sekyere (African Center for Economic Transformation), Prof. Ramos Mabugu (Sol Plaatje University), and Abebe Shimeles (Ministry of Finance, Ethiopia).

The country notes were prepared by Country Economists (see the table below) under the overall guidance and supervision of Desire J. M. Vencatachellum, Senior Director, ECCE, and the coordination of Marcellin Ndong Ntah. Staff from ECMR.1 reviewed all the country notes. The ECNR team, coordinated by Fred Kabanda and Leontine Kanziemo, and ECST staff (Anouar Chaouch), with technical support and validation by Lead Economists for each region—Central Africa (Hervé Lohoues); East Africa (Marcellin Ndong Ntah and Edward Sennoga); Nigeria Country Department (Jacob Oduor); North Africa (Audrey Verdier-Chouchane); Southern Africa (George Kararach); and West Africa (Guy-Blaise Nkamleu)—also reviewed the country notes, which were subsequently cleared by Country Managers. Tricia Baidoo provided administrative support to the team.

The cover of the report is based on a general design by Laetitia Yattien-Amiguet and Justin Kabasele of the Bank's Communication and External Relations Department. Editing, translation, and layout were done by a team from Communications Development Incorporated, led by Bruce Ross-Larson and including Joe Caponio, Mike Crumplar, Meta de Coquereaumont, Christopher Trott, and Elaine Wilson, with design support from Debra Naylor and translation support from Jean-Paul Dailly and a team at JPD Systems.

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THEMATIC COVERAGE OF PREVIOUS EDITIONS

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2005	Financing of Small and Medium-sized Enterprise (SME) Development
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HIGHLIGHTS

CHAPTER 1
AFRICA'S ECONOMIC PERFORMANCE AND OUTLOOK

African economies remain resilient amid multiple shocks, with their average growth projected to stabilize at 4.0 percent in 2024–25, nearly a one percentage point higher than the 3.1 percent estimated in 2023.

Average real gross domestic product (GDP) growth is estimated to have slowed from 4.1 percent in 2022 to 3.1 percent in 2023. The decline is attributed to a variety of factors, including persistently high food and energy prices on the back of sustained impacts of Russia's invasion of Ukraine,[1] weak global demand weighing down export performance, climate change and extreme weather events on agricultural productivity and power generation, and pockets of political instability and conflict in some African countries. Despite the continuing headwinds, 15 countries recorded a growth rate of at least 5 percent in 2023. Although three of the continent's largest economies recorded lower real GDP growth rates, more than half (31) of African countries had higher real GDP growth rates in 2023 than in 2022, with 6 of them—Burkina Faso, Djibouti, eSwatini, Libya, the Republic of Congo and South Sudan—posting real GDP growth rates of more than 2 percentage points.

Despite the global challenges that tested economies worldwide, the African continent is projected to remain resilient. Real GDP growth is projected to rise to 3.7 percent in 2024 and 4.3 percent in 2025, exceeding the 4.1 percent in 2022, as most of the effects of the above factors weighing on growth in 2023 fade away (figure 1 and annex 1.1A). The projected rebound in Africa's average growth will be led by East Africa (up 3.4 percentage points) and Southern Africa and West Africa (each rising by 0.6 percentage points). Crucially, 40 countries will post higher growth in 2024 relative to 2023, 17 economies are projected to grow by more than 5 percent in 2024, and the number could rise to 24 the following year, as the pace of growth accelerates. This is remarkable and Africa will retain its 2023 ranking as the second-fastest growing region after Asia, in 2024-25 with projected GDP growth exceeding the global average of 3.2 percent in 2024.

1 Wording agreed at the 2022 African Development Bank Group Annual Meetings in Ghana. Algeria, China, Egypt, eSwatini, Namibia, Nigeria, and South Africa entered a reservation and proposed "Russia–Ukraine Conflict."

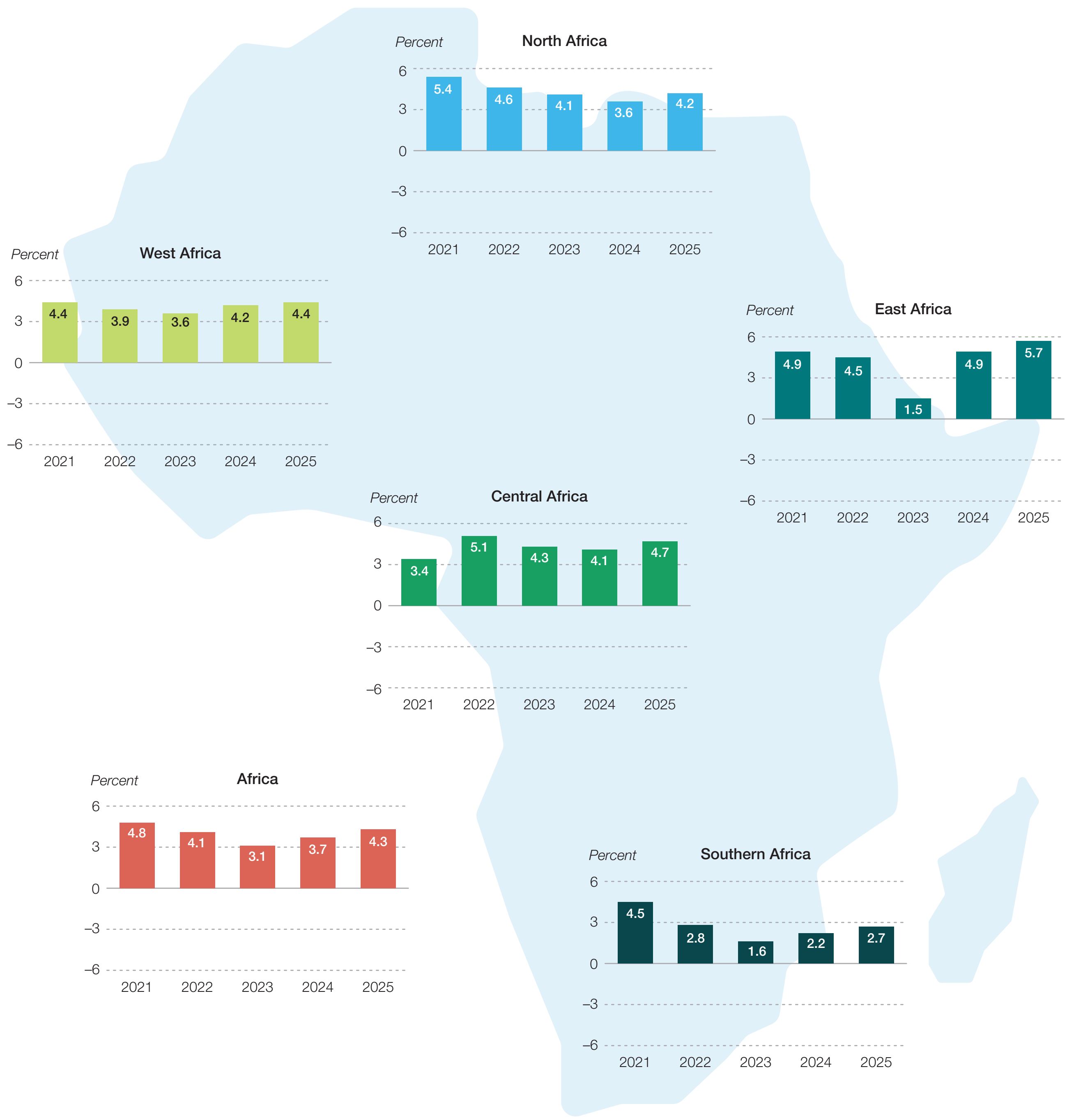
The growth outlook in 2024–25 is heterogenous across Africa's regions and economic groupings, reflecting differences in the structure of economies, commodity dependence, and the domestic policy responses to mitigate impact of these shocks.

- **East Africa** is expected to bounce back as Africa's fastest growing region, with real GDP growth rising from an estimated 1.5 percent in 2023 to 4.9 percent in 2024 and 5.7 percent in 2025. The downward revision of 0.2 percentage points for 2024 compared with the forecast in the January 2024 MEO is due to larger-than-expected contractions in Sudan and South Sudan due to the ongoing conflict in the former.
- Growth in **Central Africa** is expected to moderate from 4.3 percent in 2023 to 4.1 percent in 2024 before improving strongly to 4.7 percent in 2025. The upgraded forecast of 0.6 percentage point for 2024 over the January 2024 projections is attributable to expectations of stronger growth in Chad and the Democratic Republic of Congo due to expectations of favourable metal prices.
- Growth is projected to pick up in **West Africa**, rising from an estimated 3.6 percent in 2023 to 4.2 percent in 2024 and consolidating at 4.4 percent the following year. This is an upgrade of 0.3 percentage points for 2024 over the January MEO 2024 projections, reflecting stronger growth upgrades in the region's large economies—Côte d'Ivoire, Ghana, Nigeria, and Senegal.
- In **North Africa**, growth is projected to decline from an estimated 4.1 percent in 2023 to 3.6 percent in 2024 and 4.2 percent in 2025, with a downward revision of 0.3 percentage point for 2024 from the January 2024 MEO. Except for Libya and Mauritania, growth has been revised downward for all other countries in the region.
- Growth in **Southern Africa** is projected to pick up slightly from an estimated 1.6 percent in 2023 to 2.2 percent in 2024 and firm up to 2.7 percent in 2025. The growth rates for 2024 and 2025 show an upgrade of 0.1 percentage point over the January 2024 projections, mainly reflecting a 0.7 percentage point increase in South Africa's projected growth. Due to South Africa's larger weight in the region, the upgraded growth forecast offset the combined effect of downward revisions in Angola, Botswana, Lesotho, Zambia, and Zimbabwe.
- Average growth in **non-resource–intensive economies** is projected to improve from an estimated 4.8 percent in 2023 to 5.3 percent in 2024 and 5.6 percent in 2025. This growth is underpinned by increased public investments in major growth sectors and substantial capital outlays on critical public infrastructure including electricity, transport, and logistics.
- Growth for **tourism-dependent economies** is projected to decelerate from 5.8 percent in 2023 to 4.7 percent in 2024 and further to 3.9 percent in 2025. This deceleration reflects the stabilization of tourism numbers to trend levels, with projected slower economic growth in Mauritius and Seychelles as the key driver for the group.
- Average growth in **oil-exporting countries** is expected to decline from an estimated 3.7 percent in 2023 to 3.5 percent in 2024 but could pick up the pace to 4 percent in 2025. The projected slowdown in 2024 reflects lower oil production targets set by the Organization of the Petroleum Exporting Countries (OPEC), lower growth projections in South Sudan following the vandalizing of an oil pipeline due to the ongoing conflict, and uncertainty over new mechanisms for Angola's oil exports following its exit from OPEC.
- Growth in **other (non-oil) resource-intensive economies** on the continent is estimated to improve strongly from 0.3 percent in 2023 to 2.7 percent in 2024 and consolidate at 3.3 percent projected for 2025. The sharp increase in growth will be driven largely by rebound in China's demand for metals and minerals linked to expansions in smart grids and construction.

The projected rebound in Africa's average growth will be led mainly by East Africa (up 3.4 percentage points)

The dynamics of Africa's macroeconomic fundamentals have remained mixed amid considerable challenges. Figure 2 presents the detailed outlook for countries' key macroeconomic indicators for 2024–25 on average, while Annex 1.1B provides details for 2024 and 2025.

FIGURE 1 Growth performance and outlook by region, 2021–25 (percent)



Source: African Development Bank statistics.

Average consumer price inflation in Africa is estimated to have increased by 3 percentage points to 17 percent in 2023, from 14 percent in 2022. The increase reflects a combination of higher local food prices induced by drought-related domestic supply shortages, liquidity overhangs from pandemic-related fiscal and monetary policy stimulus undertaken in 2020–21, and the pass-through effects of currency depreciation against a strong US dollar propelled

FIGURE 2 Outlook for key macroeconomic indicators, average, 2024–25

Country	Real GDP growth	Inflation	Current account balance	Fiscal balance
Algeria	3.8	6.2	0.4	–11.5
Angola	3.5	15.3	4.3	–1.3
Benin	6.3	2.3	–4.3	–3.5
Botswana	4.2	4.3	1.2	–1.0
Burkina Faso	4.2	2.2	–6.0	–5.7
Burundi	5.2	17.3	–6.5	–4.1
Cabo Verde	4.8	2.1	–6.5	–2.7
Cameroon	4.2	5.3	–1.8	–0.3
Central African Rep.	2.7	3.7	–9.5	–2.4
Chad	5.2	3.3	1.1	2.5
Comoros	4.3	2.5	–5.6	–3.2
Congo, Dem. Rep.	5.7	13.5	–4.1	–1.6
Congo, Rep.	4.3	3.3	2.8	3.3
Côte d'Ivoire	7.0	3.2	–6.5	–3.6
Djibouti	6.4	1.9	19.8	0.1
Egypt	3.9	29.2	–3.1	–6.8
Equatorial Guinea	–1.2	3.6	–4.3	–0.5
Eritrea	3.0	4.0	12.7	0.7
eSwatini	4.2	5.0	3.4	–1.9
Ethiopia	6.7	18.4	–1.6	–2.6
Gabon	2.8	2.4	–0.2	–0.9
Gambia, The	6.0	13.5	–6.6	–2.8
Ghana	3.8	16.0	–2.1	–4.6
Guinea	4.8	10.6	–10.0	–2.5
Guinea-Bissau	5.0	4.3	–4.3	–3.4
Kenya	5.5	5.8	–4.6	–5.4

Country	Real GDP growth	Inflation	Current account balance	Fiscal balance
Lesotho	1.9	5.2	–4.8	–1.9
Liberia	5.7	7.0	–24.2	–3.0
Libya	7.0	2.7	23.4	6.5
Madagascar	4.9	7.8	–4.2	–4.4
Malawi	3.5	20.8	–8.9	–8.2
Mali	5.0	1.9	–6.2	–3.8
Mauritania	4.8	4.5	–8.0	–1.8
Mauritius	4.3	5.4	–4.3	–4.4
Morocco	3.6	3.9	–0.7	–4.3
Mozambique	5.2	4.8	–40.6	–2.4
Namibia	2.9	4.5	–9.0	–4.1
Niger	9.1	3.3	–8.3	–3.7
Nigeria	3.3	26.2	3.3	–4.2
Rwanda	6.7	6.1	–10.8	–6.1
São Tomé and Príncipe	1.6	11.6	–10.2	–3.1
Senegal	9.8	4.1	–9.6	–3.6
Seychelles	4.1	1.8	–7.2	–1.4
Sierra Leone	5.0	26.9	–3.2	–2.6
Somalia	3.8	4.6	–10.3	–0.9
South Africa	1.5	4.6	–3.0	–4.3
South Sudan	–2.0	17.8	–5.5	–4.0
Sudan	–2.7	121.7	–5.9	–4.5
Tanzania	5.8	3.4	–4.1	–2.5
Togo	5.6	2.4	–3.1	–5.3
Tunisia	2.5	6.9	–3.7	–6.2
Uganda	6.5	4.7	–8.5	–3.9
Zambia	4.5	8.2	5.8	–4.3
Zimbabwe	2.8	21.2	0.5	–1.6

Note: GDP growth and inflation are in percentage, while current account balance and fiscal balance are in percent of GDP. This heatmap plots the countries' outlook for selected key macroeconomic indicators. Countries are ranked in three criteria: "green" for good performers, "yellow" for fair performers and "red" for weak performers. Real GDP growth above 6 percent is colored green, 4–6 percent is colored yellow and below 4 percent is colored red. Inflation rates below 5 percent is colored green, 5–9.9 percent is colored yellow and double digit is colored red. Current account surplus is colored green, deficits below 5 percent is colored yellow and above 5 percent is colored red. Fiscal deficits below 3 percent is colored green, 3–5 percent is colored yellow and above 5 percent is colored red.
Source: AfDB staff calculations.

by high interest rates in the United States. Across regions, the inflation picture is mixed. **East Africa** has the highest inflation at 26.5 percent in 2023, with Sudan leading the way at 245.3 percent. **West Africa** has the second highest at 20.3 percent, with Sierra Leone and Ghana topping the list. **North Africa** experienced the highest inflation increase of 8.1 percentage points to an average 16.3 percent in 2023, driven by rising prices in Egypt and geopolitical tensions. **Central Africa's** inflation also rose 3.5 percentage points to 10.3 percent in 2023, with the Democratic Republic of Congo experiencing a 10.6 percentage point rise. Only in **Southern Africa** has the inflation rate fallen, from 10.8 percent in 2022, reaching single digit of 8.6 percent in 2023, driven by declines in Angola, Botswana, South Africa, and Zimbabwe.

Higher inflation across Africa has eroded any socioeconomic gains made before the COVID-19 outbreak. The outlook for Africa's inflation remains unfavorable, with the average rate expected to rise from an estimated 17 percent in 2023 to 17.8 percent in 2024 before cooling down to 12.3 percent in 2025. The projected increase in 2024 reflects sustained high food prices and widening imbalances between supply and demand in domestic and global food markets, as well as high energy prices, mainly affecting net oil countries. The structural nature of the current wave of high inflation has undermined the effectiveness of conventional monetary policy tools such as increases in policy rates and require a different approach to stem the tide.

The depreciation of African currencies persisted in 2023, albeit to a lesser extent than in 2022. Under pressure from sustained high global interest rates and continued global uncertainty fueled by geopolitical and trade tensions, most African currencies depreciated further against the stronger US dollar in 2023. For instance, Nigeria's naira depreciated by 95.6 percent in 2023. This depreciation largely reflected market correction following reforms undertaken in the foreign exchange market in June 2023, which led to the floating of the naira. The second biggest losses were for the Angolan kwanza (32.8 percent) and the Zambian kwacha (15.4 percent). Both countries have experienced limited foreign currency liquidity on the market, and in Angola the situation was exacerbated by lower oil prices and the end of the moratorium by Chinese creditors. The depreciation in Zambia was further compounded by weak market sentiment due to protracted debt restructuring. However, due to their total or partial peg to the euro, which regained some strength against the dollar in 2023, certain currencies such as the CFA franc, the Moroccan dirham, the Cabo Verdean escudo, the São Tomé E Príncipe dobra, and the Comorian franc pared their earlier losses and gained slightly against the US dollar in 2023.

Fiscal deficits are expected to slightly widen before reaching prepandemic levels, but uncertainties remain high. Four years since the outbreak of COVID-19, fiscal positions are slowly returning to the prepandmic levels as countries rein in spending and institute measures to mobilize domestic revenues. Updated estimates show that the average fiscal deficit on the continent increased slightly from 4.9 percent of GDP in 2022 to 5 percent in 2023, mainly due to marginal widening of the primary balance from 1.6 percent of GDP in 2022 to 2.1 percent of GDP in 2023. The deterioration in the primary deficit is mainly due to measures implemented to mitigate the effects of rising food prices amid falling energy sector revenues. The fiscal deficit across the continent is projected to narrow in 2024 to 4.7 percent of GDP and further to 4.3 percent of GDP in 2025 after the slight increase to 5 percent of GDP in 2023.

Four years since the outbreak of COVID-19, fiscal positions are slowly returning to the prepandmic levels as countries rein in spending and institute measures to mobilize domestic revenues

The average current account deficit is projected to widen from an estimated 1.7 percent of GDP in 2023 to 2 percent of GDP in 2024 and 2025. The projected widening reflects expectations that oil prices will remain relatively elevated and stabilize at around $77 per barrel, with net oil-importing economies severely affected. However, these projections—respective improvements of 0.2 percentage points and 0.1 percentage point over the January 2024 forecasts for 2024 and 2025—reflect the rebound in global trade and the boost to China's commodity imports as its construction sector stabilizes and resilience in domestic economy is aided by recovering investments and firm consumer spending.

External financial flows to Africa have suffered from tightening global financial conditions and high uncertainty. External financial flows to Africa—foreign direct investment (FDI), official development assistance (ODA), portfolio investment and remittances—fell by 19.4 percent in 2022 to $174.9 billion, or 5.9 percent of Africa's GDP, from $217.1 billion in 2021. This decline, reversing a strong immediate postpandemic recovery was broad-based. Foreign direct investment fell by about 44 percent, and the continent recorded net portfolio outflows of 17 percent and a reduction in ODA inflows of about 6 percent.

Only remittances recorded a marginal increase of 0.2 percent.

Public debt is declining but still above pre-pandemic levels, highlighting the severity of the debt burden on the continent. Africa's median public debt ratio, which rose from 54.5 percent of GDP in 2019 to 64 percent in 2020, stabilized at around 63.5 percent from 2021–23 and is expected to decline further to around 60 percent from 2024—halting a decade long upward trend. While debt levels have stabilized across the continent with relative improvements in fiscal positions, the ratio remains high and above prepandemic levels in many countries where public finances have been volatile due to the unprecedented shocks. The debt overhang reflects the burden of Africa's indebtedness in the face of government actions to support pandemic-stricken economies and to cushion households against effects of the high food and energy costs and the higher cost of borrowing induced by effects of Russia's invasion of Ukraine. In addition, external debt service payments as a proportion of government revenues have risen above the prepandemic level in many countries. The median debt service on external debt for 49 countries with available data rose from 6.8 percent of government revenue over 2015–19 to 10.6 percent over 2020–22. Resources channeled to debt service have eroded fiscal space, further constraining governments' capacity to invest in growth-promoting sectors and human capital development—education and health, two areas where average public expenditure on the continent is below that for comparator regions.

Africa's positive economic outlook comes with cautious optimism given the considerable global uncertainty and geopolitical tensions

Africa's positive economic outlook comes, however, with cautious optimism given the considerable global uncertainty and geopolitical tensions.

Main downside risks:

- Persistent inflationary pressures in many African countries could put further pressure on African economies by further lowering real wages and keeping interest rates high for longer. This has implications for private sector activity in countries with higher domestic borrowing costs.
- The protracted gridlock in global trade and investment and attendant effects stoked by rising geopolitical tensions and polarization have upended Africa's growth, and further escalation could jeopardize the continent's economic recovery.
- Higher commodity prices could ignite a new wave of inflation, upend the decline in poverty, and delay the process of monetary policy easing to spur growth on the continent, which in turn could jeopardize the positive economic outlook.
- Increased regional conflicts and political instability in some countries have imposed untold human suffering and large social and economic costs. Left unresolved, these conflicts will exacerbate the already dire humanitarian and socioeconomic situations, with long-term consequences for economic and macroeconomic stability in these economies.
- Climate shocks constitute yet another important downside risk to growth recovery in Africa. Indeed, climate change poses grave threats to countries across Africa—but especially in transition states in the Horn of Africa and across the Sahel region.

Main tailwinds:

- If the positive trend in fiscal consolidation and debt structuring gains further traction and global market conditions improve, African countries could see sovereign interest rates decline, stimulating economic growth as their risk premia fall in tandem.
- Continued structural transformation and renewed capital accumulation could strengthen growth prospects. A virtuous cycle of between- and within-sector productivity growth could lift real wages, opening space for savings mobilization needed to fund long-term capital accumulation of both public and private sectors.
- The return to lower policy rate environment in advanced economies and some emerging markets could lift economic growth. A wave of rate cuts would revive credit growth in both regions, boost consumer sentiment, alleviate pressure on public debt servicing, and reinforce global growth. Africa would directly benefit from rebounding global growth as the two regions combined represent 40 percent of the

world's GDP, 55 percent of the FDI stock in Africa, and about two-thirds of ODA to Africa.

A mix of policies is needed in the short, medium, and long terms to address Africa's macroeconomic challenges and put economies back on the path of sustained, higher growth.

In the short term

- To achieve faster disinflation and anchor inflation expectations at minimal cost to the economy amidst weakening domestic currencies requires tailored monetary policy adjustments. In particular, the monetary policy stance can be more accommodating in economies where core inflation is moderate and headline inflation is driven mostly by temporary supply shocks.
- Addressing exchange rate pressures should be a key short-term policy priority. In countries with floating exchange rates, currencies should therefore be allowed to adjust as much as possible, since trying to resist movements based on fundamentals could have adverse secondary consequences on the economy. In countries with pegged exchange rates, monetary policy must be aligned with that of the anchor country to maintain external stability and avoid further losses in foreign exchange reserves as they intervene to preserve the exchange rate parity.
- Promoting local production and diversifying import sources are key to addressing rising food prices. Supporting African smallholder farmers can trigger an agricultural revolution to feed Africa, especially in urban areas. African countries need to provide farmers with broad access to affordable finance, improved food production technologies (especially certified seeds adapted to extreme climatic conditions), and large-scale systematic extension and mechanization services to increase food production and thus stabilize food prices in the short to medium term.
- Implementing governance reforms and strengthening debt management capacity is key to reducing the burden of public debt—as is the efficient use of borrowed resources. Investing in growth-creating sectors and infrastructure is crucial to unlock the economic potential of African economies.

In the medium to long term

- With elevated public debt choking many countries, scaling up domestic resource mobilization should be a top policy priority for African countries to accelerate structural transformation. Including improving debt management and fighting illicit financial flows, a multidimensional approach is needed to improve the collection and retention of resources generated domestically.
- Reforming the current global financial architecture can accelerate debt restructuring. Key proposals include forming an expanded creditor committee with private lenders to smoothen coordination challenges and establishing a Comparability of Treatment formula to minimize technical disputes.
- Creating an enabling environment is crucial for attracting and scaling up external financial flows as complementary sources of development financing to accelerate Africa's economic transformation. Although domestic resources will remain an integral and larger part of financing Africa's economic transformation, external financial flows will be essential as complementary sources of funding development needs.
- Accelerating structural reforms to build resilient economies. The prolonged growth volatility that Africa has experienced in the aftermath of the COVID-19 pandemic, coupled with the decline in income growth, clearly calls for prioritizing structural reforms to strengthen the continent's resilience to shocks.

A mix of policies is needed in the short, medium, and long terms to address Africa's macroeconomic challenges and put economies back on the path of sustained, higher growth

CHAPTER 2 TAKING STOCK OF AFRICA'S ECONOMIC TRANSFORMATION PROGRESS

African economies have exhibited remarkable resilience amid multiple shocks, but their structural transformation has been slow and uneven. Real aggregate GDP is growing, but so is the continent's population. Thus, while real aggregate GDP grew on average at 3.8 percent annually over the four decades preceding the COVID-19 period, surpassed only by developing Asia, Africa's real GDP per capita has been consistently growing at one of the slowest rates in the world since the 1980s. Moreover, the structure of most African economies has not changed much since the 1990s, such that traditional sectors have continued to drive Africa's growth and employment.

In effect, Africa has been transforming without a marked level of industrialization but through a low-skill services sector, mainly because of low manufacturing activity. The expansion in services employment, which contributed to growth-enhancing structural change, has been matched by a sharp decline in the share of employment in agriculture. This transformation has occurred through the reallocation of economic activities from agriculture to other relatively low-productivity sectors, notably personal and retail services, rather than to more productivity-enhancing manufacturing. But this type of sectoral reallocation has a limited impact on structural transformation. So, despite recent momentum in overall services growth, only 30.1 percent of Africa's services exports in 2022 (20.7 percent in 2005) were in high-skill services, such as insurance, pensions, finance, and information and communication technology (ICT).

Africa has been transforming without a marked level of industrialization but through a low-skill services sector, mainly because of low manufacturing activity

Africa's structural transformation process has also been slow and uneven. Many African countries are still at the early stage of structural transformation, characterized by a widening gap between labor productivity in the agricultural and non-agricultural sectors. The agriculture sector, which employs 42 percent of Africa's workforce, is still 60 percent less productive than the economy-wide productivity level. Conversely, mining, utilities, and financial services, which together employ only about 3 percent of Africa's total workforce, are over 10 times more productive than the average for the economy. Most African workers are therefore stuck in low-productivity sectors and cannot earn enough to escape poverty.

Based on their sectoral employment shares, close to half (25) of African countries can be considered as structurally underdeveloped. In these countries, the agricultural sector absorbed at the median 61.9 percent of total employment in 2021, more than 21 percentage points higher than the median continental value (40.6 percent). In these countries, the median agricultural labor productivity is only 17.5 percent that of nonagricultural sectors, with a median share of agriculture in GDP at about 23.2 percent. Only 12 African countries can be categorized as structurally developed, with industrial workers outnumbering those employed in the agriculture sector.

In addition to manufacturing, services can be an engine of Africa's productivity growth if well harnessed. African countries can leverage the main features of services—smaller size of firms relative to manufacturing ones, high productivity potential regardless of firm size, and smaller role of physical capital relative to manufacturing—to develop a services-led growth model. This model should include the promotion of both nontradable services, which are generally more labor intensive and less capital intensive—and tradable services such as tourism, business, and finance, and ICTs, which could bring in foreign exchange revenues needed to finance transformation. Services already are becoming increasingly important in Africa's international trade: the value of its services trade rose more than fourfold between 2000 and 2022, from $66.4 billion to $269.4 billion.

Institutions matter for structural transformation and countries with well-defined and functioning institutions that invest in productivity-enhancing soft and hard infrastructure have transformed their economies. By being able to reduce transaction costs and information opacity, politically stable and less corrupt countries managed to crowd-in private investments, boost productivity, stimulate growth, and increase real incomes. Countries with good quality public services coupled with policy consistency are also most likely to transform their economies because of the citizenry's buy-in to structural reforms. Consequently, these countries performed relatively well in transforming their economies with more resources efficiently allocated to critical sectors (such as education, energy, transport infrastructure, and ICTs) that have large potential to foster structural transformation. Quality infrastructure—soft and hard—reinforces the transformational benefits of consistent policies and of robust institutions.

Africa will need to close an annual financing gap of about $402 billion by 2030 to fast-track its structural transformation and catch up with high-performing developing countries from other regions. This financing gap presupposes that the continent prioritizes investment needs in education, energy, productivity, and infrastructure, key Sustainable Development Goals (SDGs) more directly relevant in improving structural transformation. Mobilizing additional resources domestically—including by leveraging investment in the continent's huge endowments in natural resources, especially in critical and rare earth minerals—and tax collection coupled with more efficient public spending could help bridge a significant part of this financing gap.

Yet, domestic resources alone will be insufficient in many African countries to fill their financing gap for structural transformation by 2030. Many African countries have limited fiscal space and low tax capacity. And the private sector remains very risk averse and its participation relatively small, especially towards investment in critical sectors for structural transformation. Thus, given the short period before the SDGs deadline, a majority of countries may fail to mobilize domestically the enormous resources required to close their financing gap by 2030. For those countries, scattered across the continent's five regions, a more reasonable target and combination of financing options would be to allow for a gradual but steady structural transformation process over a longer period to ensure the mobilization of both domestic and external resources. Regardless of the targeted deadline, however, the increased participation of the private sector will be crucial to supplement public resources.

Accelerating the pace of Africa's structural transformation will thus require a multipronged and gradual approach that allows countries to mobilize their estimated colossal resources.

Policy recommendations

African countries need to establish, prioritize, and institutionalize endogenous development plans and policies tailored to areas of comparative advantage and implement them consistently, while avoiding policy reversals that tend to disrupt progress. To address their development challenges, there is a need for African countries not to outsource their development plans but to take full ownership by harnessing local knowledge of their economies and sociocultural conditions, as well as other unique areas of comparative advantage, within national, regional, and global contexts. The rate and pace of structural transformation of African countries will largely depend on the quality, relevance, and effectiveness of policies and the continued and institutionalized implementation of development plans and strategies. Therefore, there should be unreserved political commitment to rally citizens towards a nationally agreed development plan and vision, avoiding the recurrent and electoral cycle–induced policy reversals that characterize most African countries. Continuous and systematic implementation of public policies, in particular linking fiscal policies to structural transformation objectives, will create certainty and stability to attract domestic and foreign capital into areas supportive of the structural transformation agenda.

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They need to urgently scale up investments to build requisite human capital suited to local realities, circumstances and development priorities, including adequate skills training to prepare the workforce for the future. Countries need to scale up investments in education at all levels, building and improving the quality and relevance of the technical and soft skills required to drive their development agenda, tailored to local contexts and circumstances. This will require prioritizing systems of learning and curricula that enhance productivity growth in sectors of comparative and competitive advantages. For example, countries need to prioritize scaling up skills in science, technology, engineering, and mathematics (STEM), and those rich in natural resources—minerals and vast arable land—will need to train enough geologists, agronomists, and other related experts to allow them to leverage their resources to drive structural transformation. Furthermore, the domestication of education and skills learning and training systems, including the language of teaching, will be crucial to improve the quality and relevance of the education curriculum and leverage the ongoing fourth industrial revolution, technology, and ICT boom. African countries should thus establish innovation centers of excellence—in collaboration with host universities and technical and vocational training centers. They should develop demand-driven skills training programs to better align education and training systems to labor markets and thus reduce widespread skills mismatch on the continent. And they should strengthen public-private partnerships to make skills acquisition of graduates in tune with labor market needs, which holds promise in supporting Africa's structural transformation.

Countries need to scale up domestic resource mobilization and prioritize prudence in public finance management

Countries need to scale up domestic resource mobilization (DRM) and prioritize prudence in public finance management (PFM). African countries must own their development agenda and have the primary responsibility for financing their structural transformation. To this end, mobilizing more resources, in particular domestically, should be a key priority of each country's development strategy. However, domestic resource mobilization has so far not kept pace with Africa's enormous development financing needs. Revenues collected are often used inefficiently or siphoned off through corruption and other leakages. To accelerate DRM, countries need to consider the following aspects.

First, they need to mobilize more *tax revenues.* The Bank estimates that the median African tax-to-GDP ratio should increase from its current level of about 14.0 percent to a minimum of 27.2 percent to be able to close, by 2030, the estimated annual financing gap of $402.2 billion for structural transformation. To scale up DRM for structural transformation, countries need to invest in systems that improve efficiency in tax administration and public financial management. This will require, for instance, enhancing the digitalization of tax collection and administration systems.

Second, countries could also aim at increasing *nontax revenues* such as property income, royalties, fines, penalties, forfeits, and business permits , which are often neglected or difficult to administer due to complex processes and the widespread informality of economies. PFM systems should incorporate nontax revenue planning into the budgetary process, ensuring that the revenues collected are not only efficiently allocated but also utilized. Strong political commitment will be needed to develop expertise in core departments and fiscal units in charge of collecting such revenues.

Third, African countries will further need to improve *tax compliance* by enhancing the social contract with their citizens. Countries should seek to promote voluntary tax compliance to increase DRM. Enforcement capacities, which are often weak in many countries, and hard-to-tax sectors, such as informal companies, predominate. More importantly, governments should visibly use tax revenues for public welfare by providing quality public goods and services to enhance trust in the utilization of public resources and significantly reduce implicit taxation.

Fourth, enhancing the *formalization of the informal economy* could also boost DRM. The size of the informal sector in Africa significantly limits the tax base and revenue collection. For instance, informal employment in Africa accounts for 85.8 percent of total employment, the largest percentage in the world. To promote formalization, policymakers could take a broader strategic approach that seeks to register informal firms not only to tax them but also to protect their rights, entitlements, and assets as entrepreneurs. The attractiveness of the formal sector can be enhanced, for example, by providing greater access to resources and information, pension schemes, social insurance, or other incentives—conditioned on registration—through intermediaries such as business associations, nongovernmental organizations, or local community groups.

Finally, in addition to improving domestic revenue mobilization, countries need to build capacity in the *prudent and efficient management of public finance* throughout the public financial management cycle, from DRM to strengthening supreme audit and public accountability systems.

Countries need to build and deepen national and regional markets for goods, services, capital, and finance. Developing domestic and regional financial and capital markets will reduce countries' dependence on external markets and minimize vulnerability to global shocks. Developing robust financial markets will require improving property rights regimes, diversifying the supply of financial products and services in the banking sector, and regionalizing financial markets through legal harmonization and cross-listing of assets at the regional level. Capital market development will require creating an enabling policy and regulatory environment to mobilize at scale and channel resources held by pension funds and insurance and collective investment schemes for financing structural transformation. In that regard, the AfCFTA can be a game changer if fully implemented and domesticated by all African countries. It will create a single continental market for goods and services, with free movement of capital, talent, and skills. Implementing policies that enable free mobility of labor and services—such as the open visa entry for Africans being championed by Kenya and Rwanda—would facilitate the operation of the AfCFTA.

The creation of preferred procurement solutions, through the AfCFTA, will ensure that countries leverage the continent's abundant natural resources, add value to them, and expand productive capacity and services growth. The launch in 2022 of the Pan-African Payment and Settlement System (PASS) by the African Union and the African Export-Import Bank to complement trading under the AfCFTA is therefore a move in the right direction, as it will help address currency risks between trading partners. The PASS simplifies the historical complexities and costs of making payments in local currencies across African borders, providing operational efficiencies that open vast economic opportunities for all stakeholders.

Countries could further proactively pursue and promote a policy of franchising and leveraging the technological know-how of foreign firms, or promote cross-border investment among African countries, to complement local content policies and requirements, especially where capacity—technical and financial—is lacking.

Policy priority should be given to the creation of targeted and streamlined incentives to catalyze private capital flows to support countries' endogenous development plans in key sectors for structural transformation. Incentivizing the private sector could support countries' structural transformation efforts. By making the conditions right for the private sector, creating a conducive business environment, and providing carefully crafted and targeted fiscal incentives, African countries could stimulate the private sector—domestic and external—to invest more in critical sectors. The use of innovative financing instruments such as blended finance could increase private participation in infrastructure for green growth by derricking the sector. The development of sustainable finance instruments (including green bonds and loans and sustainability bonds and loans), as well as carbon markets, could boost private sector investment in green sectors.

In addition, remittances—the largest and most stable source of external funding in Africa—are an important source of external financing. Their function in promoting investment for Africa's transformation can be enhanced through, for instance, diaspora bonds and diaspora "remittance securitization."

Policy priority should be given to the creation of targeted and streamlined incentives to catalyze private capital flows to support countries' endogenous development plans in key sectors for structural transformation

Countries need to invest in natural capital accounting beneficiation and conservation and include it in the system of national accounts to expand the size of the economy. Much of Africa's natural capital resources remain largely unexploited, and the values or services they provide are typically poorly measured—and sometimes completely unmeasured—as part of African countries' wealth. As a result, the value of African economies continues to be underestimated amidst the abundance of green wealth. Investing in, measuring, and valuing natural capital and integrating them into systems of national account will help estimate the true value of Africa's green wealth,[1] expand its GDP, and improve conservation. The Bank, in collaboration with many African countries, has been advocating for proper valuation of the green wealth of the continent and the incorporation of services they offer in GDP. Indeed, Africa's natural resources provide essential environmental services such as carbon sequestration, pollution control, and retention of soil fertility, which sustain human existence. The inclusion of such critical environmental services in the valuation of country GDP—the green GDP—could encourage green transition in countries.

By investing in youth entrepreneurship development programs, African countries can harness the continent's demographic dividend. Young people are Africa's greatest asset, which, if well harnessed, could speed up structural transformation. By 2030, one in four young people in the world will be African, and, if well nurtured, this young population can drive the continent's future economic growth and its structural transformation. However, reaping the benefits of the demographic dividend from African youth would significantly depend on investment in human capital development and on creating economic and job opportunities for young people. Of people ages 15–35 not in school, one-third are unemployed and discouraged, another third are vulnerably employed, and only one in six is in wage employment. The Bank estimates that 17 million jobs need to be created every month between now and 2063 to keep the participation and unemployment rates of African youth constant. Supporting young people to create their own businesses holds promise in leveraging the continent's demographic dividend and addressing widespread youth unemployment and underemployment. That is why, under its Jobs for Youth in Africa Strategy and its Youth Entrepreneurship and Innovation Multi-Donor Trust Fund, the Bank is supporting African countries in establishing Youth Entrepreneurship Investment Banks as a model to address market failures and fragmentation in the provision of tailored financing and non-financing services to young entrepreneurs in Africa

By 2030, one in four young people in the world will be African, and, if well nurtured, this young population can drive the continent's future economic growth and its structural transformation

It is also critical that countries launch ambitious national infrastructure programs for broad-based policy implementation to accelerate structural transformation. While in the long term all types of infrastructure are important, in the short term countries need to prioritize which infrastructure to build depending on their geographic situation and level of development and concentrate limited resources on creating "islands of excellence" with dense and sector-specific infrastructure to boost productive capacities and competitiveness. Priority could be given to the energy sector, which is most likely to achieve a high social rate of return, and to the transport sector, which is especially important for landlocked countries in creating linkages to coastal countries with seaports. Given the significant transformational impact of digitalization, investing in the ICT sector will close the existing digital divide between African countries and the rest of the world. An ambitious national digitalization program in Africa will further increase economy-wide competitiveness, enhance efficiency and transparency of policy implementation, improve DRM, and curb illicit capital flows, as well as address widespread market inefficiencies, facilitate proper measurement and valuation of natural capital, and support the competitiveness of youth-led businesses.

By taking proactive actions to harness the governance of macroeconomic policies and the business environment, countries will be able to improve risk profiling and perceptions and harness the innovative global capital and financial instruments needed to build capacity in project preparation and implementation. The lack of investment-ready project pipelines is often cited as among the most important impediments not only to unlocking private finance but also to leveraging existing innovative finance instruments. Large infrastructure projects have extensive development and gestation periods and often entail multifaceted feasibility studies and expert transaction advice. Many African governments and local private sector players lack the capabilities, as well as the resources, to design and implement infrastructure projects with commercial potential. In addition, short political cycles may constrain private sector financing commitments to long-term infrastructure projects. Many investors therefore lack bankable project pipelines, as only a few projects meet financiers' risk return expectations, and so fail to reach financial closure. Building capacity in project preparation and implementation is therefore crucial. Building such capacity would require, for instance, that private financiers not only provide resources but also participate in building bankable projects. The participation of financiers across the entire project cycle from concept to bankability and financing (that is, from the development of strong feasibility studies to the analysis of market prospects and the establishment of viable business plans) will ensure that they have a stake in and ownership of proposed projects, which will increase the probability of the project receiving financing and succeeding when it becomes operational. Moreover, enhancing the governance of the macroeconomic and investment climate will be key to improving the risk profiles of African countries and changing external perceptions about African markets.

CHAPTER 3 FINANCING STRUCTURAL TRANSFORMATION IN AFRICA: REFORMING THE GLOBAL FINANCIAL ARCHITECTURE

Over the past decades, multilateral financial institutions have collectively and individually been vital for financing development. They have supported countries during major global economic challenges, such as the Latin American Debt Crisis of the early 1980s, the African Debt Crisis of the 1980s and 1990s, the Asian Financial Crisis of the late 1990s, the Global Financial Crisis of 2007–09, and the recent COVID-19 pandemic in 2020–21, to name a few. They have also supported economic recovery efforts in Africa and other developing regions by spearheading global response actions in times of crisis. Recent examples include the Debt Service Suspension Initiative, the G20's Common Framework for debt resolution, and the IMF's general allocation of the equivalent of $650 billion in Special Drawing Rights (SDRs) to ease the fiscal and balance-of-payment challenges that several developing countries faced during the pandemic.

While the global financial architecture (GFA) has served a great deal over past decades, it has also failed to deliver resources at scale to meet Africa's financing need for structural transformation. Indeed, the current global financial architecture and system of multilateralism is not delivering enough resources in a timely manner and scale to meet national and global development goals in Africa, including the SDGs and the African Union's Agenda 2063. Neither the public nor private sector as currently constituted has been able to channel enough resources to address the development financing needs of Africa. The current system also makes access to development finance very expensive and cumbersome for African countries. The high cost of sovereign borrowing by these countries relative to their peers in other regions of the world often leads to debt vulnerabilities. The structure and scale of the current global climate finance architecture mirror the current GFA, making it difficult for the most vulnerable African countries to harness climate resilience opportunities. This climate finance architecture is complicated and loosely defined, misaligned with climate vulnerabilities and climate risks, and has been unable to channel enough resources to implement African countries' Nationally Determined Contributions.

While the global financial architecture has served a great deal over past decades, it has also failed to deliver resources at scale to meet Africa's financing need for structural transformation

Another limitation of the global financial architecture is reflected in Africa's sovereigns facing higher costs of financing in international capital markets than advanced and emerging economies, given perceptions of risk by international investors originating from subjective credit ratings. In 2021, African sovereign eurobonds were issued with yields above 5 percent and, in 40 percent of the cases, yields exceeded 8 percent. In contrast, the average sovereign bond yield for advanced economies was 1.1 percent, and for emerging market economies, 4.9 percent. It has been estimated that African countries are paying 500 percent more in interest costs when borrowing in international capital markets than when borrowing from the World Bank or other multilateral development banks such as the African Development Bank.

These weaknesses of the global financial architecture have amplified calls on the necessity for reforms of institutional governance in the

multilateral institutions to make the instruments of global financial governance more nimble, inclusive, and responsive. To meet the scale and scope of global challenges, global financial institutions need to scale up development financing from billions to trillions of dollars. Achieving the required scale of financing will entail close collaboration between the public and private sectors across all levels—global, regional, and national—as well as the development of innovative financing mechanisms to leverage resources from all sources. The World Bank, IMF, and regional development banks need to work more collaboratively and deploy their risk capital more innovatively to leverage private capital at scale. There is also an urgent need to reform the GFA to make it nimbler and fit for orderly debt restructuring.

Recycling Special Drawing Rights through multilateral development banks (MDBs), implementing the MDB capital adequacy reforms, and reforming credit rating methods could increase financing for Africa's structural transformation and drive the continent to a higher level of economic development

This need for reform is most evident in Africa, where the population still living in extreme poverty is estimated at about 34 percent, debt vulnerabilities are increasing, the benefits of international trade remain below expectations, and the impacts of climate change, to which the continent has not contributed, are costing it 5–15 percent of GDP per capita growth annually. Further, debt resolution in Africa, especially outside Paris Club processes, has been disorderly and protracted, with costly economic consequences.

Given their membership structures, the multilateral development banks, and financial institutions—the World Bank, IMF, AfDB, and other regional development banks—are best placed to lead global and regional efforts to mobilize and allocate resources at scale toward achievement of the SDGs in developing countries and to addressing global commons challenges. But their governance structures (shareholding models and weighted voting systems) and the resources available to them often affect the speed and scale of financial flows to countries that need funding the most, as was evident during COVID-19 responses. Access to emergency financing was largely skewed toward developed economies that needed it least. For example, of the $650 billion in SDRs issued by the IMF in 2021 to help countries navigate the adverse effects of the pandemic, Africa received $33 billion, or 4.5 percent, of the total available envelope. In addition, of the $17 trillion (or 19 percent of global GDP) rolled out as fiscal measures to fight the pandemic in 2020–21, Africa's share was only $89.5 billion (0.5 percent). And the same trends are observed in the scale and flows of the global climate finance architecture, which is misaligned with, for example, climate vulnerability and voluntary carbon market development.

Measures are needed to strengthen global, regional, and national institutions, as are subsidiarity agreements between global and regional institutions, to increase responsiveness to increasingly complex development challenges in Africa and elsewhere in the developing world. Multilateralism, including development finance institutions, has over the decades transformed into multilayered forms of governance. Profound changes are symbolized by the growing role of regional development banks such as the AfDB, Asian Development Bank, Islamic Development Bank, Latin America Development Bank, and the Inter-American Development Bank. Most countries are members of these regional organizations, with some overlapping memberships. These banks can enhance multilateral efficiency by sharing burdens, building capacity, exchanging information and best practices, and increasing legitimacy through positive policy outcomes.

Implementation of specific reforms regarding recycling SDRs through MDBs, implementing the MDB capital adequacy reforms, and reforming credit rating methods could increase financing for Africa's structural transformation and drive the continent to a higher level of economic development. Rechanneling SDRs through the MDBs could increase financing for Africa by about $46.2 billion a year over the next 10 years if the recommendations of the Bridgetown Initiative—to rechannel $100 billion to the MDBs—is implemented. Reforms of the MDB Capital Adequacy Framework proposed by the G20 could increase financing for Africa by another $5.2 billion a year. In addition, Africa could save up to $44 billion in accumulated debt arrears if the IMF's lending into arrears policy is fully implemented. Africa could also save up to $74 billion a year in interest payments if the global credit ratings system were fairer and based on fundamentals. Collectively, these initiatives could secure $169.4 billion a year in development financing, or about 42 percent of the estimated annual financing gap of $402.2 billion, to fast-track Africa's structural transformation.

Implementing the following GFA reforms could unlock substantial capital for structural transformation in Africa, but they should not be considered a panacea. The continent needs to also capitalize on domestic resources, including leveraging its abundant natural and human capital, improving the collection of tax and nontax revenues, enhancing public spending efficiency, and fighting illicit financial flows and tax evasion and avoidance, which drain significant resources outside the continent.

Policy recommendations

Given the scale of the resources needed to accelerate structural transformation in Africa and the identified weaknesses of the global financial architecture, the following policy recommendations emerge:

Accelerate the scale of low-cost concessional financing for Africa's development, through:

- Rechannelling the IMF SDRs to MDBs to leverage more resources for structural transformation in Africa.
- Making a healthy replenishment of the concessional windows of the African Development Bank and the World Bank—the ADF and IDA, respectively.
- Reforming global tax governance to make it more transparent and accountable.
- Maximizing MDBs' funding capacity through the implementation of the G20's Capital Adequacy Framework and the Triple Agenda.
- Improving the scale and transparency of bilateral and private creditors.

Reform the global debt architecture to make it more transparent, nimble, accessible, and affordable to developing countries, through:

- Accelerating debt restructuring and updating the current Debt Sustainability Framework (DSF) to reflect the changing structure of economies and the impact of shocks on economies, especially those in Africa.
- Making the IMF–World Bank DSF methodology for assessing debt sustainability publicly available to make it easy to replicate and independently validate the findings.
- MDBs like the AfDB working with international credit rating agencies to strengthen methodologies for assessing sovereign risk and to help reduce the information gap in assessing the credit ratings of Africa's sovereigns.
- Strengthening climate finance accessibility for vulnerable countries that need it most
- Simplifying procedures of the climate finance architecture to make it more accessible to climate-vulnerable countries, who also have limited capacity to fulfill complicated and expensive project preparation procedures.
- Scaling up the Loss and Damage Fund, announced at COP27 in Egypt, to match the fiscal impacts of physical climate effects in countries.
- Discouraging the use of debt instruments as climate finance, which often increases the debt vulnerability of climate-vulnerable countries.

Adopt reforms to improve Africa's access to emergency financing facilities. Three actions could be envisioned:

- Delink access to IMF financing from quotas.
- Introduce state contingent clauses in loan agreements with the IFIs.
- Create an African emergency finance facility/financial stability mechanism or institution.

Make the governance of the GFA more inclusive to enhance Africa's participation and voice:

- Governance of the international financial system provides little voice to countries of the Global South, and particularly to Africa.
- Increasing Africa's voice in global financial institutions will increase its ownership of decisions taken in these organizations, in line with its growing importance on the global stage.
- The addition of the African Union as a full member in the G20 is a welcome initiative, but the African continent remains underrepresented, with South Africa as the only sovereign member of the group.

Global financial architecture reforms could unlock substantial capital for structural transformation in Africa, but they should not be considered a panacea

- Admitting more African countries as sovereign members is recommended.
- For the longer term, African countries need to implement growth-enhancing policies that will increase the size of their economies and amplify the continent's voice in the GFA.

Implement a mandatory requirement for countries to adopt policies for greening the wealth of nations.

- Despite playing a minimal role in global greenhouse gas emissions, Africa's natural assets, like the Congo Basin rainforest, act as critical carbon sinks, contributing significantly to climate change mitigation efforts.
- While these natural assets deliver significant global public goods, such as carbon sequestration, biodiversity conservation, and other ecosystem services, the value of these positive externalities are not fully factored in the measurement of the wealth of countries.
- Properly valuing this natural capital and accounting for it in national systems of accounts can foster sustainable development and green transitions.
- African countries can leverage their green wealth to improve their credit ratings and unlock resources, such as carbon credits, to invest in green transitions and sustainable development goals.

Leverage private sector financing for transformation and climate justice.

- The scale of public resources that can be mobilized through scaling up domestic revenue mobilization and concessional financing from official multilateral and bilateral creditors in the near term will be very modest relative to the scale of resources required to support Africa's structural transformation to meet the SDGs and Agenda 2063, even in the best-case scenarios.
- The private sector offers significant opportunities to fill the resource gap. Measures to incentivize private finance for climate and green growth in Africa are therefore critical for structural transformation in Africa.
- Reforms of the GFA could support asset recycling by transferring the existing assets of debt-distressed countries to the private sector to generate funding for infrastructure and other catalytic projects to accelerate structural transformation.
- Reforms could also embed mechanisms for a portfolio-based approach toward private sector investment, rather than a project-by-project approach, to leverage economies of scale and existing synergies of projects within the same portfolio more than projects managed in silos can achieve.

NOTE

1. As used in this context, *green wealth* is a term denoting the unmeasured value of Africa's natural capital", as espoused by Dr. Adesina, President of the African Development Bank Group. See https://www.afdb.org/en/news-and-events/speeches/keynote-speech-dr-akinwumi-adesina-president-african-development-bank-group-40th-anniversary-guardian-newspapers-lagos-nigeria-28-november-2023-66327.

1

AFRICA'S ECONOMIC PERFORMANCE AND OUTLOOK

KEY MESSAGES

Average real gross domestic product (GDP) growth is estimated to have slowed from 4.1 percent in 2022 to 3.1 percent in 2023. The decline is attributed to a variety of factors, including persistently high food and energy prices on the back of sustained impacts of Russia's invasion of Ukraine,[1] weak global demand weighing down export performance, climate change and extreme weather events on agricultural productivity and power generation, and pockets of political instability and conflict in some African countries.

Despite the continuing headwinds, more than half of African countries (31) had higher real GDP growth rates in 2023 than in 2022, with six (6) of them—Burkina Faso, Djibouti, eSwatini, Libya, the Republic of Congo, and South Sudan—showing a difference in growth rates of more than 2 percentage points. In Libya, the country that recorded the highest increase of 16.3 percentage points in 2023, growth was boosted by continued oil production as the security situation improved. Crucially, fifteen (15) countries recorded growth in real GDP of at least 5 percent in 2023.

Real GDP growth is projected to rise to 3.7 percent in 2024 and will exceed the rate posted in 2022 by 2025, reaching 4.3 percent as most of the effects of the aforementioned factors fade. The projected rebound in Africa's average growth will be led by East Africa (up by 3.4 percentage points) and Southern Africa and West Africa (each rising by 0.6 percentage points). Importantly, 40 countries will post higher growth in 2024 relative to 2023, and the number of countries with more than 5 percent growth rate will increase to seventeen (17). This is remarkable, and as the pace of growth accelerates, African will retain its position as the second-fastest growing region after developing Asia, with a projected average real GDP growth higher than the global average of 3.2 percent in 2024. Furthermore, ten (10) countries in Africa will be among the world's top 20 fastest-growing economies in 2024, sustaining the trend of the past two decades.

The growth outlook is mixed across Africa's five regions:

- **East Africa** is expected to maintain its position as Africa's fastest growing region, with real GDP growth rising from an estimated 1.5 percent in 2023 to 4.9 percent in 2024 and 5.7 percent in 2025. The downward revision of 0.2 percentage points for 2024 from the forecast in the January 2024 Africa's Macroeconomic Performance and Outlook (MEO) is due to larger-than-expected contractions in Sudan and South Sudan.
- Growth in **Central Africa** is expected to moderate from 4.3 percent in 2023 to 4.1 percent in 2024 before improving strongly to 4.7 percent in 2025. The upgraded forecast of 0.6 percentage point for 2024 over the January 2024 projections is attributable to stronger-than-expected growth in Chad and the Democratic Republic of Congo.
- Growth is projected to pick up in **West Africa**, rising from an estimated 3.6 percent in 2023 to 4.2 percent in 2024 and consolidating at 4.4 percent the following year. This is an

upgrade of 0.3 percentage points for 2024 over the January MEO 2024 projections, reflecting stronger growth upgrades in the region's large economies—Côte d'Ivoire, Ghana, Nigeria, and Senegal.

- In **North Africa**, growth is projected to decline from an estimated 4.1 percent in 2023 to 3.6 percent in 2024 and 4.2 percent in 2025, with a downward revision of 0.3 percentage point for 2024 from the January 2024 MEO. Except for Libya and Mauritania, growth has been revised downward for all other countries in the region.
- After a growth slowdown in 2023, growth in **Southern Africa** is projected to pick up slightly from an estimated 1.6 percent in 2023 to 2.2 percent in 2024 and firm up to 2.7 percent in 2025. The growth rates for 2024 and 2025 show an upgrade of 0.1 percentage point over the January 2024 projections, mainly reflecting a 0.7 percentage point increase in South Africa's projected growth. Due to South Africa's larger weight in the region, the upgraded growth forecast offset the combined effect of downward revisions in Angola, Botswana, Lesotho, Zambia, and Zimbabwe.

As the pace of growth accelerates, African will retain its position as the second-fastest growing region after developing Asia, with a projected average real GDP growth of 3.7 percent in 2024, higher than the global average of 3.2 percent

Growth outlook also varies according to economic groupings, reflecting differences in degree of exposure to underlying economic uncertainties:

- For **non-resource–intensive economies**, growth is projected to improve from an estimated 4.8 percent in 2023 to 5.3 percent in 2024 and 5.6 percent in 2025. This growth is underpinned by increased public investments in major growth sectors and substantial capital outlays on critical public infrastructure including electricity, transport, and logistics.
- The average growth rate for **tourism-dependent economies** is projected to decelerate from 5.8 percent in 2023 to 4.7 percent in 2024 and further to 3.9 percent in 2025. This deceleration reflects the stabilization of tourism numbers to trend levels, with projected slower economic growth in Mauritius and Seychelles as the key driver for the group.
- Average growth in **oil-exporting countries** is expected to decline from an estimated 3.7 percent in 2023 to 3.5 percent in 2024 but could pick up the pace to 4 percent in 2025. The projected slowdown in 2024 reflects lower oil production targets set by OPEC, lower growth projections in South Sudan following stoppages faced by the main pipeline transporting its crude oil exports through Sudan, and uncertainty over new mechanisms for Angola's oil exports following its exit from OPEC.
- Growth in **other (non-oil) resource-intensive economies** on the continent is estimated to improve strongly from 0.3 percent in 2023 to 2.7 percent in 2024 and consolidate at 3.3 percent projected for 2025. The sharp increase in growth will be driven largely by the rebound in China's demand for metals and minerals linked to expansions in smart grids and construction.

The dynamics of Africa's macroeconomic fundamentals have remained mixed amid considerable challenges. Average consumer price inflation in Africa is estimated to have increased by 3 percentage points to 17 percent in 2023, from 14 percent in 2022. The increase reflects a combination of higher local food prices induced by drought-related domestic supply shortages, liquidity overhangs from pandemic-induced fiscal and monetary policy support, and the pass-through effects of currency depreciation against a strong US dollar propelled by high interest rates in the United States. Across regions, the inflation picture is mixed. East Africa had the highest inflation at 26.5 percent in 2023, with Sudan leading the way at 245.3 percent. West Africa had the second highest at 20.3 percent, with Sierra Leone (46.6 percent), Ghana (40.3 percent), and Nigeria (24.5 percent) topping the list. North Africa experienced the highest inflation increase, driven by rising prices in Egypt and spillover effects of geopolitical tensions in the Middle East. Central Africa's inflation also rose, with the Democratic Republic of Congo experiencing a 10.3 percentage point increase to 19.9 percent in 2023. Higher inflation across Africa has eroded the socioeconomic gains before the COVID-19 outbreak.

Fiscal deficits are expected to slightly widen before reaching prepandemic levels, but uncertainties remain high. Average fiscal deficits on the continent increased marginally to 5 percent of GDP in 2023 from 4.9 percent in 2022, reflecting slight widening of the primary balance from 1.6 percent of GDP in 2022 to 2.1 percent of GDP in 2023 as countries continue to implement measures to mitigate the effects of rising food prices amid falling energy sector revenues. Oil-exporting countries are expected to see a budget deficit increase in 2024, while other groups should experience a gradual reduction.

The average current account deficit is projected to widen from an estimated 1.7 percent of GDP in 2023 to 2.0 percent of GDP in 2024 and 2025, respectively. The projected widening in the average current account deficit reflects expectations that oil prices will remain relatively elevated and stabilize at around $77 per barrel, with net oil-importing economies severely affected. However, these projections—respective improvements of 0.2 percentage points and 0.1 percentage point over the January 2024 forecast for 2024 and 2025—reflect the rebound in global trade and the boost to China's commodity imports as its construction sector stabilizes and resilience in its domestic economy is aided by recovering investments and firm consumer spending, which could benefit Africa's commodity exporters.

The depreciation of African currencies persisted in 2023, albeit to a lesser extent than in 2022. Under pressure from sustained high global interest rates and continued global uncertainty fueled by geopolitical and trade tensions, most African currencies depreciated further against a stronger US dollar in 2023. For instance, Nigeria's exchange rates depreciated by 95.6 percent in 2023. This depreciation largely reflected a correction following reforms in the foreign exchange market in June 2023, which led to the floating of the Naira. Other countries with large currency depreciation rates included Angola, Malawi and Zambia. These countries have experienced limited foreign currency liquidity on the market, and in Angola, the situation was exacerbated by lower oil prices and the end of the moratorium by Chinese creditors. The depreciation in Zambia was further compounded by weak market sentiment due to protracted debt restructuring process. However, due to their total or partial peg to the euro, which regained some strength against the dollar in 2023, the CFA franc, the Moroccan dirham, the Cabo Verdean escudo, the São Tomé and Príncipe dobra, and the Comorian franc pared their earlier losses and gained slightly against the US dollar in 2023.

Public debt is declining but still above pre-pandemic levels, highlighting the persistence of the debt burden on the continent. Africa's median public debt ratio, which rose from 54.5 percent of GDP in 2019 to 64 percent in 2020, stabilized at around 63.5 from 2021–23 and is expected to decline further to around 60 from 2024—halting a decade long upward trend. While debt levels have stabilized across the continent with relative improvement in fiscal positions, the ratio remains high and above prepandemic levels in many countries where public finances have been volatile due to the unprecedented shocks. The debt overhang reflects the burden of Africa's indebtedness in the face of government actions to support pandemic-stricken economies and to cushion households against high food and energy costs and the higher cost of borrowing induced by Russia's invasion of Ukraine.

The main downside risks to the outlook include the following:

- Persistent inflationary pressures in many African countries could put further pressure on African economies by further lowering real wages and keeping interest rates high.
- The protracted gridlock in trade and investment and attendant effects stoked by rising geopolitical tensions and polarization have upended Africa's growth, and further escalation could jeopardize the continent's economic recovery.
- Higher commodity prices could ignite a new wave of inflation, upend the decline in poverty, and delay the process of monetary policy easing on the continent, which in turn could jeopardize the positive economic outlook.
- Increased regional conflicts and political instability in some countries have imposed untold human suffering and large social and economic costs. Left unresolved, these conflicts will exacerbate the already dire humanitarian and socioeconomic situations, with long-term consequences for economic and macroeconomic stability in these economies.
- Climate shocks constitute yet another important downside risk to growth recovery in Africa. Indeed, climate change poses grave threats to countries across Africa—but especially transition states.

Potential upside risks include, inter alia:

- Further traction of the recent positive trend in fiscal consolidation and progress in debt structuring, improved global market conditions, and

Under pressure from sustained high global interest rates and continued global uncertainty fueled by geopolitical and trade tensions, most African currencies depreciated further against a stronger US dollar in 2023

a decline in risk premia for African countries' debt. Combined, these factors could stimulate investors' confidence, thereby stimulating economic growth.

- Renewed investment and capital accumulation to further boost the pace of structural transformation could strengthen growth prospects.
- The return to a lower policy rate environment in advanced economies and some emerging markets could ease the cost of capital and limit capital outflows and other macroeconomic shocks in Africa, with attendant benefits for medium-term economic growth prospects.

A mix of short-medium term and long-term policies are needed to address Africa's macroeconomic challenges and put economies back on the path of sustained, higher growth.

Countries need to increase debt transparency by improving the collection, reporting, and management of debt statistics and strengthening the monitoring of state-owned enterprises to reduce fiscal risks from undisclosed debt and contingent liabilities

In the short term

To achieve faster disinflation and anchor inflation expectations at minimal cost to the economy requires tailored monetary policy adjustments. In economies with high core inflation, central banks should keep policy rates high enough to ensure that inflation expectations remain firmly anchored to reverse the upward trend. Many African countries where domestic demand pressures are acute or inflation is very high, such as Egypt, Ethiopia, Ghana, Malawi, Nigeria, and Zimbabwe, need to tighten monetary policy quickly and decisively to reduce cost on rising inflation on the economy and households.

Promoting local production and diversifying import sources are key to addressing rising food prices. Supporting African smallholder farmers can trigger an agricultural revolution to feed Africa, especially in urban areas. African countries need to provide farmers with broad access to affordable finance, improved food production technologies (especially certified seeds adapted to extreme climatic conditions), and large-scale systematic extension and mechanization services to increase food production and thus stabilize food prices in the short to medium term.

Implementing governance reforms and strengthening debt management capacity are key to reducing the burden of public debt—as is the efficient use of borrowed resources. Countries need to increase debt transparency by improving the collection, reporting, and management of debt statistics and strengthening the monitoring of state-owned enterprises to reduce fiscal risks from undisclosed debt and contingent liabilities. Good governance also forms the basis for broader economic reforms. Efficient use of borrowed resources through investment in growth-creating sectors and infrastructure will further unlock the economic potential of African economies.

Addressing exchange rate pressures should be a key short-term policy priority. The depreciation of currencies in African countries has continued despite various measures to stabilize the exchange rates, largely because the pressure is externally induced. In countries with floating exchange rates, currencies should therefore be allowed to adjust as much as possible, since trying to resist movements based on fundamentals could have adverse secondary consequences on the economy. In countries with pegged exchange rates, monetary policy must be aligned with that of the anchor country to maintain external stability and avoid further losses in foreign exchange reserves as they intervene to preserve the exchange rate parity.

In the medium to long term

Reforming the current global financial architecture can make it fit for African countries' financing needs. And expanding the representation of developing countries will improve decisionmaking, increase transparency, and reduce the cost of capital. The resulting additional finance mobilized for development could help alleviate fiscal pressures on African countries, promote macroeconomic stability, boost market confidence, and reduce borrowing costs.

With elevated public debt choking many countries, scaling up domestic resource mobilization should be a top policy priority for African countries to accelerate structural transformation. In addition to improving debt management and fighting illicit financial flows, a multidimensional approach is needed to improve the collection and retention of resources generated domestically. To tackle illicit international flows, the measures include tightening financial regulations by imposing transparency and putting the burden of accountability on financial institutions.

Creating an enabling environment is crucial for attracting and scaling up external financial flows as complementary sources of development financing to accelerate Africa's economic transformation. Although domestic resources will remain an integral and larger part of financing Africa's economic transformation, external financial flows will be essential as complementary sources of funding for development needs. Africa has performed relatively well in attracting foreign direct investment (FDI) but much of this investment has been in extractive sectors and limited to few mostly large economies. African economies need to implement structural policies and create a supportive macroeconomic environment to attract more quality and stable FDI and predictable official development assistance to reap the growth dividends of external financial flows.

Accelerating structural reforms is essential to build resilient economies. The prolonged growth volatility in Africa in the aftermath of the COVID-19 pandemic, coupled with the decline in income growth, clearly calls for prioritizing structural reforms to strengthen the continent's resilience to shocks. In countries where growth volatility is largely due to monopolies in the energy sector—one of the main causes of power generation inefficiencies and related bottlenecks—liberalizing the energy sector should be a priority. In an environment where gaps in development financing remain large and financing conditions tight, budget spending should be reprioritized to redirect it to growth-enhancing public investment projects. Countries must also prioritize climate adaptation policies to improve their resilience to climate-related disasters and thus strengthen resilience.

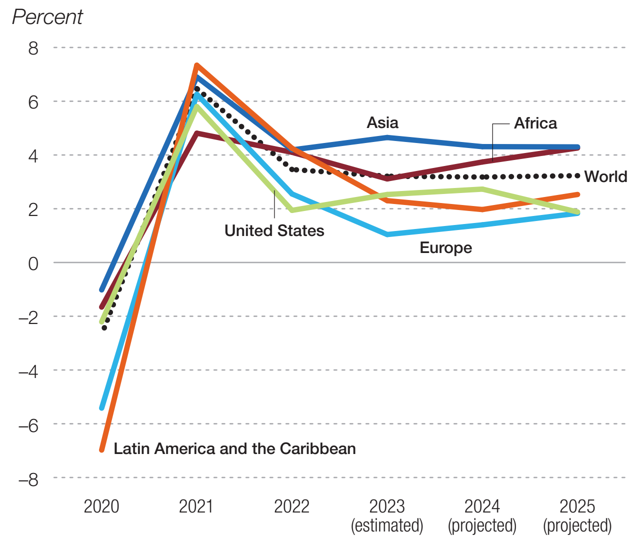
MACROECONOMIC PERFORMANCE AND PROSPECTS

Growth performance and outlook

Africa's growth performance remains volatile, with entrenched structural challenges and susceptibility to shocks

Average growth in real gross domestic product (GDP) decelerated to an estimated 3.1 percent in 2023 (figure 1.1). This rate is a deceleration of

FIGURE 1.1 Real GDP growth, by world region, 2020–25



Source: African Development Bank statistics and the International Monetary Fund's World Economic Outlook, April 2024.

1.0 percentage point from 4.1 percent recorded in 2022. It reflects persistently high food and energy prices on the back of sustained impact of Russia's invasion of Ukraine, weak global demand weighing down on exports performance, the impact of climate change and extreme weather events on agricultural productivity and electricity generation, and pockets of political instability and conflicts in some African countries. The slowdown was compounded by monetary policy tightening aimed at bringing inflation down amid depreciation pressures on exchange rates in several countries.

Although the growth deceleration was broad-based, affecting Africa's five regions, East Africa was the most affected as the conflict in Sudan raged on and continued to destabilize economic activity with spillover effects across the region. The impact of the conflict on Sudan's economy appears to be much deeper than previously assessed, with a contraction in real output increasing more than three times to 37.5 percent in 2023, from the 12.3 percent in the January MEO 2024.[2] The conflict is also having a significant contagion impact, particularly in neighboring South Sudan, which relies heavily on the former's pipelines and refineries, as well as port infrastructure for oil exports. Oil contributes about 90 percent to South Sudan's revenue and almost all of its exports. The adverse impact of the conflict in Sudan is evident in growth estimates for Africa. Excluding Sudan, average GDP growth for Africa is estimated to be 0.6 percentage point lower in 2023 relative to 2022, compared with 1.0 percentage point with Sudan included. Even more telling, the growth estimates for East Africa excluding Sudan increase to 5.7 percent in 2023 from 5.4 percent in 2022 compared with a growth of 1.5 percent when Sudan's deep contraction is factored in.

Despite the continuing headwinds, more than half of African countries (31) had higher real GDP growth rates in 2023 than in 2022, with six (6) of them—Burkina Faso, Djibouti, eSwatini, Libya, the Republic of Congo, and South Sudan—showing a difference in growth rates of more than 2 percentage points. In Libya, recording the highest growth increase of 16.3 percentage points in 2023, growth was boosted by continued oil production as the security situation improved. Crucially, fifteen (15) countries recorded growth rate in real GDP of at least 5 percent in 2023. Conversely, real output in Equatorial Guinea contracted in 2023, joining Sudan and South Sudan, which have been in recession since 2019 and 2021, respectively.

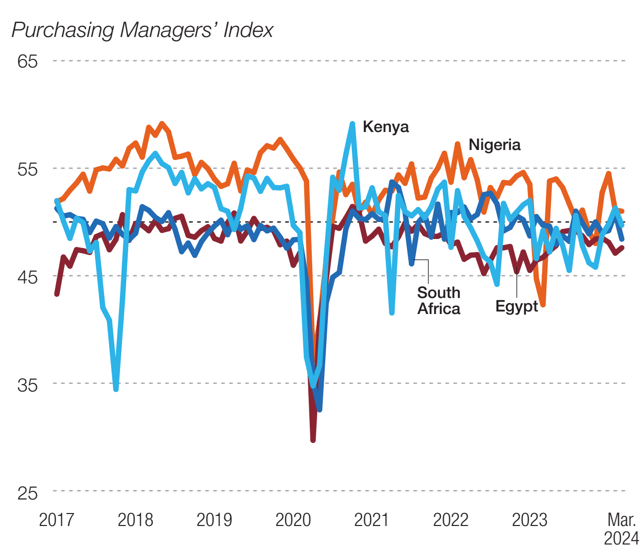
Despite the continuing headwinds, more than half of African countries (31) had higher real GDP growth rates in 2023 than in 2022

Looking forward, economic performance in Africa is poised to gradually improve. Real GDP growth is projected to increase to 3.7 percent in 2024 and firm up at 4.3 percent in 2025, as most of the effects of the risks that caused the deceleration in 2023 begin to subside. The projected stronger growth in 2024 and 2025 reflects expansions in East Africa (by 3.4 percentage points), Southern Africa (by 0.6 percentage point), and West Africa (by 0.6 percentage point)—and in 40 countries. However, 17 countries are expected to post growth rates higher than 5 percent in 2024, up from 15 in 2023, and the number could rise to 24 the following year. In 12 countries, the projected output expansion in 2024 will be below 1 percentage point than in 2023, meaning a slowing pace of growth in these economies. Despite the higher projected growth in the short to medium term, the dynamics of the conflict in Sudan remain fluid, and this is likely to weigh on Africa's average growth, particularly if the depth of the recession in that country and its contagion to South Sudan and the broader East Africa region deepens.

Despite the slowdown in Africa's estimated average growth rate in 2023, the continent is still ranked the second-fastest growing region after Asia. The growth projections for 2024 and 2025 also indicate that the continent will retain this position. The International Monetary Fund's April 2024 edition of the World Economic Outlook (WEO) estimates global growth to average 3.2 percent in 2023, led by Asia at 4.7 percent (see figure 1.1). The WEO projects global growth to stabilize at 3.2 percent in 2024 and 2025, while Asia's growth is projected to decline to 4.3 percent in 2024 and 2025. With Africa consistently posting the second-fastest growth rate globally in the last four decades, several African countries have been ranked among the top 20 fastest-growing economies globally. But average growth in the continent is still too low and insufficient to engender a faster economic transformation and convergence to higher income regions, as Asia experienced from 1970 to 2016, when its share in world industrial production increased tenfold from 4 percent to 40 percent.

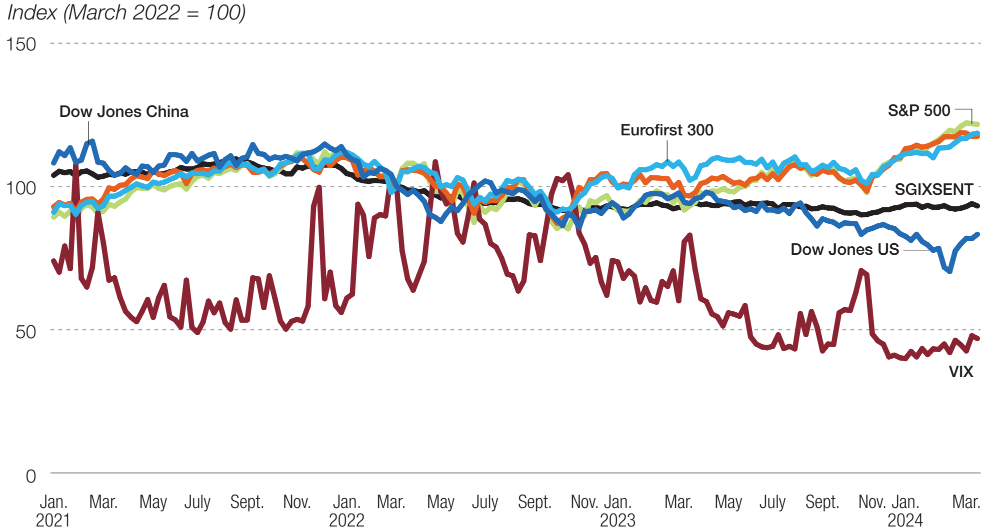
The estimated slowdown in Africa's real output growth in 2023 is corroborated by other high frequency indicators of economic activity. For instance, the Purchasing Managers' Index (PMI) in three of Africa's top six economies declined in 2023 (figure 1.2). The PMI was 47.9 in Egypt, 48.1 in Kenya and South Africa, 49.3, all below the 50 benchmark, showing weakening of economic

FIGURE 1.2 **Purchasing Managers' Index for four of the big six economies in Africa, 2017–March 2024**



Source: Haver Analytics and IHS Markit.

FIGURE 1.3A Global capital market indicators, 2021–March 2024



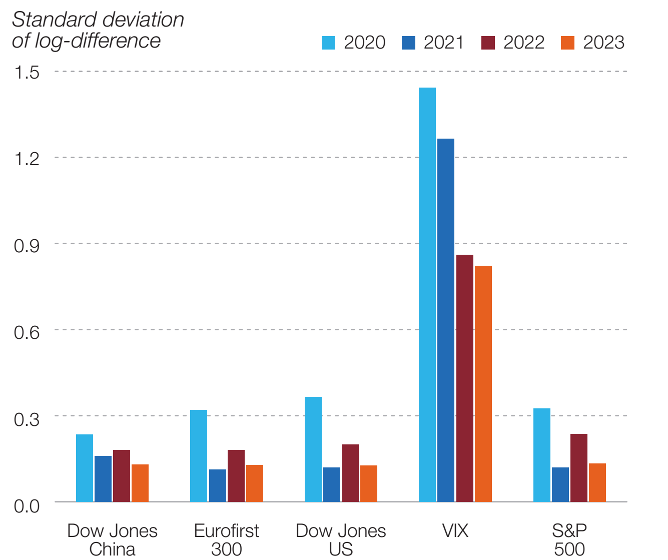
Note: SGIXSENT is the SG Global Sentiment Index.

Source: African Development Bank statistics, SG Global, and Bloomberg.

activity. The decline in the PMI in these countries was attributed to several factors including weak domestic currencies, high input prices and inflation, suppressing demand. In Kenya (–2.3 percent) and South Africa (–3.0 percent), the PMI value in 2023 deteriorated further from the average value in 2022. And although the PMI improved in Egypt in 2023, the reading remained below 50, signaling continued weakness in economic activity. Meanwhile in Nigeria, the PMI dropped to 50.4 in 2023, from 53.9 in 2022, due to heightened inflationary pressures and a weak domestic currency weighing on economic activity.

Global financial markets were calmer in 2023 than in the previous year after adjusting to the shock following Russia's invasion of Ukraine, causing a significant dip in sentiments and heightened volatility (figure 1.3a). The Global Sentiment Index was relatively stable in 2023 (figure 1.3b), compared with the volatility in 2022, largely reflected in the relative stability in global financial markets. Global financial market conditions have also benefited from the receding inflationary pressures in advanced economies and some major emerging market economies. More recently, the global financial markets appear to have commenced a strengthening phase in the first quarter of 2024, mirroring improving investor sentiment. The strengthening of global markets could be attributed to the expectations of higher economic growth in 2024 relative to the previous year.

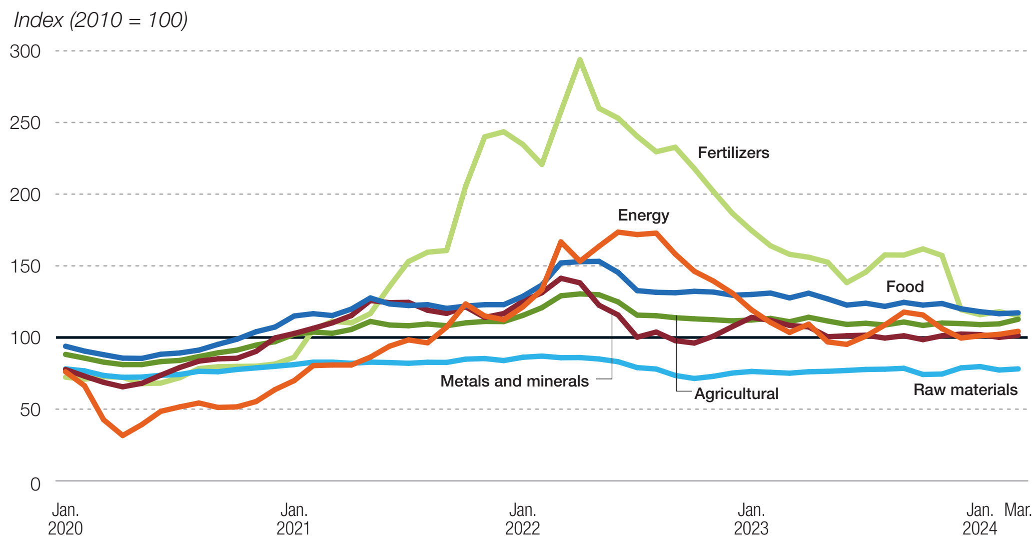
FIGURE 1.3B Global capital markets index volatility, 2020–23



Source: Staff calculations.

Although global commodity prices fell in 2023, they remained high relative to the immediate period before and during the peak of the COVID-19 pandemic (figure 1.4). While average energy and food prices declined in 2023 by about 30 percent and 9.2 percent, respectively, from 2022, they were about 100.3 percent and 34.7 percent

FIGURE 1.4 Global commodity price indices, January 2020–March 2024



Source: African Development Bank statistics based on the World Bank Commodity database.

While average energy and food prices declined in 2023 by about 30 percent and 9.2 percent, respectively, from 2022, they were about 100.3 percent and 34.7 percent higher than the level in 2020

higher than the level in 2020. The decline in average energy and food prices last year largely reflected subdued global demand. The receding trend in commodity prices continued even after the eruption of the conflict in the Middle East in October 2023 and sustained attacks on ships by Houthis rebels in the Red Sea in the last six months. Energy and food prices were respectively lower 3.0 and 2.5 percentage points on average during the last two quarters to March 2024, compared with the third quarter of 2023.

The short-term outlook of commodity prices remains highly uncertain. The evolution of energy prices will be shaped largely by a combination of global demand and supply conditions, geopolitical tensions, and decisions by OPEC+.[3] While OPEC estimates in March 2024 show that demand for oil would grow by 2.2 million barrels a day in 2024, geopolitical tensions and attacks in the Red Sea pose risks to energy supply and prices. And although food prices are expected to continue a downward trend facilitated by demand moderation amid increased supplies of major crops, particularly corn and soybeans, supply chain disruptions and effects of extreme weather events including the effects of El Niño, on agricultural output remain a major risk to this outlook.

Unlike real GDP growth, where Africa's performance compares favorably with most global regions, trailing only Asia, the continent's growth rate of real GDP per capita has lagged all other global regions for three consecutive years (figure 1.5). In 2023, estimated real GDP per capita growth in Africa was 0.7 percent, representing a decline of 1.0 percentage point from 2022. Moreover, Africa's estimated real GDP per capita growth in 2023 trailed Asia, the best performing region, by 3.3 percentage points and Europe, the second least performing region, by 0.5 percentage points. This is a significant setback for a continent that seeks to achieve income convergence toward advanced economies. Looking ahead, although real GDP per capita in Africa is projected to double to 1.4 percent in 2024 and reach 1.9 percent in 2025, it will still trail all other regions. At these relatively low real GDP per capita growth rates, it becomes increasingly evident that without deliberate sustained policies to engender structural transformation to spur higher economic growth, it will take much longer for countries to transition to higher income categories.

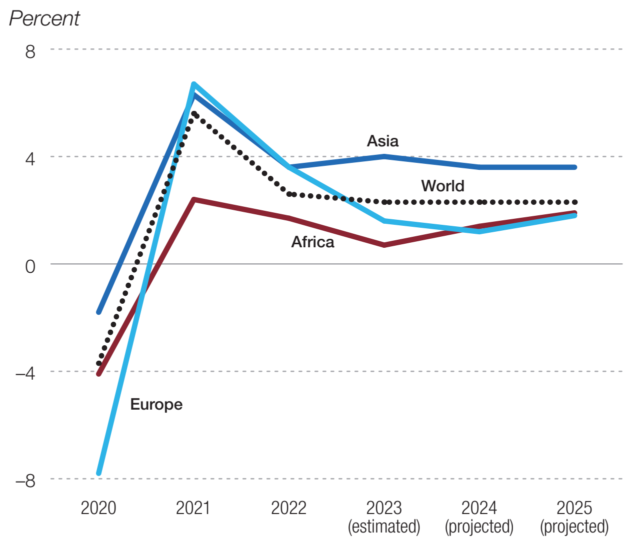
Sectoral and demand-side decomposition of growth

The decline in GDP growth in 2023 reflects the slow improvement in private consumption on the demand side and the vulnerability of the services sector, which dominates the supply side

While private consumption has for many years been the driver of growth on the demand side, some common factors explain the slow growth of this component of GDP. These include the persistent negative shocks, the tightening of monetary policy and the erosion of household incomes due to inflation pass-throughs that weigh on their purchasing power. Consequently, the contribution of private consumption to real GDP growth of 3.1 percent increased only modestly from 1.5 percent of GDP in 2022 to 1.7 percent in 2023 as the weight of these factors rose (figure 1.6). In 2024, the contribution is projected to increase to 2.4 percent and maintain the growth momentum in the medium term. However, the positive trajectory in private consumption may be scaled down with the increasing cost of living caused by structural challenges and inflation pass-throughs that affect household incomes.

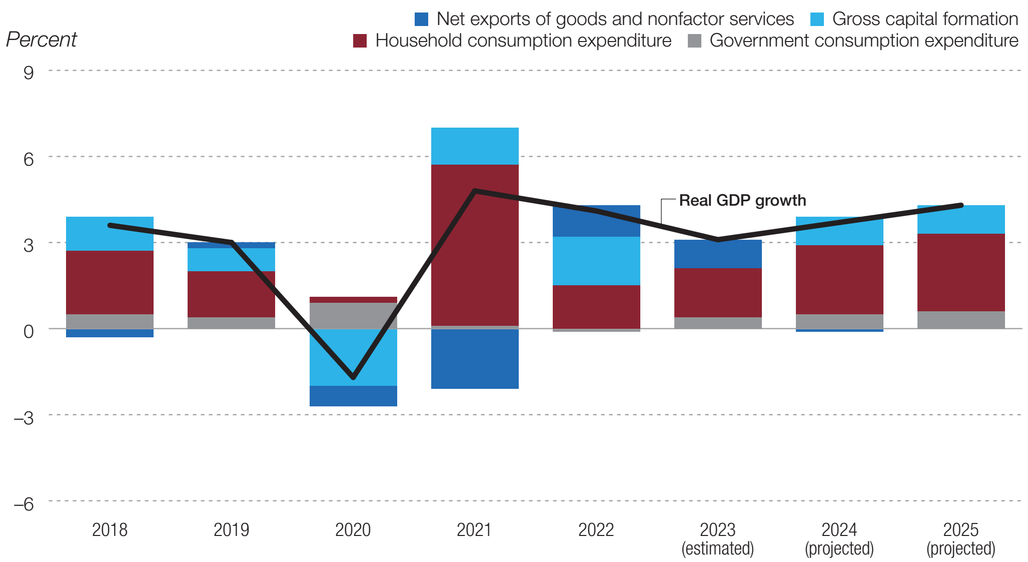
The contribution of net exports marginally declined by 0.1 percent between 2022 and 2023, reflecting the weakening of the domestic currencies which contributed to less than proportionate improvement in export growth than the reduction in imports. In 2024–25, the contribution of net exports is projected to decline by an average of 0.1 percent due to the expected strengthening of the domestic currencies thus expanding the imports. On the other hand, investment growth declined from a contribution of 1.7 percent in 2022 to negative 0.2 percent in 2023 but is projected to improve to 1.0 percent in 2024–25 to support GDP growth. The growth momentum expected in the medium term for investment could be supported through private sector growth and policy reforms expected to attract both domestic and foreign direct investment.

FIGURE 1.5 **Growth of real GDP per capita, by world region, 2020–25**



Source: African Development Bank statistics; the International Monetary Fund's World Economic Outlook, April 2024; and United Nations Population Division estimates.

FIGURE 1.6 **Demand-side decomposition of GDP growth, 2018–25**



Source: African Development Bank statistics.

The service sector is the main driver of growth on the supply side despite a decline in contribution from 2.9 percent in 2022 to 2.3 percent in 2023. The decline was due to exposure of the sector to a confluence of global shocks such as the geopolitical tensions and the slowdown of the global economy constraining tourism and terrorist attacks in the Red Sea which have disrupted shipments and trade. The influential role of the services sector is projected to remain in 2024 and 2025 despite the elevated downward risks for the sector. The renewed geopolitical tension in the Middle East and prolonged effects of Russia's invasion of Ukraine could further constrain tourism services and logistics, investments in the sector, and export growth of services such as transport, finance, and ICTs.

The contribution of agriculture to real GDP growth is estimated to have marginally declined from 0.5 percent in 2022 to 0.4 percent in 2023 while industry remained unchanged at 0.6 percent

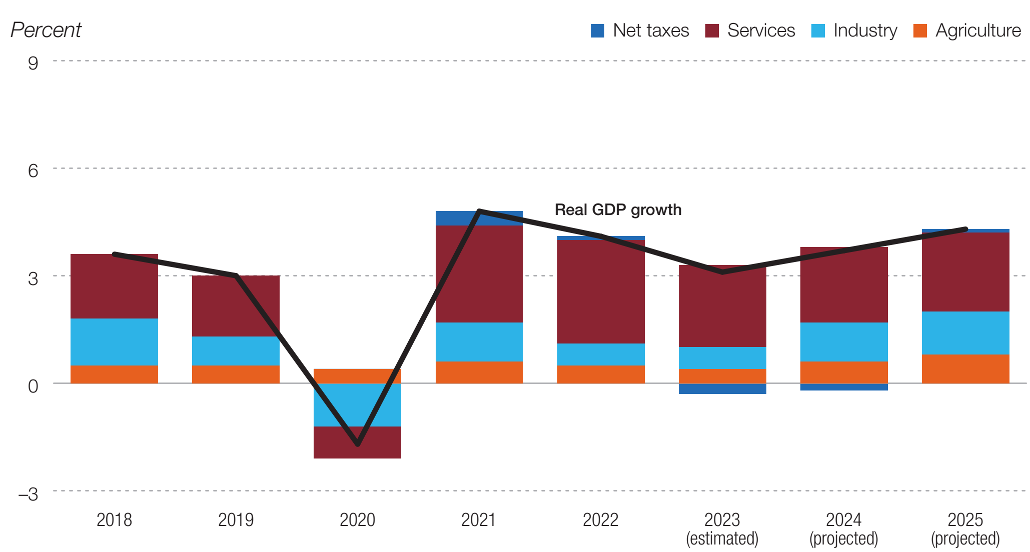
The contribution of agriculture is estimated to have marginally declined from 0.5 percent in 2022 to 0.4 percent in 2023 while industry remained unchanged at 0.6 percent (figure 1.7). The decline in agriculture was due to climate challenges such as droughts that affected yields while industry continues to face structural challenges such as the skills mismatch, high cost of capital, low internet access, and weak governance, among others, all discouraging investment. In 2024–25, agriculture is projected to improve by an average of 0.7 percent and industry by 1.2 percent as the impact of climate change eases in several countries in the region. This is premised on improved climatic conditions and the ongoing policy interventions to improve agricultural productivity in countries such as Kenya, Ethiopia, Nigeria, and South Africa. But downward risks to both agriculture and industry remains, including the negative effects of climate change, the escalation of global tensions that may affect imports of fertilizers and equipment, and the uncertainty limiting capital inflow to the productive sectors. Targeted policy interventions to improve productivity are required to build the resilience of the supply-side factors to cushion countries against emerging shocks.

Growth performance and outlook across-regions and countries

Expected improvements in economic performance with cross-regional variations

East Africa is expected to maintain its position as Africa's fastest growing region, with real GDP growth for the region projected to rise from an estimated 1.5 percent in 2023 to 4.9 percent in 2024 and 5.7 percent in 2025, respectively (figure 1.8). The downward revision of 0.2 percentage points for 2024 from the January 2024 MEO forecast is attributable to the economic contraction in Sudan and South Sudan. The 4.2 percentage

FIGURE 1.7 Sectoral decomposition of GDP growth, 2018–25



Source: African Development Bank statistics.

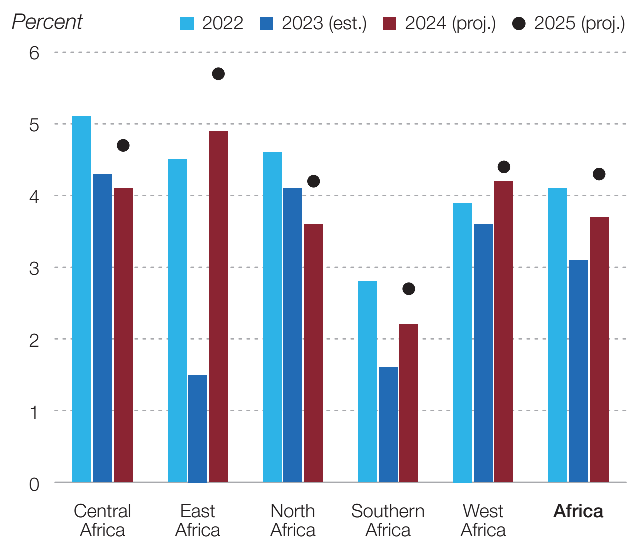
point markdown to Sudan's growth since the January 2024 MEO reflects the persistence of the country's devastating civil conflict that has severely reduced vital agricultural output and caused extensive destruction to critical industrial capacity as well as major logistic infrastructure and supply chains, resulting in significant impediments to foreign trade and exports.

Combined with the collapse of the key commerce and financial sector, Sudan continues to grapple with substantial capital flight and an 80 percent decline in state revenues. Its economy is projected to contract by 5.9 percent in 2024 before growing by a tepid 0.5 percent in 2025 while that of South Sudan could contract further in 2024 by 5 percent before posting modest growth of 1 percent in 2025. The 9.6 percentage point downward revision to South Sudan's growth from the January 2024 projection reflects the effects of rising domestic insecurity and the spillover of the conflict in neighboring Sudan, both of which have caused substantial disruptions to key crude oil exports and impeded livelihoods, trade, and food assistance delivery in a South Sudanese economy already grappling with severe humanitarian needs stemming from internal conflicts along with the rising frequency and severity of adverse weather events.

For the region, the economic slowdown in both countries is expected to be mitigated by the anticipated strong economic performance of 5 percent or higher in Ethiopia (6.7 percent), Rwanda (6.5 percent), Djibouti (6.2 percent), Uganda (6 percent), Tanzania (5.7 percent), and Kenya (5.4 percent). For these countries, the forecast growth acceleration in 2024 will be bolstered strong government spending and strategic investments to improve in-country connectivity and facilitate trade with neighboring nations, coupled with ongoing efforts to modernize agricultural production and boost productivity in the services sector.

Growth in **Central Africa** is expected to moderate from 4.3 percent in 2023 to 4.1 percent in 2024 before improving to 4.7 percent in 2025. The forecast upgrade for 2024 of 0.5 percentage point over the January 2024 projections for the region is attributable to stronger-than-expected growth in Chad and the Democratic Republic of Congo

FIGURE 1.8 GDP growth in Africa, by region, 2022–25



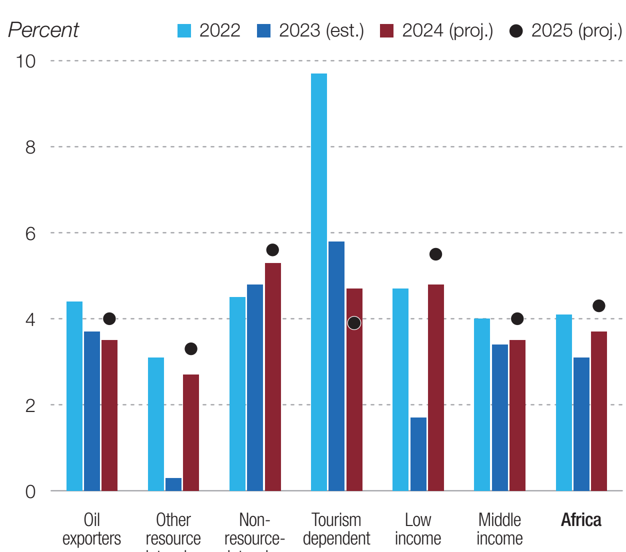
Source: African Development Bank statistics.

(DRC). Growth in Chad is projected at 5.2 percent in 2024 and 5.3 percent in 2025, with an upward revision of 1.3 percentage point for 2024 since the January 2024 MEO. The upward revision reflects enhanced oil recovery from existing production units, asset optimization, and new exploration and development of Chad's substantial oil and gas resources, as well as planned injection of funds generated from improved domestic resource mobilization toward improvements in infrastructure and provision of public services. In the DRC, growth is projected at 5.7 percent in 2024 before moderating slightly to 5.6 percent in 2025. The respective upward revisions of 1 and 0.3 percentage points for 2024 and 2025, from the January 2024 MEO forecasts, reflect the DRC's increased mobilization of external revenues in financing essential investments in energy and infrastructure projects. Authorities in the DRC seek to build on recent strong extractive industry performance and advance oil and gas exploration, transport, processing, and distribution for the country's development to previously unserved areas.

Growth is projected to pick up in **West Africa**, rising from an estimated 3.6 percent in 2023 to 4.2 percent and 4.4 percent in 2024 and 2025, with an upgrade of 0.3 percentage point for 2024 over the January MEO projections. Among major economies in the region, there are upgrades in 2024 of 1.1 percentage point for Senegal, 0.6 percentage point for Ghana, 0.3 percentage point for Nigeria, and 0.3 percentage point for Côte d'Ivoire. In Senegal, the growth upgrade for 2024 reflects rising export revenues thanks to increased production of natural gas and crude oil following the completion of key phases in two major hydrocarbon projects. The upward revision for Nigeria reflects recovering oil production and fiscal reforms to boost non-oil revenue. The forecast revision for Ghana reflects the carryover from stronger-than-expected growth in the last quarter of 2023 and the boost to private consumption stemming from exchange rate stability as the country's authorities implement an economic program aimed at restoring macroeconomic stability and securing debt sustainability.

In **North Africa**, growth is projected to decline from an estimated 4.1 percent in 2023 to 3.6 percent in 2024 and 4.2 percent in 2025, with a downward revision of 0.3 percentage point for 2024 since the January 2024 MEO. Apart from Libya, Morocco, and Tunisia, growth is revised downward by between 0.2 to 0.9 percentage points for all other countries in the region. While Egypt has managed to secure multilateral funding and international guarantees to clear foreign exchange shortages and mitigate any near-term risk of default, high inflation and strict fiscal tightening continue to constrain economic performance. So, its growth is projected at 3.3 percent in FY2023/24, 0.4 percentage point lower than January 2024 MEO forecast.

FIGURE 1.9 GDP growth in Africa, by country group, 2022–25



Source: African Development Bank statistics.

Growth in **Southern Africa** is projected to pick up slightly from an estimated 1.6 percent in 2023 to 2.2 percent in 2024 and 2.7 percent in 2025, with an upgrade of 0.1 percentage point for both periods over the January 2024 forecast. Downward growth revisions for Zimbabwe (1.6 percentage point), Lesotho (0.9 percentage point), Angola (0.2 percentage point) and Zambia (0.2 percentage point) could be offset by a projected doubling of growth in South Africa and sustained higher growth in other countries. For Zambia, the downward revision in its growth forecast reflects the lingering impacts of a recent cholera outbreak that coincided with the country's worst drought in two decades, devastating nearly half of its key maize output and inducing increased rationing of electricity across the country. More than 80 percent of Zambia's electricity supply is from hydropower plants. Zimbabwe also faces similar conditions as the El Niño drought reduced the power supply from the Kariba dam that the country shares with Zambia. The drought has also hit tobacco production, with reduced crop quality and depressed sales having severe consequences for the incomes of many smallholder farmers. The adverse weather conditions are also expected to halve the country's cereal harvest and reduce food security for some 3 million citizens. Growth in the region's economic powerhouse, South Africa, is projected at 1.3 percent in 2024 and 1.6 percent in 2025, with a slight upward revision of 0.2 percentage point for 2024 since the January 2024 forecast. Although growth remains tepid in South Africa, it reflects a significant improvement from weaker output growth in recent years as the country's manufacturing and mining sectors have struggled with high inflation, energy deficits, and logistical problems in exporting minerals due to deteriorating road, rail, and port infrastructure.

Real GDP growth in 2023 and projections across country groupings for the short to medium term are in line with the January 2024 MEO forecasts (figure 1.9). For **non-resource intensive economies**, growth is projected to improve from an estimated 4.8 percent in 2023 to 5.3 percent and 5.6 percent in 2024 and 2025, respectively. Economic performance across this country group will benefit from increased public investments in major growth sectors (mainly manufacturing and services) and substantial capital outlays on critical public infrastructure including electricity, transport, and logistics (in Rwanda, Burundi, Tanzania, Ethiopia, Uganda, Kenya, Djibouti, and Côte d'Ivoire, in that descending order). Growth for this group will also be supported by investments aimed at enhancing productivity and value addition within the key agricultural sector (Togo, Benin, and The Gambia).

Average growth for **tourism-dependent economies** is projected to decelerate from 5.8 percent in 2023 to 4.7 percent in 2024 and 3.9 percent in 2025. The slowdown for this country group reflects stabilizing tourism numbers at trend levels. Average growth in **oil-exporting countries** is expected to decline from an estimated 3.7 percent in 2023 to 3.5 percent in 2024 before improving to 4 percent in 2025, a downward revision of 0.1 percentage point for 2024 and an upward revision of 0.1 percentage point for 2025 from the January 2024 forecast. The downward revisions for 2024 are mainly attributable to temporarily lower oil production targets set by Organization of the Petroleum Exporting Countries (OPEC) for Nigeria, and uncertainty regarding new mechanisms for Angola's oil exports following its exit from OPEC amid disputes over production quotas and steadily declining output.

Growth in **other resource-intensive economies** on the continent is expected to remain steady and in line with the January 2024 MEO projections. This group is estimated to grow from 0.3 percent in 2023 to 2.7 percent in 2024 and 3.3 percent in 2025. Improved growth for this group will be largely driven by China, where strong demand is linked to expansions in smart grids and construction.

Downside and upside risks to the growth outlook

The projected economic recovery could strengthen as long as the global economy remains resilient, fiscal consolidation measures across the continent continue, efforts to reduce inflation are sustained, and recent progress on debt restructuring is extended to other countries. However, Africa's current economic performance and prospects are affected by many downside risks, including higher inflation if not addressed, an escalation of geopolitical tensions and regional conflicts, and climate change that could reverse the projected economic recovery.

Downside risks

Persistence of inflationary pressures in many African countries could put further pressure on African economies. The persistence of inflationary pressures is a key risk and one of the driving forces explaining Africa's economic performance and prospects. These inflationary pressures, due to increases in food and energy prices triggered by the COVID-19 pandemic and exacerbated by Russia's invasion of Ukraine, continued to weigh on the continent's economic performance in 2022 and 2023. To combat the rise in inflation and persistent inflationary pressures, several African countries have taken a cue from advanced economies and tightened monetary policy, but the results are yet to materialize and may be mixed, depending on structure of their economies and degree of exposure to global shocks. Sustained higher inflation could trigger successive waves of interest rate hikes, which could jeopardize the predicted economic recovery.

To combat the rise in inflation and persistent inflationary pressures, several African countries have taken a cue from advanced economies and tightened monetary policy, but the results are yet to materialize and may be mixed

Rising geopolitical tensions and polarization could jeopardize global trade and international investment. As tensions in the Middle East remain elevated and risks of a full-blown regional conflict are not discounted and international trade routes are becoming increasingly under threat (as with the Al-Mandab strait), trade flows are disrupted, causing supply chain problems worldwide and raising the cost of transshipment. While the World Container Index price fell by 25 percent from its January 2024 peak, it is still twice the value for December 2023. Ensuing economic stress from trade disruptions may spill over to financial and commodity markets and reduce FDI, while increasing uncertainty, political instability, and risk premia across Africa as capital flows to safer jurisdictions. A new wave of higher inflation and subdued economic growth may also hit the global economy, with dire consequences for African economies already struggling with multiple decade-long high inflation. According to IMF estimates, all African regions except North Africa could experience a permanent decline of up to 4 percent of GDP after 10 years due to geopolitical tensions and stand to lose an estimated $10 billion of FDI and official development assistance (ODA) inflows.[4]

Higher commodity prices could ignite a new wave of inflation and upend the decline in poverty. Commodity prices have caught a substantial headwind from the Fed's and ECB's planned rate cuts and geopolitical tensions. Oil prices have risen by 25 percent from their late 2023 lows, a trend reinforced by OPEC+ confirming its current production policy of caps, which has already tightened oil supply and helped prices move higher. Oil prices are key contributors to rising consumer price indexes worldwide. Basic input to industrial production such as metals, especially copper and aluminum, have also seen renewed price increase in recent months. Higher commodity prices may also delay much anticipated policy rate cuts in developed economies, especially in the United States, where energy prices are key drivers of policy rates, and this could lower global economic growth. These developments heighten the risk of tilting the world economy off its disinflationary path and could hit Africa's most vulnerable countries where food and energy make up a large share of household consumption. A deepening of these risks could thus dampen prospects for Africa's projected economic recovery.

As seen recently, political instability triggered by unconstitutional changes of government elicits sanctions from regional and international communities, depressing economic activity due to trade disruptions and a loss of investors' confidence

Increased regional conflicts and political instability in some countries. Regional conflict and political instability could impose large economic and social costs. They could also increase countries' fragility and strain public finances by lowering revenues and raising defense spending, shifting resources away from development and social support. As seen recently, political instability triggered by unconstitutional changes of government elicits sanctions from regional and international communities, depressing economic activity due to trade disruptions and a loss of investors' confidence. If political paralysis persists, the cost to economies could be large and prolonged. For instance, recent military coups in Burkina Faso, Gabon, Guinea, Mali, and Niger and coup-related sanctions from regional blocs have disrupted economic activity and imposed heavy social costs. Political instability and concerns over human rights violations have led to the Central African Republic, Gabon, Niger, and Uganda losing benefits from the US African Growth and Opportunity Act. The loss of the benefits has consequences for import prices and the export of more than 1,800 products with duty-free access to the US market. Internal conflicts and violence could also result from rising prices for fuel and other commodities due to weaker domestic currencies and reforms. For instance, the removal of fuel subsidies in Angola, Ethiopia, Kenya, and Nigeria and the resulting social costs have led to social unrest driven by opposition to government policy.

Climate shocks. Unfavorable climate and weather events are another important risk factor for Africa's growth prospects. These adverse events pose a serious threat to African countries, but especially to countries in transition, and can exacerbate fragility and undermine development prospects. For example, El Niño-related rainfall anomalies are leading to excessive drought in Southern Africa and are likely to result in below-average harvests this year. In general, African countries suffer more from floods, droughts, storms, and other climate-related shocks than other countries but contribute the least to climate change. Recent empirical studies show that climate change causes more lasting macroeconomic costs in emerging African countries, with cumulative GDP losses reaching around 4 percent three years after extreme weather events. In comparison, the loss in other countries is around 1 percent.[5]

Upside risks

Continuing fiscal consolidation and renewed economic growth to improve African public finances. Fiscal consolidation measures, a projected rebound in economic growth making room for greater fiscal revenues, and private creditors taking steps for debt restructuring are the main contributors to the improving fiscal outlook. In

Zambia, for instance, the "official sector" creditor committee led by China signed in June 2023 a memorandum to restructure $6.3 billion of the country's debt. In March 2024, the authorities reached an agreement with bondholders to restructure more than $3 billion sovereign debt. Ghana is also making steady progress with debt restructuring, and its Extended Credit Facility with the IMF is on course. As a result of these tailwinds, Africa's debt-to-GDP ratio is projected to decline to around 60 percent in 2024 from around 63.5 percent in 2021–23, halting an almost decade-long increase. If the positive trend persists and global market conditions improve, African countries could see sovereign interest rates decline, stimulating economic growth as their risk premia decline accordingly.

Continued structural transformation and renewed capital accumulation to promote sustainable economic growth. Structural transformation, defined as the shift from low-productivity to high-productivity sectors, is slow but progressing in Africa. While Africa's labor productivity grew by 1.26 percent over 1990–2021, half of it came from labor reallocations to higher productivity sectors. The shift in labor is contributing to raising GDP per capita by sustaining an increase in domestic production, not just aggregate demand, which also helps to build resilience to external shocks. For instance, the share of agriculture in Africa's economy declined from 55.7 percent to 42.7 percent over 1990–2021, if with marked cross-country differences. Productivity growth could be further enhanced by private investment and public infrastructure projects, and as increased production capacity lowers inflation, interest rates could start declining. A virtuous cycle of between- and within-sector productivity growth could lift real wages, opening space for savings mobilization needed to fund the long-term capital accumulation of both public and private sectors.

Lower policy rates in advanced economies and some emerging markets lift economic growth. As disinflation continues in advanced economies and some emerging economies, leading central banks such as the European Central Bank (ECB) have signaled incoming cuts to their policy rates in 2024. The likelihood of imminent monetary policy easing is reinforced in the Euro area by faster disinflation than expected and subdued economic growth in the region's two largest economies, Germany and France. A cooling labor market in the United States could ease the labor market and weaken underlying inflationary pressures, and such developments could allow the Fed to push ahead with its monetary easing plan much sooner than expected. The Fed's readiness to accommodate higher inflation in the face of deteriorating fiscal health is also favoring monetary policy easing despite record high equity and home prices. A wave of rate cuts would revive credit growth in both regions, boost consumer sentiment, alleviate pressure on public debt servicing, and reinforce global growth. Africa would directly benefit from rebounding global growth as the two regions combined represent 40 percent of the world's GDP, 55 percent of the FDI stock, and about two-thirds of ODA to Africa.

Asia-led economic growth spilling over to Africa. At 8.4 percent in the last quarter of 2023, India's economy grew at its fastest pace in one-and-half years. Higher growth in Asia's third largest economy was led by strong expansion in manufacturing (+11.6 percent year-on-year) and construction activity (+9 percent year-on-year). Investment growth was also above 10 percent for the second consecutive quarter. In parallel, China's GDP forecasts are being revised up as factory activity, car sales, and foreign trade firm. Tourism and services figures are also pointing to a solid recovery in consumer sentiment and consumption in Africa's largest trading partner. But loans climbing to record highs and the ongoing contraction in the property sector are, however, weighing on growth. But contrary to most advanced economies, China can rely on ample policy space. The People's Bank of China recently signaled strong support for its existing pro-growth policies, and the government is pushing ahead with transforming the growth model toward making structural adjustments, improving quality, and enhancing performance. These conditions, underpinning an Asian-led economic growth, bode well for Africa's projected recovery in the near term.

A virtuous cycle of between- and within-sector productivity growth could lift real wages, opening space for savings mobilization needed to fund the long-term capital accumulation of both public and private sectors

OTHER MACROECONOMIC DEVELOPMENTS, IMPLICATIONS, AND OUTLOOK

Inflation developments, implications, and outlook

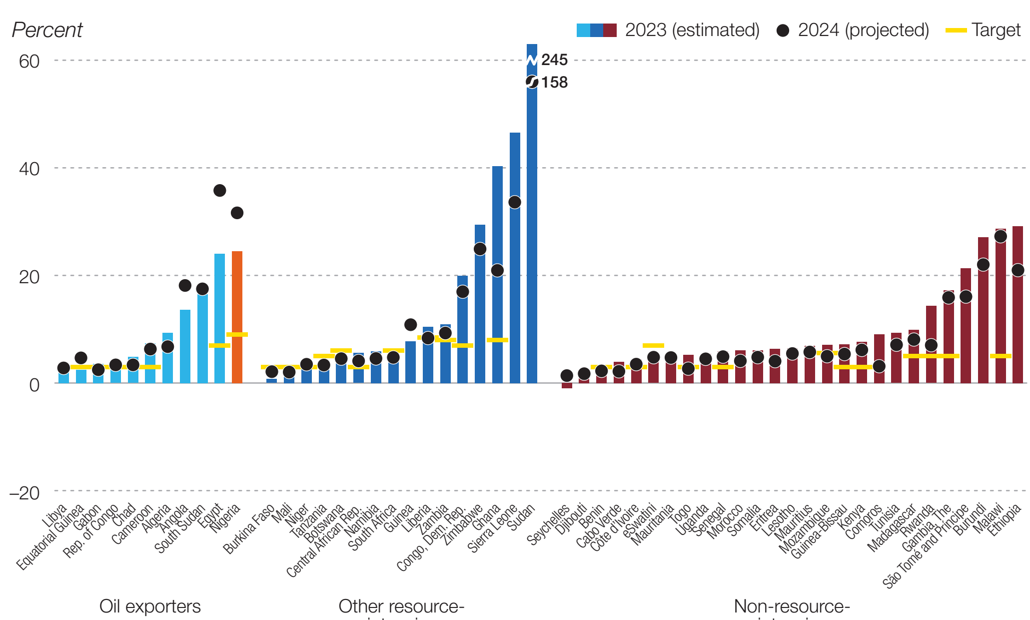
Inflation remains persistently high and continues to weigh on African economies

Inflation, on an upward trend in Africa since the start of the COVID-19 pandemic, is set to remain high despite aggressive monetary policy interventions started last year. Average consumer price inflation in Africa is estimated to have increased by 3 percentage points to 17 percent in 2023, from 14 percent in 2022, eroding socioeconomic gains prior to COVID-19 (figure 1.10). The increase reflects a combination of higher local food prices induced by drought-related domestic supply shortages, liquidity overhang from pandemic-related fiscal and monetary policy stimulus, and the pass-through effects of currency depreciation against a strong US dollar propelled by high interest rates in the United States. From 2022 to 2023, inflation rose in 32 African countries. At the end of 2023, 17 African countries had double-digit inflation, and this number is expected to remain high. In three of the six largest African countries by GDP and population, inflation was above 20 percent in 2023—Egypt (24.0 percent), Nigeria (24.5 percent) and Ethiopia (29.2 percent). But excluding these three countries, the average inflation rate is estimated to have fallen from 12.6 percent in 2022 to 11.3 percent in 2023 and is forecast to fall further, reaching single digits of 8.4 percent in 2024 and decelerating further to 6.3 percent in 2025.

> Average consumer price inflation in Africa is estimated to have increased by 3 percentage points to 17 percent in 2023, from 14 percent in 2022, eroding socioeconomic gains prior to COVID-19

Across regions, the inflation picture is mixed. Despite a decline from 30.8 percent in 2022 to 26.5 percent in 2023, inflation in East Africa was highest in the continent. A faster decline in inflation for the region is constrained by Sudan, where inflation was estimated at 245.3 percent in 2023, up from 164.6 percent in 2022. The ongoing war has disrupted the country's economy and led to shortages of goods and services, stoking widespread price increases. Inflation is also touching double digits in Ethiopia (29.2 percent), Burundi (27.1 percent), South Sudan (16.5 percent), and Rwanda (14.3 percent). West Africa has the second-highest inflation, estimated at 20.3 percent in 2023, up from 16.9 percent in the previous year, with Sierra

FIGURE 1.10 Consumer prices inflation, 2023–24



Note: Values for Sudan have been truncated for a better visibility of other countries.

Source: African Development Bank statistics.

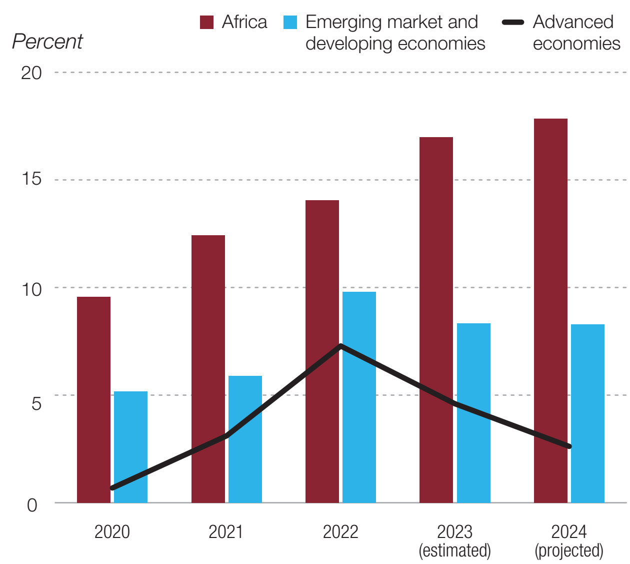
Leone (46.6 percent) and Ghana (40.3 percent) topping the list, ahead of Nigeria (24.5 percent), which abolished fuel subsidies early in 2023. This policy reform drove the price of premium motor spirit up by 220 percent between November 2022 and November 2023. At 16.3 percent, up from 8.2 percent in 2022, North Africa recorded the highest increase in inflation in 2023, driven by rapidly rising inflation in Egypt, from 8.5 percent in FY2021/22 to 24 percent in FY2022/23, catalyzed by geopolitical tensions, which destabilized food supplies and unsettled global food markets.

Inflation is also on the rise in Central Africa, though to a lesser extent, rising from 6.8 percent in 2022 to 10.3 percent in 2023, driven by the Democratic Republic of Congo, which recorded an increase of 10.6 percentage points in 2023 on the back of high food prices and a depreciating currency. The weakening of the Congolese franc is expected to be more moderate in 2024 thanks to the recovery in mineral prices, which will help prop up export revenues and replenish foreign exchange reserves and eventually weigh down on inflation. The transmission of monetary tightening will also have an impact on prices, after the Central Bank of Congo sharply hiked its key rate from 11 percent to 25 percent in October 2023. Only in Southern Africa has the inflation rate fallen—from 10.8 percent in 2022 to 8.6 percent in 2023, driven by inflation developments in Angola, Botswana, South Africa, and Zimbabwe. In Angola, inflation sharply fell by 8 percentage points to 13.6 percent in 2023, as factors such as the continued weakness of the currency and the phasing out of fuel subsidies, which pushed up inflation last year, subsided. South Africa's inflation also fell from 6.9 percent in 2022 to its upper policy limit of 6 percent in 2023, as transportation costs finally came down.

Inflation is expected to peak in 2024 before cooling thanks to the expected easing of food and energy prices and tight monetary policy

Following the aggressive tightening of monetary policy initiated by most central banks, emerging and developing economy inflation and global inflation began to decline from their respective 2022 peaks of 9.8 and 7.3 percent to (projected) 8.3 and 5.9 percent by 2024, respectively (figure 1.11).

FIGURE 1.11 Inflation persists in Africa, more than the rest of the world, 2020–23



Source: African Development Bank statistics.

Falling energy prices and the normalizing supply chains contribute to falling prices worldwide. In Africa, by contrast, despite similarly aggressive monetary policy tightening, inflation remains high and is weighing on growth and livelihoods. Empirical studies show that an increase in inflation by one percentage point on the continent translates into a loss of 0.21 percentage point in the average growth rate of real GDP (box 1.1). Worryingly, the trajectory of inflation in both advanced economies and Africa point to increasing divergence, falling in the former and increasing in the latter. The outlook for Africa's inflation remains bleak, with the average rate expected to rise from an estimated 17.0 percent in 2023 to 17.8 percent in 2024. The projected increase is reflected in persistently high food prices and the imbalance between supply and demand in both domestic and global food markets.

Monetary policy, implications, and outlook

African central banks are going against the global trend by raising interest rates

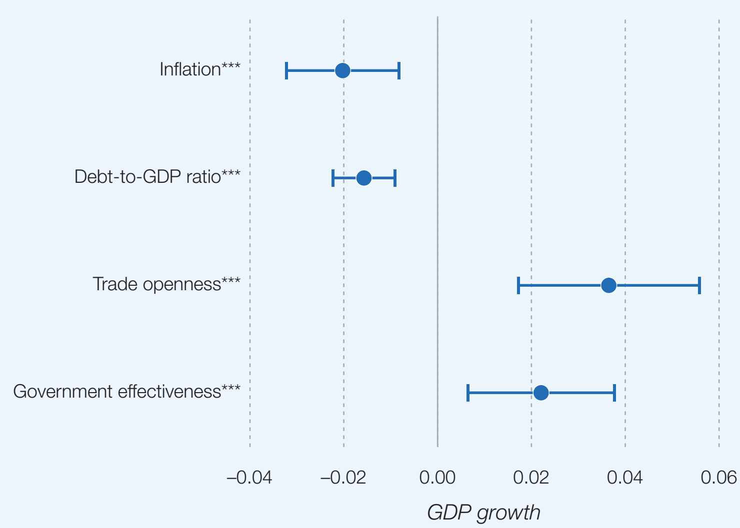
Higher inflation in Africa has left little room for African central banks to begin interest rate cuts similar to those initiated or envisioned in other regions of the world. Since the January 2024 MEO, 20

BOX 1.1 High inflation weighs on Africa's real GDP growth

The relationship between inflation and real GDP growth is a topic of ongoing debate in macroeconomics. According to the classical view of the "neutrality of money," an increase in inflation has little impact on GDP, as inflation increases both prices and wages in the same way. Here, the long-term impact of inflation on real GDP growth in African economies is examined using panel data from 52 countries over 2002–22. The empirical assessment shows that a one percentage point increase in the inflation rate leads to a loss of 0.01 to 0.03 percentage points in the average growth rate of real GDP (box figure 1.1.1).

The results suggest that implementing macroeconomic policies to reduce inflation rates should be a priority if African countries want to sustain their projected growth momentum and build resilient economies. As control variables, a high debt-to-GDP ratio has a negative impact on growth, while greater trade openness and government efficiency have a positive impact on real GDP growth. For instance, an increase in the debt-to-GDP ratio of one percentage point leads to a loss of 0.01 to 0.02 percentage points in real GDP growth. As a result, maintaining a higher growth dynamic also requires further debt restructuring to reduce the debt burden in African countries.

BOX FIGURE 1.1.1 Impact of inflation on real GDP growth

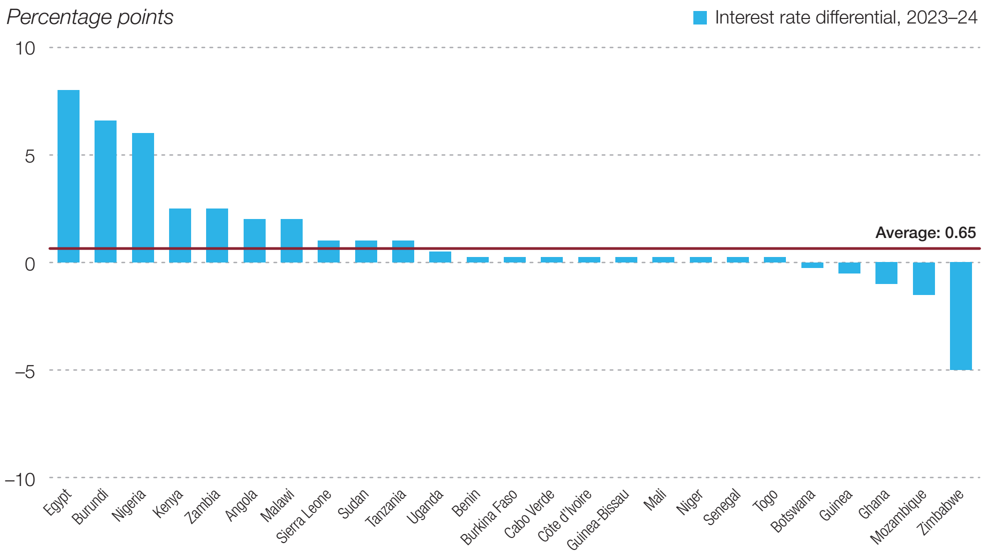


Source: Staff calculations.

African central banks raised their policy rates as 5 lowered them (Botswana, Ghana, Guinea, Mozambique, and Zimbabwe). The remaining countries left their rate unchanged (figure 1.12). Among countries that increased policy rates, 6 of the 10 largest economies—Egypt +8 percentage points, Nigeria +6 percentage points, Kenya +2.5 percentage points, Angola +2 percentage points, Tanzania +1 percentage point, and Côte d'Ivoire +0.25 percentage point—account for 40 percent of Africa's GDP. African central banks are also using the Cash Reserve Ratio (CRR) as a monetary policy instrument. For instance, while keeping its policy rate unchanged, Ghana's central bank adjusted the CRR to encourage lending by banks instead of investing in treasury bills. In Nigeria, the central bank maintained the CRR for commercial banks as high as 45 percent of naira deposits in an effort to control inflation and support the naira.

The policy impact of these measures in the noninflation-targeting countries has been less

FIGURE 1.12 Policy rate differential (percentage points) for Africa 2024–25, excluding Zimbabwe

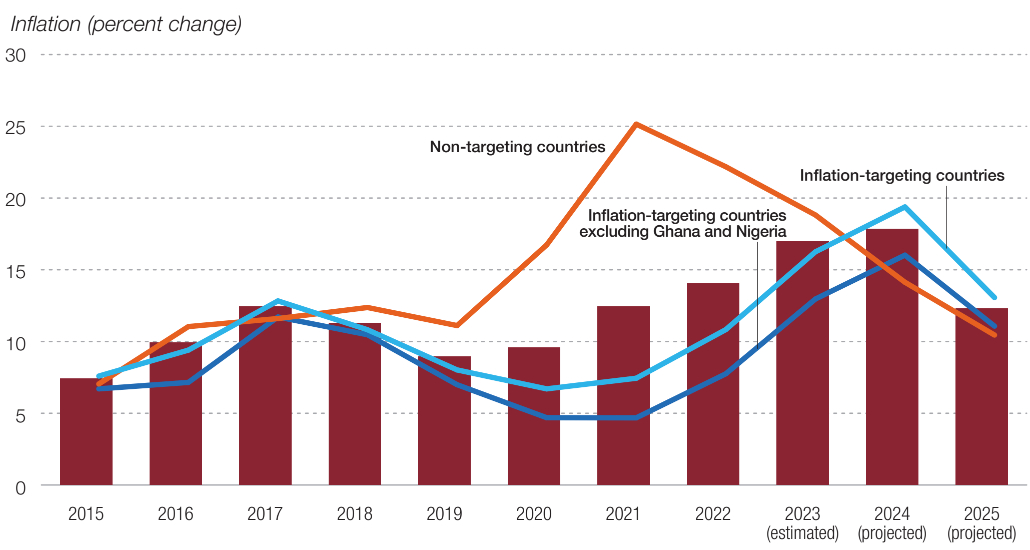


Source: African Development Bank statistics.

effective, and inflationary pressures are estimated to have remained elevated in 2023 compared with the outturn in the inflation-targeting peers. The forecast in the short to medium term shows convergence in inflation rates for the two groups (figure 1.13), but inflation-targeting countries will need to do more to bring inflation back to target levels in 2024 and 2025. The differences in the pace of disinflation across countries reflect different vulnerabilities to commodity prices and

Higher inflation in Africa has left little room for African central banks to begin interest rate cuts similar to those initiated or envisioned in other regions of the world

FIGURE 1.13 Inflation dynamics in targeting and nontargeting countries



Note: Inflation targeters are Benin, Botswana, Burkina Faso, Cameroon, Central African Republic, Chad, Democratic Republic of Congo, Republic of Congo, Côte d'Ivoire, Egypt, Equatorial Guinea, Gabon, The Gambia, Ghana, Guinea-Bissau, Kenya, Liberia, Liberia, Malawi, Mali, Mozambique, Niger, Nigeria, Rwanda, Senegal, South Africa, eSwatini, Tanzania, Togo, Uganda, and Zambia.
Source: Staff calculations.

currency volatility, as well as varying degrees of economic overheating and fiscal dominance. The effectiveness of traditional tools of monetary policy in Africa has been weakened by the current nature of inflationary pressures. The high rate of inflation across Africa is largely structural, driven by external factors as well as domestic food supply shocks. In such an environment, sustaining high policy rates may not be tenable, without imposing a cost on private sector growth, especially for small and medium enterprises.

By contrast, the high- and middle-income economies interest rate cutting cycle has started in earnest with seven countries lowering rates in 2024 (Brazil, Chile, Czech Republic, Hungary, Mexico, Peru, and Switzerland), with the European Central Bank (ECB) preparing to do so. Only two central banks have raised rates this year, in Japan and Turkey. Policy rates have indeed remained high in both the United States and the euro area since mid-2023. However, the two regions' business cycles are now increasingly diverging, with contrasted impacts on African economies. The relative buoyance of the US economy increasingly questions the policy rate cuts much expected by the Fed. This is likely to maintain downward pressure on African currencies and impede the fight against inflation in the continent. By contrast, the euro area economy stagnated in the fourth quarter of 2023, following a 0.1 percent contraction in the previous quarter. As a result, the ECB is now expected to lower rates ahead of the Fed. The ensuing weakening of the euro and sluggish growth in the region are likely to weigh on Africa's exports to Europe, which is Africa's second main trading partner after Asia, well ahead of intra-African trade. In Asia, inflation remains elevated. As a result, apart from China and Vietnam, Asian central banks kept policy rates equal to or higher than their prepandemic levels. Policy support in China, combined with forthcoming rate cuts amid solid growth in other Asian countries, is likely to benefit Africa and alleviate pressure on its currencies.

The high rate of inflation across Africa is largely structural, driven by external factors as well as domestic food supply shocks

Careful identification of the sources of inflation and better coordination between monetary and fiscal policy are needed

The persistently high inflation in Africa despite aggressive monetary tightening revives the debate on the effectiveness of monetary policies. A key issue is that supply factors are more important for inflation in Africa—related to recent geopolitical and commodity price shocks as well as more structural issues such as low productivity and inadequate infrastructure. In addition, supply factors are expected to become more frequent and persistent in Africa due to geopolitical polarization and global value chain reconfigurations. Supply shocks push up inflation and reduce output, presenting an unfavorable tradeoff between output and inflation stabilization. Indeed, inflation and output are often negatively correlated in Africa, in contrast with high-income countries where demand shocks are more frequent and the stabilization of inflation also serves to stabilize output. Targeted supply-side policy responses that are not necessarily monetary are then needed, such as deepening trade liberalization through intraregional trade or boosting domestic supply and attracting investment. But demand shocks have also been at play recently, such as accommodative monetary policy in the wake of the COVID-19 pandemic and enduring fiscal dominance. Fiscal policy should be aligned with monetary policy, especially if the latter is trying to restrain aggregate demand. Raising policy rates under strong fiscal dominance is unlikely to bear fruit but will further reduce private economic activity. As African central banks struggle to bring inflation back to acceptable levels, monetary and fiscal policy coordination should be given a higher priority in Africa.

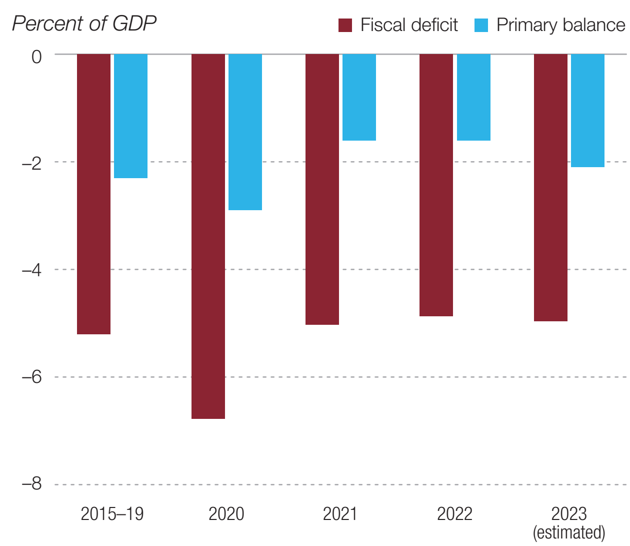
Fiscal positions and domestic resource mobilization

Fiscal deficits are expected to widen marginally before narrowing toward prepandemic levels, but uncertainties remain high

Four years since the outbreak of COVID-19, fiscal positions are slowly returning to the prepandemic levels (figure 1.14) as countries rein in spending and institute measures to spur mobilization of revenues. Updated estimates show that the average fiscal deficit on the continent inceased slightly from 4.9 percent of GDP in 2022 to 5 percent in 2023, mainly due to the marginal widening of the primary balance from 1.6 percent of GDP in 2022 to 2.1 percent of GDP in 2023. The slight deterioration in the primary deficit is mainly due to measures implemented to mitigate the effects of rising food prices amid falling energy sector revenues. Debt servicing, however, has stabilized thanks to additional debt restructuring programs, benefiting countries such as Ethiopia, Ghana, and Zambia, whose budget deficits narrowed in 2023.

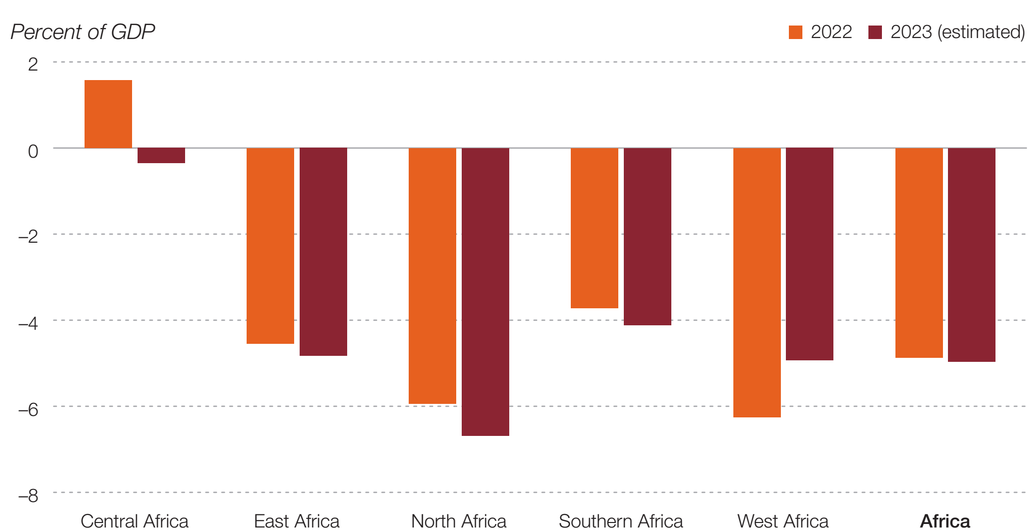
Of the five African regions, four have seen an increase in their fiscal deficits (figure 1.15). Central Africa saw the sharpest increase, from a surplus of 1.6 percent of GDP in 2022 to a deficit of 0.4 percent in 2023, led by Equatorial Guinea and the Republic of Congo, whose surpluses fell from 11.9 percent and 8.9 percent of GDP in 2022 to 0.8 percent and 4.2 percent in 2023, respectively, mainly due to a decline in oil revenues. The North Africa region recorded the second-highest increase in the budget deficit from 5.9 percent of GDP in 2022 to 6.7 percent in 2023, driven by Algeria and Libya. The budget deficit in Algeria worsened from 7.8 percent of GDP in the previous year to 10.2 percent in 2023, and Libya turned its budget surplus of 3.1 percent of GDP in 2022 into a near-balanced budget position in 2023, mainly due to lower revenues from the oil sector. Southern Africa and East Africa also recorded increases in their budget deficits, albeit to a lesser extent, from 3.7 percent of GDP to 4.1 percent and from 4.5 percent of GDP to 4.8 percent respectively. By contrast, the West Africa region strengthened its fiscal position by reducing its budget deficit from 6.3 percent in the previous year to the continent's average of 4.9 percent of GDP in 2023. The improvement in fiscal positions in countries such as Côte d'Ivoire, Ghana, Nigeria, and Sierra Leone has helped reduce the budget deficit in the region. Ghana stands out in particular with a budget deficit that fell by 7.3 percentage points of GDP, from 11.8 percent of GDP in 2022 to 4.5 percent

FIGURE 1.14 Overall fiscal balance and primary fiscal balance, 2015–23



Source: African Development Bank statistics.

FIGURE 1.15 Fiscal balance as a share of GDP by region, 2022–23



Source: African Development Bank statistics.

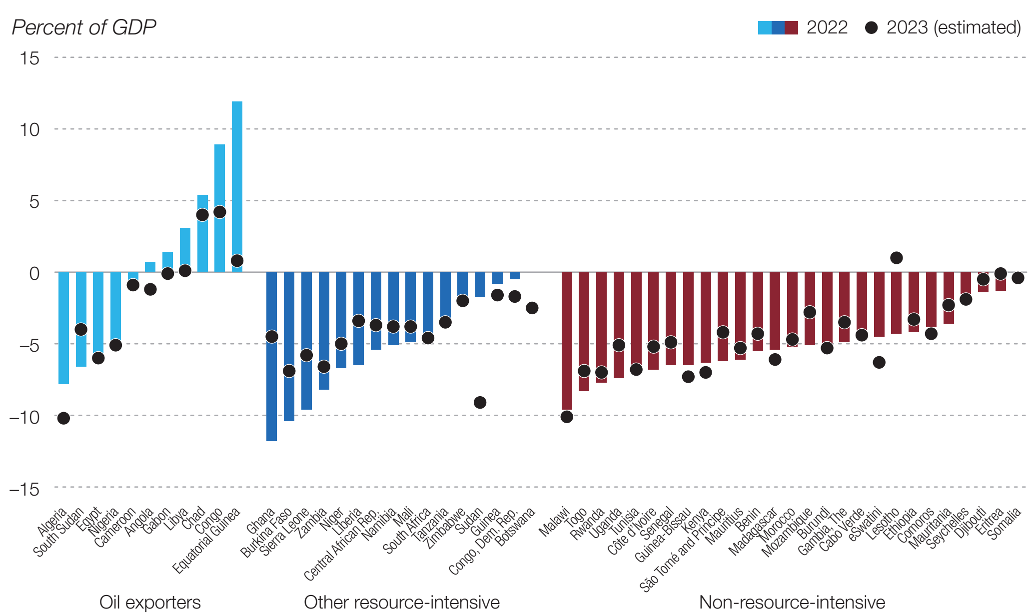
of GDP in 2023. This improvement is partly due to the improvement in the primary balance and partly to the macroeconomic stabilization measures implemented. Ghana received a three-year Extended Credit Facility (ECF) program of around USD 3 billion from the IMF and embarked on a global restructuring of its debt. In this context, the authorities have committed to consolidating the budget and implementing structural reforms in the areas of fiscal policy, tax administration, and public financial management.

Of the 11 oil-exporting countries, 7 posted fiscal deficits in 2023, while only 4 countries had budget surpluses

Of the 11 oil-exporting countries, 7 (Algeria, Angola, Cameroon, Egypt, Gabon, Nigeria, and South Sudan) posted fiscal deficits in 2023, while only 4 countries (Chad, Equatorial Guinea, Libya, and the Republic of Congo) had budget surpluses (figure 1.16). Despite this bifurcated situation, the group recorded on average a fiscal deficit of 5.4 percent of GDP in 2023 compared with 4.6 percent in 2022. The average fiscal deficit of non-resource-intensive economies continued to improve, from 5.7 percent of GDP in 2022 to 4.9 percent of GDP in 2023, supported by cheaper import bills and slightly improving economic activity. More than two-thirds of countries in this category improved their fiscal balance in 2023. Lesotho, Mozambique, São Tomé & Príncipe, and Uganda reduced their fiscal deficit by more than two percentage points of GDP. The average fiscal deficit of other resource-intensive economies also narrowed slightly, from 4.6 percent of GDP in 2022 to 4.4 percent of GDP in 2023. Like the non-resource-intensive economies, all countries in this group recorded a budget deficit in 2023, and two-thirds reduced its size from 2022.

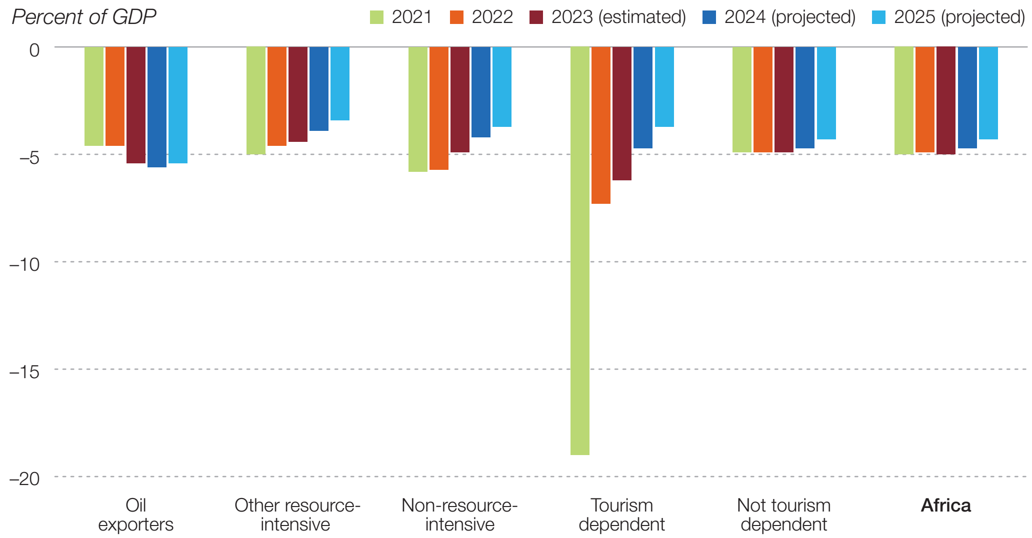
The fiscal deficit across the continent is projected to narrow in 2024 to 4.7 percent of GDP and further to 4.3 percent of GDP in 2025 after the slight increase to 5 percent of GDP in 2023 (figure 1.17). After the record deficit following the COVID-19 outbreak, tourism-dependent countries have seen an improvement in their budget deficits with the resumption of international tourism activities. This group is expected to have the lowest fiscal deficit by 2025. With the exception of oil-exporting countries whose budget deficit could increase in 2024 to 5.6 percent of GDP from 5.4 percent in 2023 before reverting and stabilizing at 5.4 percent in 2025, other groups are likely to experience a gradual reduction in their budget deficit in the short term. The easing of energy prices is expected to lower oil revenues for oil-exporting countries, creating risks to their fiscal position. Budgetary consolidation programs linked to debt restructuring in several

FIGURE 1.16 Fiscal balance as a share of GDP by country, 2022–23



Source: African Development Bank statistics.

FIGURE 1.17 **Fiscal balance as a share of GDP by country grouping, 2020–25**



Source: African Development Bank statistics.

countries should free up some budgetary space, contributing to the reduction of their fiscal deficit.

Domestic resource mobilization remains the most daunting policy challenge for African countries to finance their economic transformation

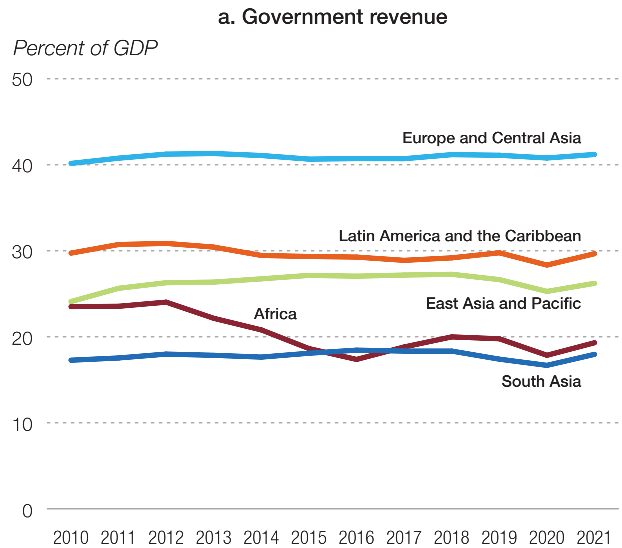
Increased domestic resource mobilization remains a pressing policy challenge facing African countries in financing their transformation agenda. Domestic resources, if mobilized at scale, can sustain Africa's efforts to reduce extreme poverty and inequality, ensure provision of quality health and education services, and develop basic infrastructure to support inclusive growth. Countries must therefore ensure that public spending is meaningful and efficient in supporting sustainable development and protecting the most vulnerable from the harmful effects of climate change and other shocks. Despite recent efforts in mobilizing domestic resources, Africa's average general government revenue (tax and nontax revenues, excluding grants) declined substantially from 23.5 percent of GDP in 2010 to 19.8 percent of GDP in 2019 (figure 1.18).

The reduction in average gross government revenue is mainly due to a steady decline in tax revenue, which is the main source of domestic revenue in most countries in Africa. Tax revenues declined by 1.8 percentage points over the same period, from 16.1 percent of GDP in 2010 to 14.3 percent of GDP in 2019. The decline was partly due to inefficient tax collection systems and insufficient use of digital technologies to improve compliance and tax collection. Over the five years before the COVID-19 pandemic (2015–19), average tax revenue was only 14.1 percent of GDP, below the 15 percent minimum for a developing country to adequately finance its Sustainable Development Goals (SDGs). This ratio is also well below the corresponding period average for Latin America (23.9 percent) and less than half the average for Europe and Central Asia (31.7 percent). Estimates for the post-COVID-19 period (2021–22) show a sign of recovery in tax revenues to an average of 14.6 percent of GDP. Although 28 African countries recorded an increase in tax revenues in 2022 relative to the five-year average prior to outbreak of COVID-19, only 21 countries had tax revenues above the 15 percent threshold mentioned above.

The pattern of gross revenues mimics the evolution in tax revenues. In tandem with the fall in tax revenues, general government revenue fell by almost 2 percentage points to an average of 17.8 percent of GDP in 2020, from 19.8 percent of GDP in 2019. In 2022, general government revenue was estimated at 20.5 percent of GDP, a recovery

After the record deficit following the COVID-19 outbreak, tourism-dependent countries have seen an improvement in their budget deficits with the resumption of international tourism activities

FIGURE 1.18 Total government and tax revenue in Africa since 2010

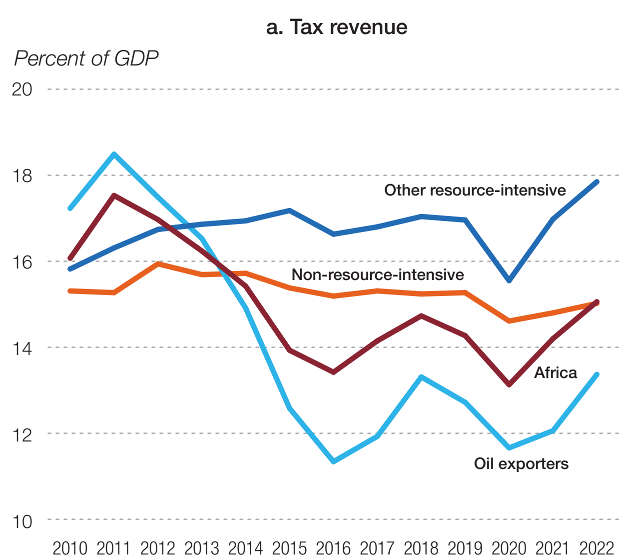


Source: Staff calculations based on data from the IMF World Economic Outlook.

from the pandemic-induced decline. Here too, Africa's performance was below comparator regions, except South Asia (17.6 percent of GDP). Reflecting the diverse economic landscapes in the continent, revenue ratios vary considerably across country groupings. This heterogeneity highlights the need for country-specific tax policies.

The trend in revenues in Africa was mainly driven by non-oil resource-intensive economies (figure 1.19). For this group, general government and tax revenues were estimated at 20.5 percent of GDP and 17.0 percent in 2019. Tax revenues for non-resource intensive countries, which depend largely on direct income taxes, notably corporate income and pay-as-you-earn, have fallen progressively over the last decade due to inefficiency in tax collection systems. More worryingly, oil-dependent economies, while deriving significant

FIGURE 1.19 Government revenue and tax revenue by economic characteristics



Source: Staff calculations based on data from the IMF World Economic Outlook.

revenues from oil activities over the same period, have not substantially increased their non-oil tax revenues. The ratio of their tax revenues increased slightly to 13.4 percent of GDP in 2022 from 11.7 percent in 2020. These revenues have also been volatile, in tandem with the cyclicality in commodity prices. In contrast, non-oil resource intensive countries began to take advantage of the post-pandemic recovery, increasing their tax revenues to 17.8 percent of GDP in 2022 from 15.6 percent reached in 2020.

On average, African countries mobilize only half as many internal resources relative to GDP as advanced economies, and despite a variety of strategies to increase public revenues, the progress made remains limited. Numerous factors determine a country's domestic resource mobilization. Studies and research reports on public finance show that success in domestic resource mobilization depends on several macroeconomic, political, demographic, and institutional factors (see MEO 2024). Macroeconomic determinants include the level of development, the level of debt, the rate of private investment, the size of the manufacturing sector, the terms of trade, the ease of access to private sector credit, the rate of inflation and the size of the informal sector. Demographic factors such as the proportion of the working population or economically dependent population and the degree of urbanization are also among the determinants highlighted in the literature. Institutional factors include the ability of authorities to maintain a stable political environment, fight corruption, and create a favorable economic environment with property rights and simplified administrative procedures.

External position and current account balance

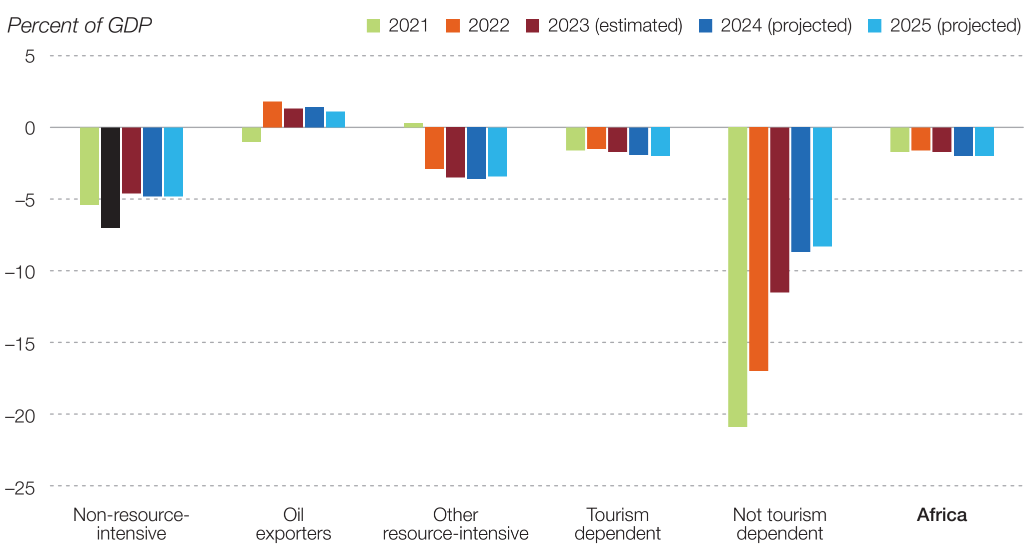
Africa's overall external position is projected to weaken slightly in 2024–25

The average current account deficit is projected to widen from an estimated 1.7 percent of GDP in 2023 to 2 percent of GDP in 2024 and 2025, respectively (figure 1.20). The projections, which represent a narrowing of the deficit by 0.2 percentage points in 2024 over the January 2024 MEO forecast, reflect the rebound in global trade and the boost to China's commodities imports as its construction sector stabilizes and resilience in its domestic economy is aided by recovering investments and firm consumer spending.

The average current account deficit is projected to widen from an estimated 1.7 percent of GDP in 2023 to 2 percent of GDP in 2024 and 2025, respectively

Current account surpluses in net oil-exporting economies are expected to improve from an estimated 1.3 percent of GDP in 2023 to 1.4 percent of GDP in 2024 before declining to 1.1 percent of GDP in 2025, with an upward revision

FIGURE 1.20 **Current account balances in Africa, by country group, 2021–25**



Source: African Development Bank statistics.

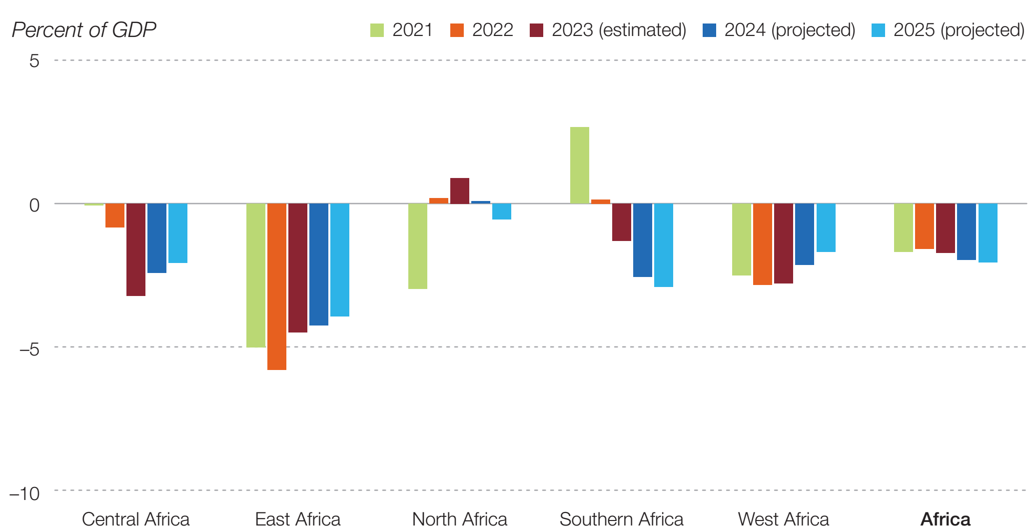
of 0.1 percentage points from the January MEO figure for 2024, reflecting rising oil prices stemming from persistent geopolitical tensions in the Middle East and supply shocks mainly from several unilateral and negotiated output cuts by OPEC and OPEC+ countries. Although Chinese imports of nonenergy raw materials is rising, the allocation of these imports to stockpiles rather than end-users have had little impact on prices, which declined from their post-pandemic peak in 2023. The slump in prices of nonenergy raw materials has hit other resource-intensive economies, where the current account deficit is projected to widen from an estimated 3.5 percent of GDP in 2023 to 3.6 percent of GDP in 2024 before narrowing slightly to 3.4 percent in 2025, representing a downward revision of 0.1 and 0.2 percentage points for both 2024 and 2025 figures, respectively, from the January 2024 MEO forecasts.

North Africa's positive external position, given the estimated current account surplus of 0.9 percent of GDP in 2023, is projected to decline to 0.1 percent of GDP in 2024

The average current account deficit in nonresource intensive economies is projected to widen from an estimated 4.6 percent of GDP in 2023 to 4.8 percent of GDP in both 2024 and 2025, respectively. While figures for 2024 and 2025 represent 0.7 and 0.3 percentage points upgrade on the January 2024 MEO forecast, they mainly reflect the carryover effects of capital import bills as governments ramp up spending on public infrastructure in energy, transport, and logistics. Improvements in the external position is anticipated for tourist-dependent economies, where the current account balance is projected to narrow from an estimated 11.5 percent of GDP in 2023 to 8.7 percent and 8.3 percent of GDP in 2024 and 2025, respectively. The improvements, a 3.3 and 2.2 percentage point upgrade for the 2024 and 2025 figures over the January 2024 ME0 forecast, reflect the carryover of reduced fuel import bills and growth in tourism revenues boosted by higher occupancy rates and continuing recovery in tourist arrivals.

North Africa displays a positive external position (figure 1.21), given the estimated current account surplus of 0.9 percent of GDP in 2023 projected to decline to 0.1 percent of GDP in 2024 and the large deficit of 8.5 percent of GDP in Mauritania more than offset by Libya's current account surplus of 24.5 percent of GDP. However, this surplus could deteriorate into a deficit of 0.6 percent of GDP in 2025. Mauritania's deficit, down from an estimated 9.8 percent of GDP in 2023, reflects an anticipated rise in export earnings with expansions in output of iron ore, gold, and gas complemented by reduced spending on imported capital goods. For Libya, the current account surplus, projected to average 21.8 percent between 2023 and 2025, is due to improvements in stability which has aided increased oil output. Despite double-digit deficits in Liberia (23.7 percent of GDP), Senegal

FIGURE 1.21 **Current account balances, by African region, 2021–25**



Source: African Development Bank statistics.

(10.9 percent of GDP), and Guinea (10.3 percent of GDP), West Africa is projected to have the second-lowest external deficit (2.1 percent of GDP), driven by the projected improvement in external surplus in the region's largest economy, Nigeria, from an estimated 0.9 percent of GDP in 2023 to 3.0 percent of GDP in 2024. The average current account deficit in Central Africa is projected at 2.4 percent of GDP in 2024, with the external surplus in Chad (1.3 percent of GDP) and the Republic of Congo (3.2 percent of GDP) offset by the wide external deficit in the Central African Republic (9 percent of GDP), the Democratic Republic of Congo (4.5 percent of GDP), and Equatorial Guinea (3.5 percent of GDP).

The projected current account deficit of 2.6 percent in Southern Africa reflects the offsetting of external balance surpluses in Angola (5.1 percent of GDP), eSwatini (3.9 percent of GDP), Zambia (3.4 percent of GDP), Botswana (1.1), and Zimbabwe (0.7 percent of GDP) by significant external deficits in Mozambique (38.1 percent of GDP), São Tomé & Príncipe (11.4 percent of GDP), Namibia (9.6 percent of GDP), and Malawi (8.2 percent of GDP). The surge in Mozambique's current account deficit is attributable to the rise in capital imports associated with the resumption of Total's Area 1 LNG project. In Malawi, persistence in the current account deficit is expected to be fueled by the carryover of foreign exchange shortages amid rising import bill for food and energy, coupled with negative consequences of adverse weather shocks on output of key agricultural exports. South Africa, the region's economic powerhouse, is set for a negative external position at 2.9 percent of GDP in 2024, on the back of weak export commodity prices, the intensified logistics infrastructure constraints, and strong imports for energy-related projects.

Despite the exceptional current account surpluses in Djibouti (20 percent of GDP) and Eritrea (12.4 percent of GDP), East Africa is projected to have the highest external deficit (4.2 percent of GDP) in 2024. The region is forecast to have the second-highest median deficit in 2024 (6.7 percent of GDP), with Rwanda (10.9 percent), Somalia (10.4 percent), and Uganda (8.3 percent) having the highest level of external imbalance. In Rwanda and Uganda, the deficits are attributable to persistent effects of the decline in prices of traditional exports and the negative impact of adverse weather on coffee and tea production, coupled with a drop in secondary incomes. The current account imbalance in Somalia reflects the decline in exports due to drought and insecurity caused by frequent terrorist attacks, and rising merchandise import bills, particularly food items as well as machinery and transport equipment essential to ongoing private and public construction projects.

Decomposition of the current account

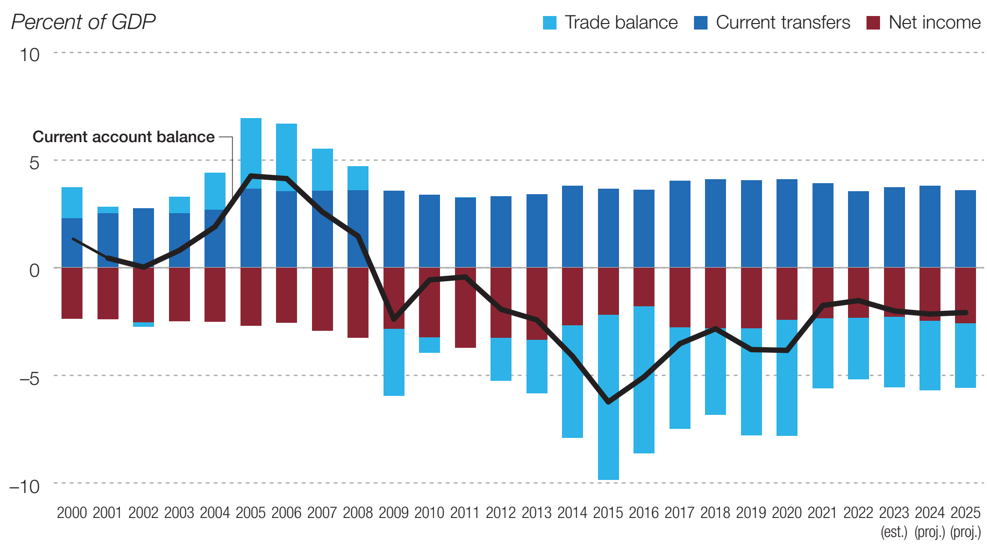
The analysis of Africa's current account, according to the external accounts approach, reveals that the slight increase (+0.2 percent of GDP) in the 2023 deficit arose from a widening of the trade deficit to 3.3 percent of GDP compared to 2.8 percent the previous year (figure 1.22). The net income deficit (2.3 percent of GDP) remained broadly unchanged. The current transfer surplus in 2023 (3.7 percent of GDP) increased slightly from that of 2022 (3.6 percent of GDP). The trade deficit could narrow slightly in 2024 (3.2 percent of GDP) and this trend is likely to continue in 2025 with the deficit projected at 3 percent of GDP, in line with an expected improvement in export revenues. The current account is expected to remain in deficit at 2.0 percent of GDP in 2024 and 2025, due to slight widening in the deficit on net income. This decomposition shows that the instability and persistent current account deficit are largely driven by the dynamics of the trade balance, itself dependent on the evolution of the terms of trade.

Despite the exceptional current account surpluses in Djibouti (20 percent of GDP) and Eritrea (12.4 percent of GDP), East Africa is projected to have the highest external deficit (4.2 percent of GDP) in 2024

The unstable and persistent trade deficit since the financial and economic crisis of 2008 harms economic stability and fuels the increase in debt in Africa. To escape dependence on terms-of-trade cycles and macroeconomic instability that are harmful to economic and social development, African economies must diversify by taking advantage of their natural capital endowment. Developing the manufacturing sector and reducing the size of exports of unprocessed raw materials must be part of the economic transformation strategy of African countries.

A decomposition of the current account according to the savings-investment approach shows that variations in national savings would have an important role in driving the current account, particularly for countries with widening current account deficits

FIGURE 1.22 Dynamics and decomposition of the current account in Africa, 2000–25



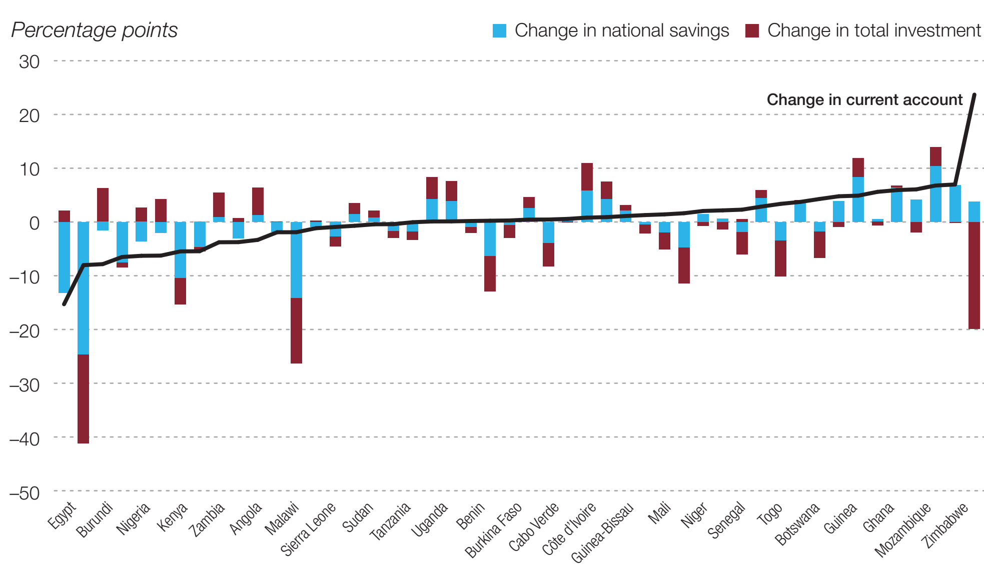
Source: African Development Bank statistics.

A decomposition of the current account according to the savings-investment approach shows that variations in national savings would have an important role in driving the current account, particularly for countries with widening current account deficits

(figure 1.23). Five countries (Algeria, Angola, Chad, the Republic of Congo, and South Sudan) experienced the greatest deteriorations in their current accounts in 2023, underpinned by the weakness in national savings. Although the increase in investment contributed to widening the current account deficit in these countries, the decline in national savings was more decisive. In South Sudan, the current account deteriorated on account of sharp decline in national savings, which more than offset the fall in investment due to deepening instability and associated risk to investment.

Countries with marked improvement in their current accounts increased national savings, as for Lesotho, Mauritania, Namibia, Senegal, and eSwatini. In contrast, the stronger improvement in Mozambique is mainly due to the sharp decline in investment. From the perspective that African

FIGURE 1.23 Change in current account, national savings, and total investment, 2022–23



Source: Staff calculations based on the WEO database.

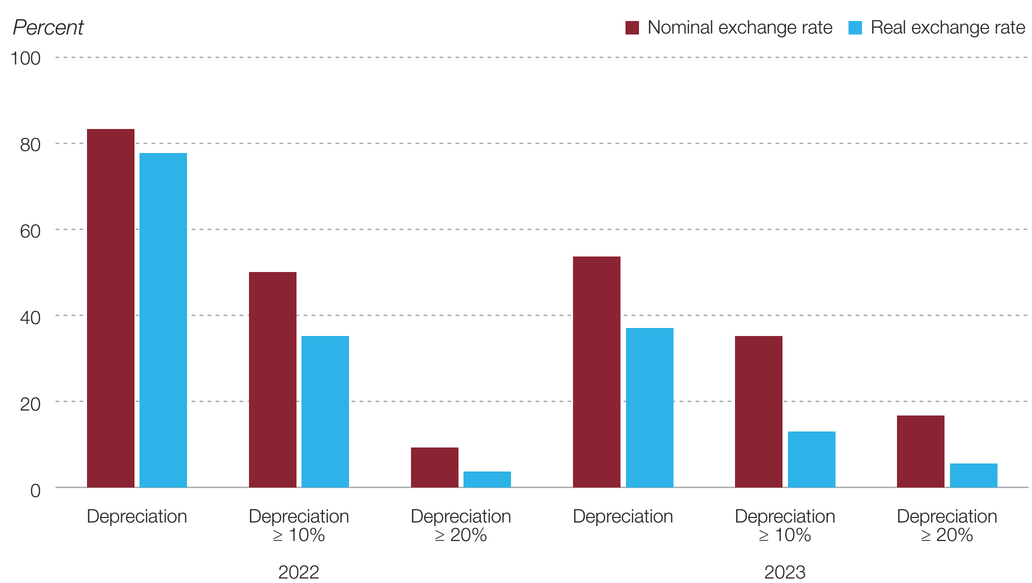
economies must accelerate productive investments to meet the challenges of structural transformation, policies aimed at encouraging savings—private savings and controlling budget deficits—are fundamental to avoid worsening external imbalances. One of the keys to increasing savings remains improving the employment rate. Creating opportunities for decent work for Africa's young population has the potential to raise national savings and reduce dependence on debt to support domestic investment.

Exchange rate and monetary policy developments

The depreciation of African currencies persisted in 2023 but with less broad coverage. Under the pressure of persistently high global interest rates and ongoing global uncertainty, fueled by geopolitical and financial tensions, most African currencies depreciated further against the US dollar in 2023. However, currencies such as the CFA franc, the Moroccan dirham, the Cape Verdean escudo, the São Tomé and Príncipe dobra, and the Comorian franc have regained value due to their full or partial peg to the euro, which regained some strength against the dollar in 2023. Conversely, the Zimbabwean dollar (–89.8 percent), Sudanese pound (–77.6 percent), South Sudanese pound (–46.0 percent), Egyptian pound (–37.4 percent), Angolan kwanza (–32.8 percent), and Zambian kwacha (–15.4 percent) recorded the largest depreciations in 2023. These sharp depreciations are the consequences of persistent economic difficulties (Egypt and Zimbabwe) and political instability (Sudan and South Sudan). The sharp depreciation of the kwanza results from the lack of foreign currency on the market, the downward trend in oil prices, and the end of the moratorium provided by Chinese creditors. Overall, 29 African countries were affected by a nominal depreciation against the US dollar in 2023, compared to 45 in 2022 (figure 1.24). For 19 of them, the nominal depreciation was at least 10 percent, while 9 countries had a nominal depreciation of at least 20 percent. High inflation in most African countries has dampened the effect of nominal depreciation, with fewer countries showing real exchange rate depreciation. Rather, many countries recorded an appreciation of their exchange rates, in real terms, against the dollar. Countries with the highest rates of appreciation (over 10 percent) range from Ghana (11.6 percent) to Sudan (163.6 percent), as domestic hyperinflation offset the effect of nominal depreciation of the exchange rate.

Overall, 29 African countries were affected by a nominal depreciation against the US dollar in 2023, compared to 45 in 2022

FIGURE 1.24 **Proportion of African countries with depreciated currencies, 2022–23**



Note: Depreciation without further indication refers to a fall in the value of the domestic currency regardless of the value.

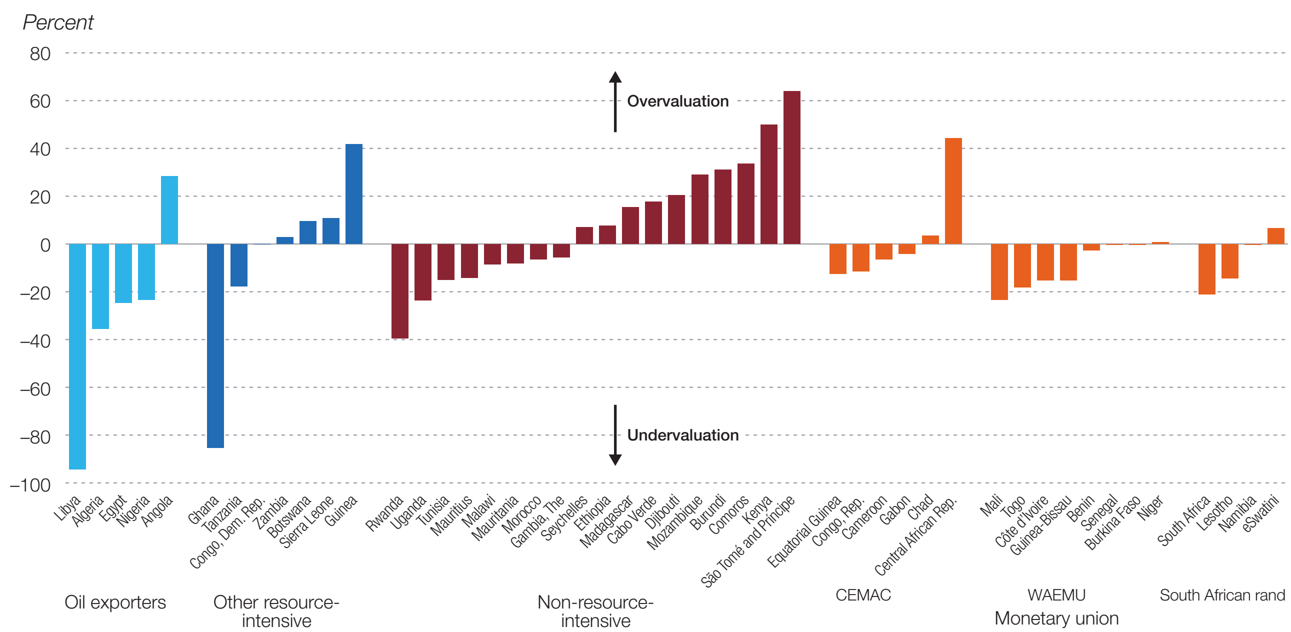
Source: Staff calculations.

The sharp fluctuations in African currencies, combined with record inflation in some countries, led to major currency misalignments
Currency misalignments—overvaluations and undervaluation—constitute imbalances between the effective exchange rate and its equilibrium level (annex 1.4). The series of global shocks since 2022—Russia's invasion of Ukraine, tightening monetary conditions, hyperinflation—have triggered exchange rate misalignments in African economies, though the degree of misalignment differs depending on the country's exchange rate regime and macroeconomic fundamentals (figure 1.25). These include the level of net foreign assets, productivity, terms of trade, and public spending, among others. In currency unions in which price stability played a relatively important role, the distortions were limited. The Central African Republic, for instance, experienced a 44.3 percent overvaluation due to a decline in net foreign assets and terms of trade. Most oil-exporting countries recorded a real undervaluation, with Libya experiencing the largest undervaluation in 2022. Other resource-intensive economies, such as Ghana, Guinea, Rwanda, and São Tomé and Príncipe, displayed varying economic conditions, with Ghana experiencing the highest undervaluation (85 percent), Guinea experiencing the highest overvaluation (23 percent), and Rwanda experiencing the highest appreciation.

Exchange rate misalignments are costly for growth, but real undervaluation is beneficial for economies with a large manufacturing sector

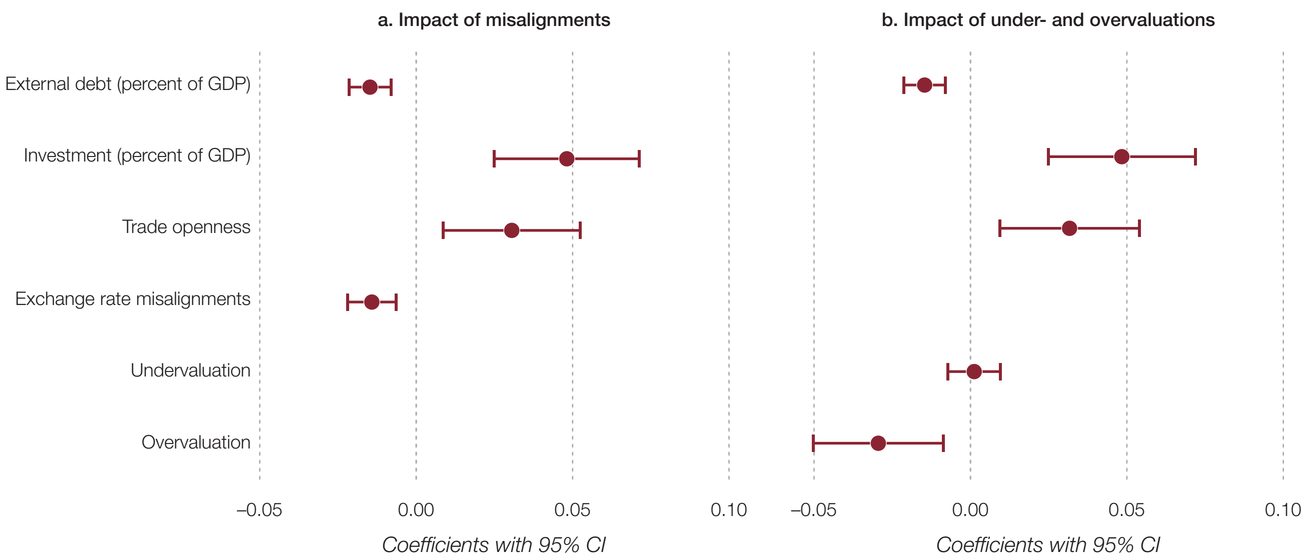
Exchange rate misalignments are costly for growth, but real undervaluation is beneficial for economies with a large manufacturing sector.
Exchange rate misalignment is detrimental to economic growth and trade.[6] An empirical analysis using a panel of 44 African countries over 1980–2022 shows that exchange rate misalignment has had a negative impact on economic growth in African countries. But the impact is asymmetrical, given that growth losses are mainly associated with loss of real competitiveness (figure 1.26). The analysis shows that undervaluation has a significant positive impact on growth, especially for countries with a large manufacturing sector (annex table 1.4.2). As part of the development strategy, many African countries provide incentives to foster growth of the manufacturing sector, seen as a precursor to structural transformation of these economies. Besides structural and targeted incentives such as tax breaks, maintaining price stability is also fundamental to improving the competitiveness of the manufacturing sector.

FIGURE 1.25 Exchange rate misalignments, 2022



Source: Staff calculations.

FIGURE 1.26 Impact of exchange rate misalignments on economic growth



Source: Staff calculations.

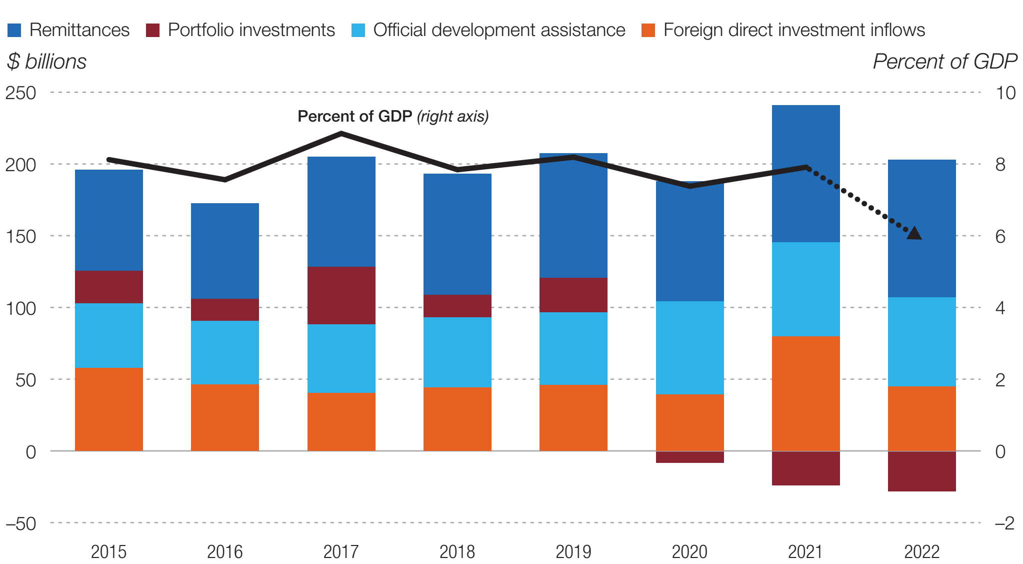
External financial flows, implications, and outlook

External financial flows to Africa have suffered from tightening global financial conditions and high uncertainty

External financial flows to Africa—foreign direct investment (FDI), official development assistance (ODA), portfolio investment and remittances—fell by 19.4 percent in 2022 to $174.9 billion, or 5.9 percent of Africa's GDP, from $217.1billion in 2021 (figure 1.27). This decline, reversing a strong immediate postpandemic recovery was broad-based. Foreign direct investment fell by about 44 percent), and the continent recorded net portfolio outflows of 17 percent and a reduction in ODA inflows of about 6 percent). Only remittances recorded a marginal increase of 0.2 percent.

After more than doubling to around $80 billion in 2021, FDI fell sharply in 2022 to almost

FIGURE 1.27 External financial flows to Africa, 2015–22



Source: African Development Bank statistics.

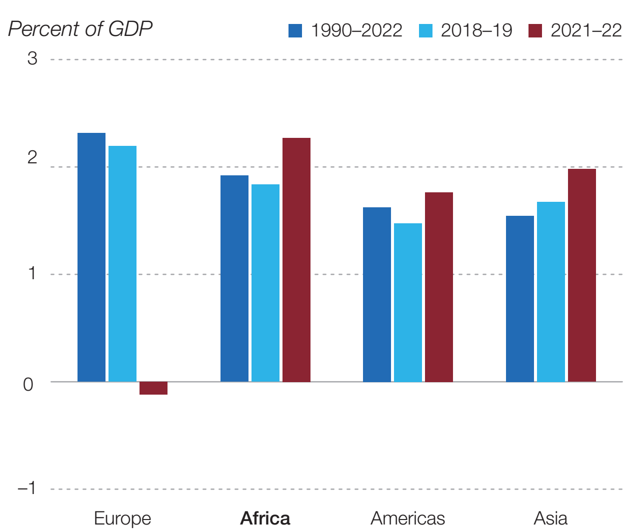
$45 billion[7] The decline was mainly driven by large corporate reconfiguration in South Africa, whose share of FDI in Africa more than halved from 49 percent in 2021 to 20 percent in 2022, around $32 billion less than in 2021. The FDI to Africa reflects the investors' risk perception due to increasing global uncertainty despite the continent offering comparably higher investment returns than other world regions.[8] Even though Africa's share of global FDI flows in 2022 was only 3.5 percent, down from 5.2 percent in 2021, its share of global FDI has increased since the 2000s, from an average of 2.8 percent in the first decade of the century to 3.3 percent in 2010–22.

FDI inflows to Africa have remained broadly buoyant relative to historical performance and the associated risks from the pandemic crisis and tightening global financial conditions

Despite the decline in FDI flows, the number of announcements of new projects increased by 39 percent to 766, suggesting that the fall in FDI in 2022 is due more to perceived risk than informed by macroeconomic and other fundamentals. The amount of announced greenfield investment projects for 2022 is estimated at $195 billion, compared with $52.1 billion in 2021, or nearly three times more. In addition, Africa accounted for 40 percent of the 15 main greenfield investment megaprojects globally (worth more than $10 billion) announced in 2022.[9] These megaprojects offer enormous opportunities for job creation, capacity building, and technology transfer. The energy sector, both extractives and energy generation, saw the largest growth. Since FDI growth is important for the continent's economic prosperity, priority must be given to policies that promote the attraction of more FDI by reducing the misperception of risk in Africa. This includes advocating the acceleration of reforms to the global financial architecture and the promotion of interregional investment flows, which generally remain blind to uncertainty.

Official development assistance (ODA) declined by 5.5 percent, from $65.6 billion in 2021 to $62 billion in 2022 due to the increasing global uncertainty since 2020, including geopolitical tensions and fiscal challenges facing major donor countries. Net portfolio investment outflows increased by 17 percent to reach $28 billion in 2022, compared with $24 billion in 2021, driven by the rise in interest rates in advanced economies and the depreciation of currencies in African countries. Compared with 2021, remittances withstood inflationary pressures in 2022 and remained the largest component of financial flows to Africa. They increased by 0.2 percent to $96 billion in 2022, of which 52 percent come from advanced economies and 48 percent from developing countries.

FIGURE 1.28 **Foreign direct investment in Africa and other regions**



Source: Staff calculations with data from UNCTAD Statistics.

Foreign direct investment is an important and complementary source of financing for Africa's economic transformation, but several challenges remain

Despite the ravages of COVID-19, FDI inflows to Africa have remained broadly buoyant relative to historical performance and the associated risks from the pandemic crisis and tightening global financial conditions. From 1990–2022, only Europe attracted more FDI as a proportion of GDP than Africa, averaging of 2.3 percent, compared with 1.9 percent for Africa, and 1.6 percent for the American and Asian continents (figure 1.28). Prior to COVID-19, the share of FDI in GDP was declining in relation to historical levels for all world regions except Asia. The decline was more pronounced in Europe and America. Africa's performance in the post-COVID era is particularly notable, with FDI as a percentage of GDP increasing by 24.5 percent over the two years preceding the pandemic. In contrast, foreign investment grew by 17.5 percent in Asia and was stagnant in America, with Europe experiencing a sharp drop of more than 100 percent.

Volatility in FDI is harming development of the manufacturing sector

Foreign direct investment is critical to the development of Africa's manufacturing sector and in fostering structural transformation, because it brings new capital, technologies, and skills. Historically, FDI has been more stable and resilient to shocks than portfolio investment. But the severity of shocks over the past 3 years triggered uncertainty and volatility in FDI. Rising FDI volatility is detrimental to manufacturing activity and creating sustainable jobs. The volatility of FDI and the lack of private sector financing constitute two main obstacles to the development of Africa's manufacturing sector (figure 1.29). Political stability and the absence of violence and conflict, as well as good governance and price stability are also key challenges that African economies need to address to ensure the stability of FDI, essential for the industrial sector. Further, while bank financing to the private sector approaches 100 percent of GDP globally, it is below 30 percent in Africa. It is therefore crucial that the banking sector becomes more involved in financing private sector activity in Africa.

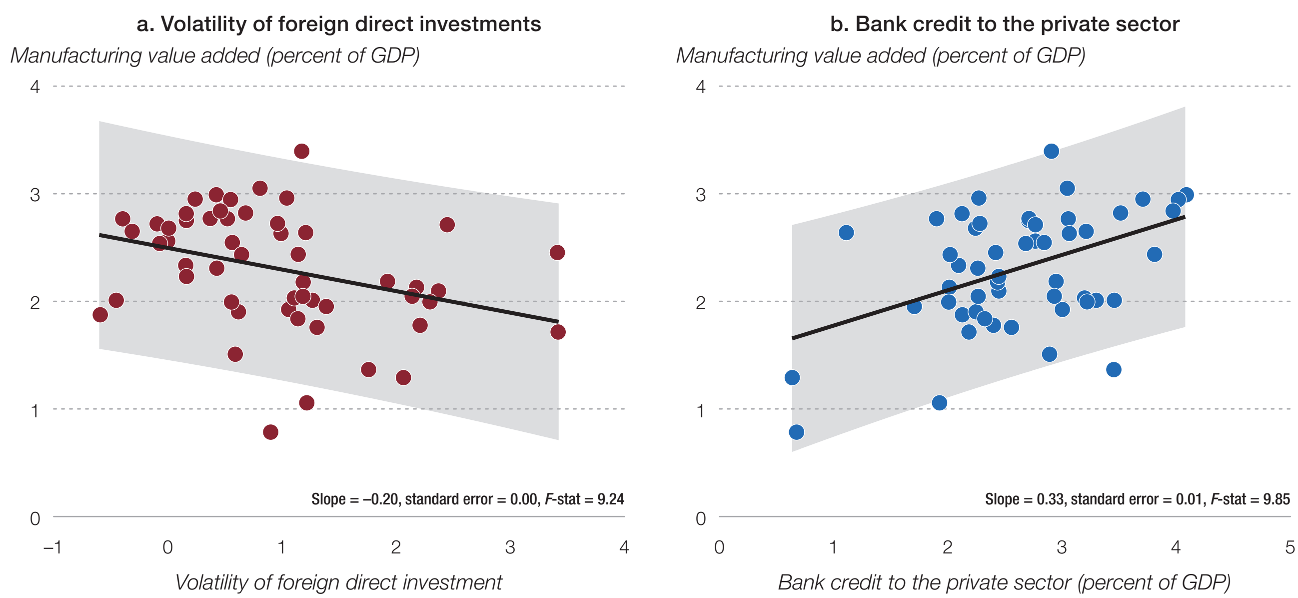
Official development assistance has not met the challenge of getting African economies out of debt, and several countries have contracted the aid curse

Official development assistance to Africa has been volatile and largely on a downward trend. The decline, which highlights shrinking fiscal space in source countries, has drawn African countries facing a funding squeeze toward external borrowing with the share of non-concessional debt increasing over time (see figure 1.27). This evidence is supported by empirical analysis showing that ODA has not helped African countries escape of the burden of debt. On the contrary, ODA appears to be positively and significantly associated with the increase in budget deficits and public debt. Empirical evidence shows that a one percentage point increase in ODA (as a percentage of GDP) leads to an increase in the debt ratio of 1.90 percentage points and an increase in the budget deficit of 0.67 percentage points (annex 1.4).

Despite the conditions attached to ODA disbursement, the support has not helped African countries control their expenditure. For example, from 1990 to 2022, 19 African countries received ODA of more than 10 percent of GDP, and 15 of them did not

Rising FDI volatility is detrimental to manufacturing activity and creating sustainable jobs

FIGURE 1.29 **Volatility of FDI, bank financing of the private sector and the manufacturing sector**



Note: FDI volatility for each country represents the standard deviation of FDI over the period 1980–2022. Bank credit to the private sector (percent of GDP) as well as the value added of the manufacturing sector (percent of GDP) are averages over the 1980 period. To facilitate the interpretation of the coefficients in terms of elasticity, all variables are expressed in logarithm.

Source: Staff calculations.

show evidence of improved fiscal performance—for either of three possibilities: public expenditure increased faster than revenue, public expenditure decreased less rapidly than revenue, or expenditure increased while revenue decreased. Only in Rwanda, with 19 percent ODA as share of GDP, did revenue grow faster than public expenditure.

This evidence suggests that most African countries have become trapped into the aid syndrome resulting in more spending increases or less efforts to mobilize domestic resources, or a combination of both. To create ownership of Africa's development process, there is need to rethink the current model of the aid architecture, focusing more on supporting countries' investments in growth and job-creating sectors. International support should focus more on transferring technology and skills and building capacity to mobilize domestic resources.

Remittances are currently the largest and most stable source of external funding in Africa, estimated at 3.2 percent of GDP in 2022, higher than that of Latin America and the Caribbean

Remittances are concentrated in a limited number of countries, requiring proactive strategies from others to harness its full potential

Remittances are currently the largest and most stable source of external funding in Africa, estimated at 3.2 percent of GDP in 2022, higher than that of Latin America and the Caribbean. However, remittances to Africa are dwarfed by those to South Asia, at 4 percent of GDP, suggesting substantial room for the continent to attract more resources from its diaspora, especially as the majority of remittances received by Africa are concentrated in few countries and intra-Africa migration is higher than extra-Africa emigration. Egypt and Nigeria together accounted for more than 50 percent of the $96 billion total remittances received in 2022, representing 6 percent and 4.3 percent of their GDP respectively. This is not an isolated phenomenon, as these two countries have consistently received more than half of the continent's remittances in the last five years. While country size matters—Nigeria and Egypt are the most populous countries in Africa—the strategy to actively involve the diaspora in development financing is more important. For instance, Senegal, smaller than Egypt and Nigeria in economic size and population, attracts remittances of up to 10 of GDP a year, largely because of the country's proactive policy toward the diaspora (box 1.2).

BOX 1.2 Senegal's winning strategy to attract more remittances

Senegal, with a population of 17.3 million, has seen remittances from the diaspora exceed 10 percent of GDP over the last decade, accounting for over 50 percent of the state budget. The diaspora, comprising around 700,000 people, contributes to the construction of schools, maternity wards, and water distribution infrastructure. Remittances are a crucial source of income and poverty reduction for many Senegalese households, especially in rural areas. With over 55 percent of remittances coming from France, Italy, and Spain, they contribute to Senegal's balance of payments, stabilize the national currency, and mitigate external shocks on the economy.

The Senegalese model of involvement of the diaspora in the country's economic and social development is a model of success, with initiatives such as the support Program for Solidarity Initiatives for Development (PAISD), the Fund to support the Investment of Senegalese Abroad, and the Haut council of Senegalese abroad. Since 2012, nearly $25 million has been mobilized to support investment by the Senegalese diaspora.

Africa's diaspora has immense funding potential, potentially mobilizing $80 billion annually in remittances. To harness this, countries must invest in creating bridges with diasporas, creating ministries involving them in political institutions, and creating ministries for promoting their contribution to economic and social development through financial, technological and skills transfers. Encouraging diaspora bonds and implementing appropriate institutional frameworks can also help secure investment and support sustainable development.

DEBT VULNERABILITIES AND IMPLICATIONS FOR DEBT RESTRUCTURING

Debt dynamics and implications for growth

Public debt is declining but still above the prepandemic level

A recent path toward the normalizing fiscal policy in many African countries is helping to gradually put public finances on a strong footing. The COVID-19 pandemic and its repercussions shaped public finances in the last four years and continued to have a bearing even as severe effects of the pandemic receded. In 2020, the median fiscal deficit expanded to 6.8 percent of GDP from 5.2 percent in 2015–19, owing to the impact of the pandemic on revenues and the need to protect the most vulnerable. Consequently, Africa's median public debt-to-GDP ratio increased to 64 percent in 2020, from 54.5 percent in 2019 (figure 1.30). After providing extraordinary support during the pandemic and then during the Russia's invasion of Ukraine, fiscal policy is returning to normal as most countries entered the polycrisis with limited fiscal space to maintain public support to the economy, and most authorities have since started to consolidate. As a result, the debt-to-GDP ratio stabilized at around 63.5 percent in 2021–23 and is projected to decline to around 60 percent starting 2024—halting an almost decade-long upward trend.

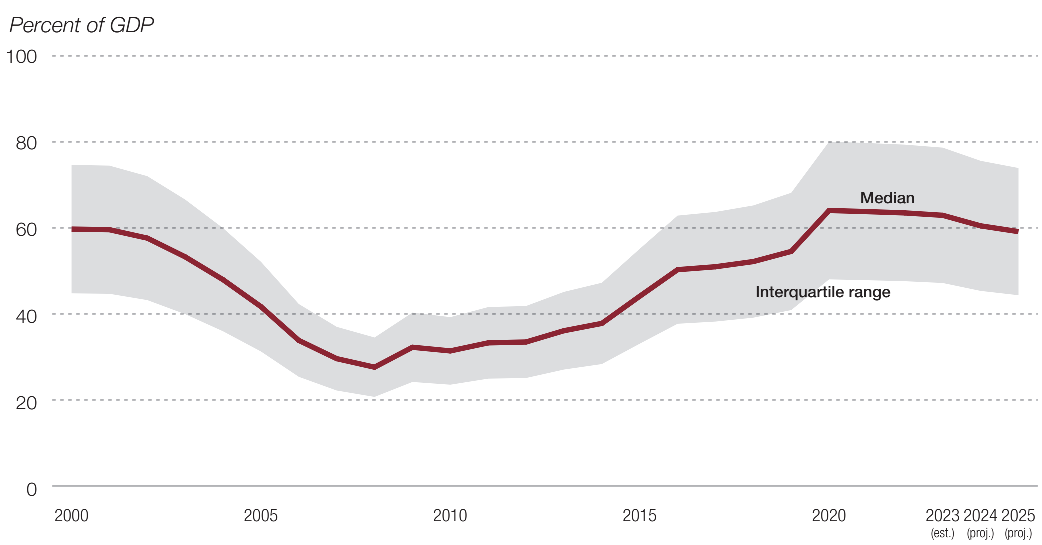
While the debt-GDP ratio is stabilizing continent-wide, in many countries the ratio is still elevated and above the prepandemic levels, underpinned by volatility in public finances, higher interest rates (box 1.3), and reflecting the impact of shocks and government actions to mitigate against these shocks (figure 1.31). However, the ratio of public debt in 10 African countries is expected to decline in 2023 and 2024 to below the prepandemic level. The most significant decline is in São Tomé & Príncipe (39.6 percentage points), followed by Angola (29 percentage points), Ethiopia (18 percentage points) and The Gambia (11 percentage points). The decline in debt in these countries is due to general fiscal consolidation. And in some countries (Angola and The Gambia), it reflects the benefits of significant energy subsidy reforms that created space and improved fiscal balances, reducing the incentive to take on more debt relative to historical levels.

Challenges and vulnerabilities remain

Despite the projected overall decline in the debt ratio, significant challenges remain due to increased vulnerabilities stemming from marked

A recent path toward the normalizing fiscal policy in many African countries is helping to gradually put public finances on a strong footing

FIGURE 1.30 Gross government debt as a share of GDP, 2010–25



Source: Staff calculations based on the World Economic Outlook database 2024.

BOX 1.3 **Drivers of debt dynamics in Africa**

The impact of the drivers of debt dynamics in Africa is estimated by linking the debt-to-GDP ratio to its standard determinants and augmented with other control variables. The empirical analysis relies on annual panel data covering 47 African countries from 1998 to 2021. It follows a two-step generalized method of moment (GMM), which combines the instrumental variables (IV) method and the generalized least squares (GLS) method. The two-step method produces convergent and robust estimates. The Sargan-Hansen test is used to test the validity of the instruments. The Arellano-Bond (1991) postestimation test also tests the presence of autocorrelation.

The results show that a one-percentage point increase in interest rate leads to nearly three-percentage-point increase in the median debt-to-GDP ratio of countries in the sample. As the economy grows faster than rate of debt accumulation and higher than the interest rate at which such debt is contracted, the debt-to-GDP ratio tends to increase but at slower pace. This is corroborated by the estimation in box table 1.3.1. A one-percentage point increase in real GDP growth is reflected in about a one-percentage-point decline in the median debt-to-GDP ratio. By investing borrowed resources in transformative projects or in highly productive sectors, governments can expand the economic base and accelerate growth at a rate faster than the interest rate on debt. This growth-interest rate differential is fundamental to the resolution of the debt conundrum in African countries, especially under current conditions, when the cost of borrowing has significantly increased.

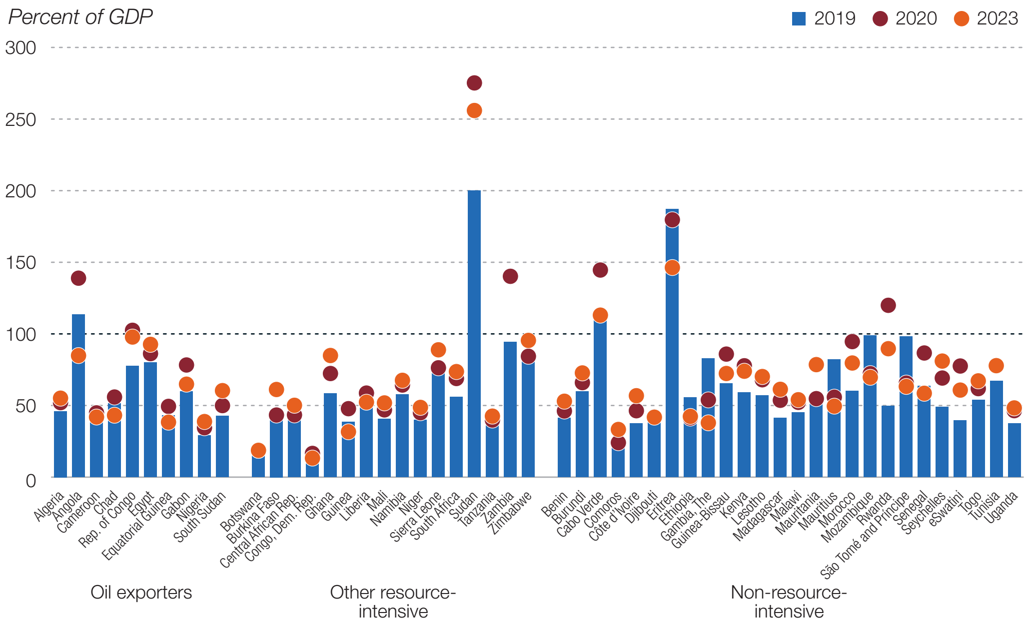
BOX TABLE 1.3.1 **Long-run estimates outcomes GMM system model**

	Dependent variable: Debt-to-GDP		
	Long-run coefficients		
	(1)	**(2)**	**(3)**
Lagged debt-to-GDP	0.74***	0.58***	0.68***
Interest rate	2.7***	3.22***	2.69***
Real GDP growth rate	–1.12***	–0.97**	–0.55*
Primary balance		–1.97***	–1.53***
External debt-to-GDP	1.00***	0.69***	1.04***
Squared external debt-to-GDP	–0.001***		–0.001***
Lagged debt-to-GDP growth	20.17***	38.49***	23.98***
Inflation	0.20***	0.24***	0.28***
Exchange rate appreciation	0.01***	0.01***	0.01***
Trade openness	–0.29***	–0.23***	–0.16***
FDI-to-GDP		–0.22***	–0.38***
Seigniorage	–0.01***	–0.01***	–0.004***
Population growth	–3.1***	–6.72***	–3.05***
Gov. effectiveness	–0.64***	–0.56***	–0.51***
Control of corruption	0.2***	0.10	0.11
Constant	42.02***	52.49***	28.1***
Observations	282	282	282
Wald-p-value	0.0000	0.0000	0.0000
Sargan p-value	1.0000	1.0000	1.0000
AR1 p-value	0.0408	0.0235	0.0193
AR2 p-value	0.4572	0.4152	0.8894

Note: Z statistics are in parentheses. *, **, and *** denote significance at the 10, 5, and 1 percent confidence level, respectively.

Source: Staff calculations.

FIGURE 1.31 Change in debt-to-GDP ratios, 2019–23

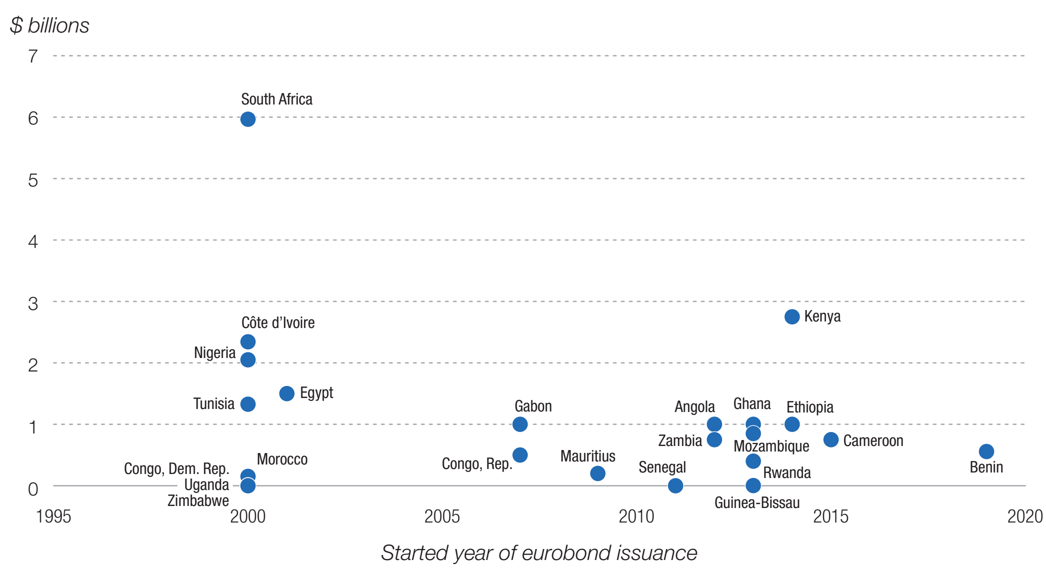


Source: Staff calculations based on the World Economic Outlook database 2024.

shifts toward market-based financing. Seven African countries made their debut in the international capital market in the 2000s (figure 1.32). However, most eurobond issuances started between 2009 and 2014 when accommodative global financial conditions and the search for positive real yields prevailed, underpinned by improved macroeconomic conditions in Africa following the Heavily Indebted Poor Countries (HIPC) debt relief initiative, which facilitated larger volumes of financing to African countries. Further, the 2014–16 collapse in oil prices and wider primary fiscal deficits in oil-rich countries also led to growing financing needs, pushing some countries, including Angola

The ratio of public debt in 10 African countries is expected to decline in 2023 and 2024 to below the prepandemic level

FIGURE 1.32 Start year of eurobond issuance by African countries



Source: Staff calculations using data from World Bank International Debt Statistics, 2024.

and Cameroon, to issue their first eurobonds in 2012 and 2015, respectively. Overall, between 2000 and 2021, 23 African countries issued more than 125 eurobond instruments valued at over $1.51 trillion.

Moreover, most public and publicly guaranteed (PPG) external debt in Africa is denominated in US dollars and the share has increased over time. Since 2014, US dollar denominated debt accounted for a minimum of 65 percent of Africa's outstanding PPG debt. As of 2022, the share stood at 70 percent compared with 14.5 percent for the euro, while other currencies accounted for 15.5 percent (figure 1.33). The dominant role of the US dollar highlights the vulnerabilities many African countries face with the strengthening of the US dollar since the tightening of global financial conditions.

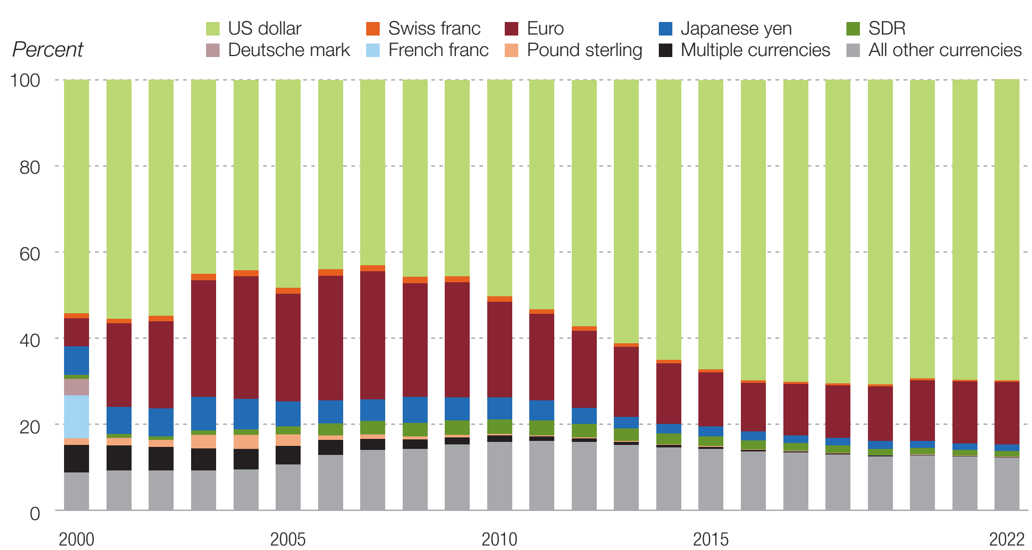
The dominant role of the US dollar in public and publicly guaranteed external debt highlights the vulnerabilities many African countries face with the strengthening of the US dollar since the tightening of global financial conditions

Domestic and external debt arrears present another source of debt vulnerabilities in many African countries

Domestic debt arrears are a form of forced financing of government deficits where debt repayments to domestic suppliers and creditors are rescheduled while the government continues to roll over domestic debt. While not paying suppliers and forcing them to become creditors may free up funds to help cover financing needs, long delays in domestic arrears clearance can be damaging to the private sector and can also lead to stress on the banking sector, with negative ramifications for growth. Arrears also undermine trust in government and the effectiveness of fiscal policy.

According to a recent survey covering 2005–18, at least 70 percent of countries in all Africa regions (excluding North Africa) had domestic arrears estimated at 3.3 percent of GDP at the end of 2018, with a maximum of 18 percent of GDP in the Republic of Congo.[10] Domestic arrears are particularly high in oil exporters (about 8.5 percent of GDP), countries with a fixed exchange rate regime (4.4 percent), and countries in state of fragility (4.1 percent) (figure 1.34). In addition, the survey finds that countries with a higher level of public debt and a weaker Debt Sustainability Analysis (DSA) risk rating tend to have more arrears. The breakdown shows that domestic arrears owed to private suppliers of goods and services are the most common, representing on average 53 percent in all countries. In contrast, wage arrears are rare and occur mainly in countries experiencing severe political instability or large balance of payment imbalances. It is likely that the large fiscal deficits in the previous four years have led to the accumulation of more domestic debt arrears given the growing financing needs and difficult access to external financing.

FIGURE 1.33 Currency composition of public and publicly guaranteed external debt (percent of total PPG external debt), 2000–22

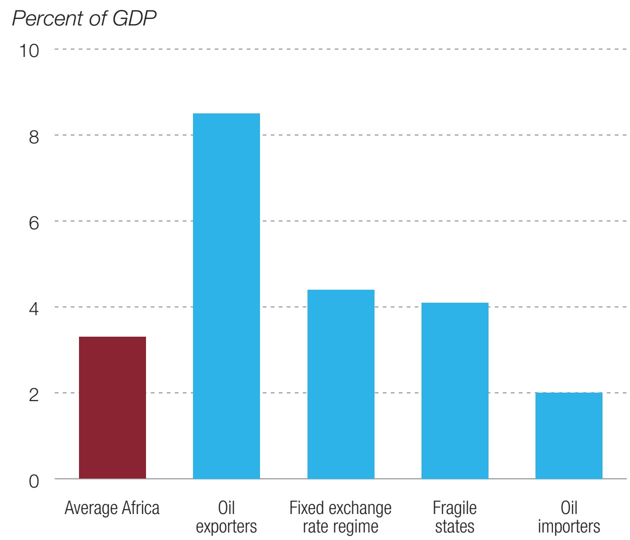


Source: Staff calculations using data from World Bank International Debt Statistics 2024.

Reflecting the trend of total government debt and the lack of fiscal capacity to service maturing debt, external debt arrears accumulation continues to be significant in many Africa countries (figure 1.35). External debt arrears steadily declined between 2004 and 2011 from $44.9 billion to $27.6 billion in part due to the debt relief provided to 34 African countries. Since 2014, arrears on external debt have been on the rise, however, from $29.2 billion in 2014 to $44.1 billion at the end of 2022. While in nominal terms debt arrears continued to accumulate since 2014, total external arrears as a percentage of gross national income have remained relatively stable since 2014 at around 1.6 percent after sharply declining from 7.9 percent in 2001. Despite this decline, debt arrears constitute a burden for many governments, adding to debt service cost, which already diverts government revenue and reduces fiscal space (see figure 1.35). For instance, if outstanding debt arrears of $44 billion at the end of 2022 were to be cleared in full, Africa would have to pay $118 billion, which includes the $74 billion in debt service due in 2024. This figure represents 21 percent of annual revenues (or 4 percent of GDP) in 2023.

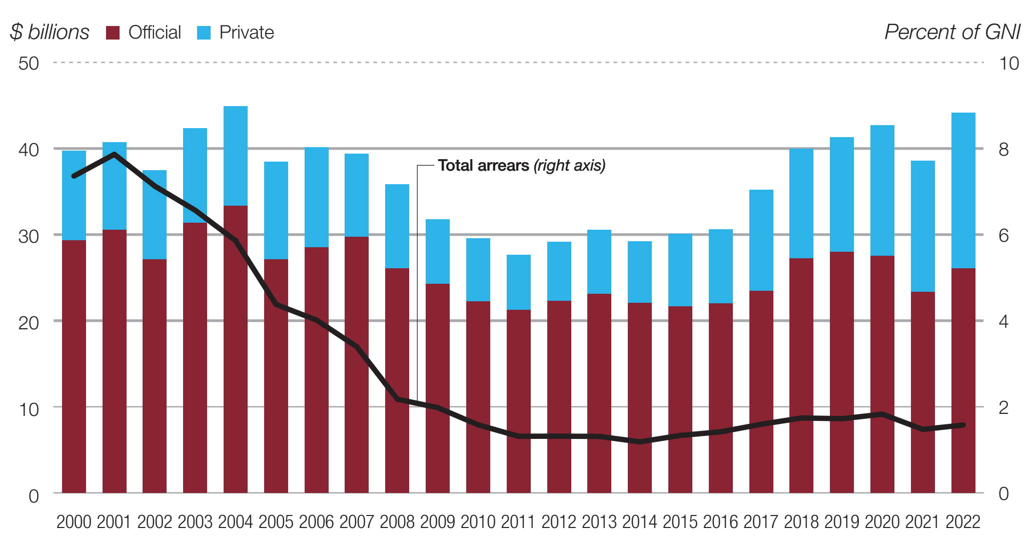
Missed payments to official creditors have been more significant than arrears to private creditors. At the end of 2022, arrears to official creditors represented 59 percent of arrears on total external debt. The greater amount of arrears to official creditors than private creditors is explained in part by the seniority structure of sovereign debt. Indeed, private creditors are typically paid first and lose less than bilateral official creditors. Multilateral institutions such as the African Development Bank, IMF, and World Bank are also senior creditors. In contrast, official bilateral (government-to-government) debt is subordinated (junior) to other debt.[11]

FIGURE 1.34 **Stock of domestic debt arrears by country group, 2018**



Source: Staff calculations using data from the IMF regional economic outlook, 2019.

FIGURE 1.35 **Private and official external debt arrears, 2000–22**

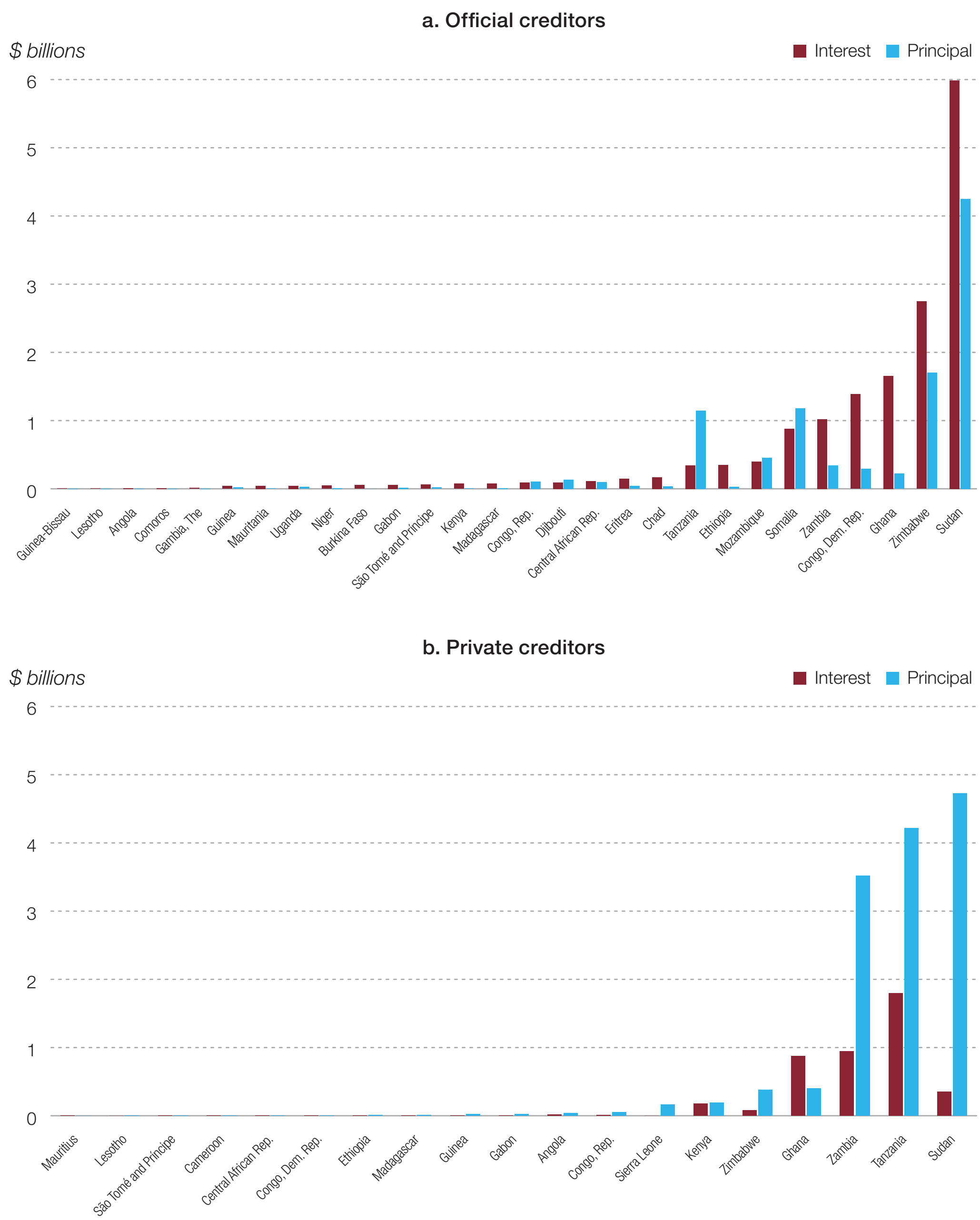


Source: Staff calculations using data from World Bank International Debt Statistics, 2024.

Countries with the highest external debt arrears—both in principal and interest payments—owed to official creditors at the end of 2022 were Sudan, Zimbabwe, Ghana, the Democratic Republic of Congo, Zambia, Tanzania, and Somalia in descending order (figure 1.36a). Together these countries accounted for about half of the total official arrears. Principal arrears dominate interest arrears in all countries except in Djibouti, Mozambique, Somalia, and Tanzania, an indication that most countries missed payments on principal to official creditors. At the end of 2022, Zimbabwe's external debt arrears to official creditors stood at $4.4 billion, representing about 94 percent of total external debt. Likewise, Sudan's external arrears to official creditors were $10.2 billion as at the end of

Debt arrears constitute a burden for many governments, adding to debt service cost, which already diverts government revenue and reduces fiscal space

FIGURE 1.36 External interest and principal arrears, as at end 2022



Source: Staff calculations using data from World Bank International Debt Statistics, 2024.

2022, accounting for about 67 percent of external debt. The Zimbabwe case is an indication that the bulk of the current fiscal and balance of payment issues facing the country is due to arrears accumulation. The importance of arrears as a driver of debt sustainability in many African countries highlights the need for a comprehensive arrears clearance strategy or debt restructuring to allow these countries to regain access to new financing from official creditors. It also highlights the need for pre-emptive debt restructuring before default materializes.

For arrears to external private creditors, Sudan has the highest amount (figure 1.36b). At the end of 2022, arrears to private creditors stood at $5.1 billion, representing 33 percent of total external debt. Adding the arrears to official creditors (67 percent of external debt), the bulk of total external debt in Sudan is composed of arrears. Tanzania, Zambia, the Republic of Congo, and Angola are, in this order, countries that have missed the highest principal and interest payment to external private creditors after Sudan. Arrears accumulation due to private creditors in Tanzania amounted to $6 billion, representing 31 percent of total external debt. For Zambia, arrears to private creditors totaled $4.4 billion, representing 27 percent of total external debt.

While domestic arrears can distort the domestic economy, external arrears can reduce access to new external financing, from both private and official creditors. For instance, multilateral external arrears in many countries have reduced access to concessional financing from international financial institutions, with the normalization of relationship in many cases subject to arrears clearance before a country can regain access to new financing. In a country like Zimbabwe, this has turned a solvency problem into a liquidity crisis, resulting in exchange rate pressures and hyperinflation, highlighting the need for reforms of the international financial architecture to provide more flexibility for countries that have accumulated arrears and are in dire need of emergency financing.

Global financial conditions and implications for debt restructuring

Tighter global financial conditions have increased borrowing costs

The wave of global interest rate hikes that started in July 2022, the ensuing elevated sovereign debt spreads, and the exchange rate depreciations have raised borrowing costs and shut most market-access countries from international capital markets. The average sovereign spreads in Africa have soared—to three times the emerging market average since the beginning of the tightening cycle (figure 1.37). As a result, debt service costs have

The wave of global interest rate hikes that started in July 2022, the ensuing elevated sovereign debt spreads, and the exchange rate depreciations have raised borrowing costs and shut most market-access countries from international capital markets

FIGURE 1.37 Africa sovereign spread and global emerging market bond index (EMBI)

Source: Staff calculations based on Haver Analytics.

risen, and 20 African countries were in debt distress or at high risk of debt distress in February 2024.

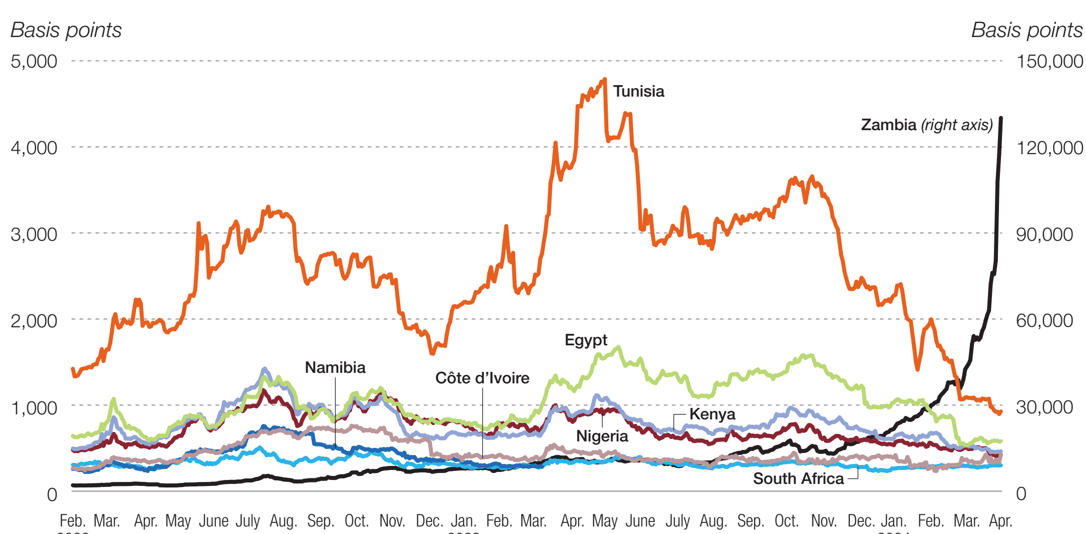
The pause in global financial tightening that started toward the end of 2023 have eased sovereign spreads from their peak in October 2023. Indeed, the first quarter of 2024 has seen a further narrowing of the spread, but borrowing costs remain elevated compared to their precrisis levels. As a result, no eurobond was issued between April 2022 and the end of 2023. However, the first quarter of 2024 saw a return of African countries to the eurobond markets with the successful eurobond issuances by Benin, Côte d'Ivoire, and Kenya. Indeed, Côte d'Ivoire became the first African country to re-enter the market post COVID-19, issuing $2.6 billion in eurobonds in January 2024 to repurchase and refinance its existing eurobonds. Kenya issued a new $1.5 billion eurobond in February 2024 to buy back the $2 billion eurobond due June 2024. The coupon rate on the new issuance was higher than the 6.875 percent on the eurobond maturing in 2024. In March 2024, Benin completed a buyback of its €176.36 million debt outstanding due in 2026 with 5.75 percent interest rate and €700 million debt outstanding due in 2032 with 4.875 percent interest rate.[12] If successful, Nigeria will most likely be the fourth country to issue a eurobond in 2024.[13] The Kenya example is not unique and shows the growing cost of external financing compared with the pre-pandemic era, even though sovereign spreads are gradually declining.

Reflecting the sovereign bond spreads, interest rates on public external debt are higher in African countries than other developing regions, and significantly lower in advanced economies

The country-level sovereign spread reflects the continental trend (figure 1.38). Indeed, except for Zambia, where the spread has been on an upward trend since the pause in global interest rate hikes in October 2023, all countries have experienced a narrowing of their sovereign spread. For instance, in Egypt, the 10-year bond yield spreads have narrowed by 997 basis points (bps) since then. And Nigeria, which introduced fuel subsidy reforms and fiscal consolidation measures, had its spread fall by 326 bps, but in South Africa, it has increased by 53 bps. Despite the decline in sovereign spread in many countries, the yield remains higher than precrisis levels. For non-debt distressed countries, the average yield on outstanding eurobonds was over 12 percent since Russia's invasion of Ukraine in 2022, up from 7 percent before the pandemic. For distressed countries, the yield has more than doubled compared to the pre-crisis level. For instance, the yield on an outstanding eurobond for Ghana was 21.7 percent compared with 9 percent before Russia's invasion of Ukraine.

Reflecting the sovereign bond spreads, interest rates on public external debt are higher in African countries than other developing regions, and significantly lower in advanced economies. For

FIGURE 1.38 Sovereign spreads in selected African countries



Source: Bloomberg.

example, data on the interest rate on new external commercial debt from 2010 to 2022 show that the average eurobond for African countries was issued at 4.7 percent (figure 1.39). And interest rates in 22 African countries exceeded 5 percent. According to a recent IMF study, the average yield on the African sovereign eurobond was above 5 percent in 2021, and in 6 countries, above 8 percent.[14] For comparable developing economies from Latin America and the Caribbean, South Asia, and East Asia and Pacific, the interest rate on new commercial debt was 4.3 percent, 3.5 percent, and 4 percent respectively (see figure 1.39). This contrasts with the average interest rate of outstanding sovereign debt in advanced economies which fell to around 1 percent in 2021.[15] The relatively high sovereign bond yield in Africa is often due to unfair risk perception but also to domestic and other external factors.

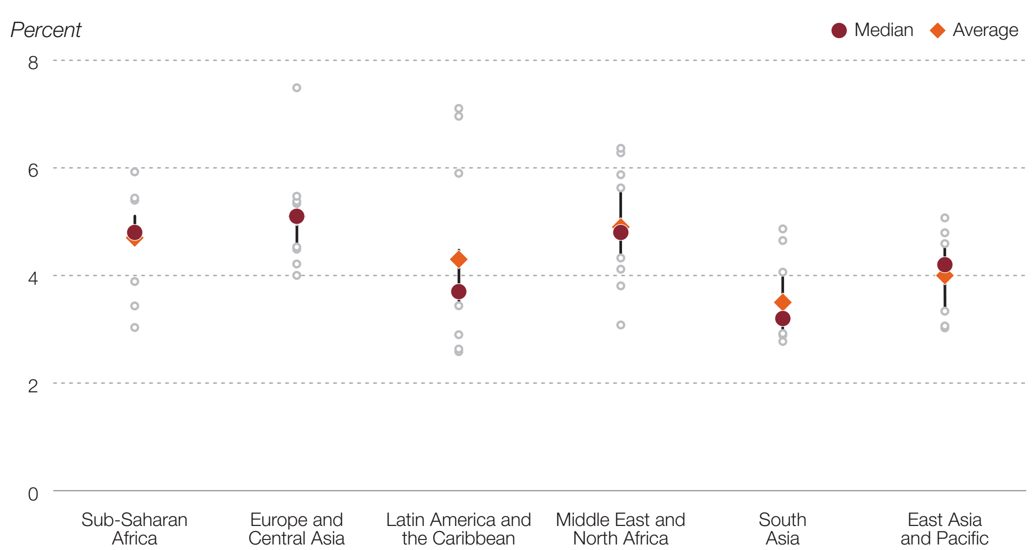
The implication is that while developed countries can sustain high levels of debt with low debt service burdens, developing countries, particularly the most vulnerable among them, are devoting an increasingly large proportion of their fiscal resources to servicing public debt. Therefore, reforms of the international financial architecture, especially multilateral development banks are key to providing low-cost concessional financing to African countries. Indeed, while the average interest rate on new external commercial debt commitment for Africa is 4.7 percent, that on new external concessional debt commitment is 1.8 percent, about 3 percentage points lower than the market rate (figure 1.40).

Debt burdens weigh on public finances, diverting resources away from infrastructure investment, thus constraining future GDP growth

Debt service costs have risen, narrowing the scope for government spending, and increasing debt vulnerabilities. External debt service payments as a proportion of government revenues have risen above the prepandemic level in many countries (figure 1.41). The median debt service on external debt as a percent of government revenue for 49 countries with data rose from 6.8 percent over 2015–19 to 10.6 percent over 2020–22. Resources channeled toward debt service have eroded fiscal space, further constraining government capacity to invest in growth-promoting sectors and human capital development—education and health, two areas where average public expenditure on the continent is below that for comparator regions. Between 2010 and 2019, average public expenditure on education in Africa was 3.6 percent of GDP, below the world average of 4.2 percent of GDP. Public spending on health in Africa was even lower at 1.8 percent

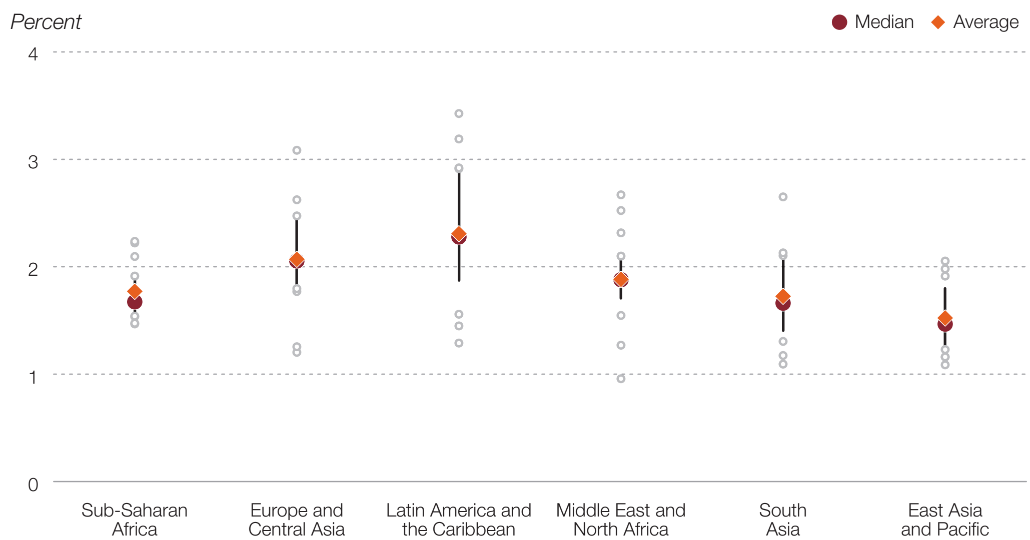
While developed countries can sustain high levels of debt with low debt service burdens, developing countries, particularly the most vulnerable among them, are devoting an increasingly large proportion of their fiscal resources to servicing public debt

FIGURE 1.39 **Interest rate on new external debt commitment, private**



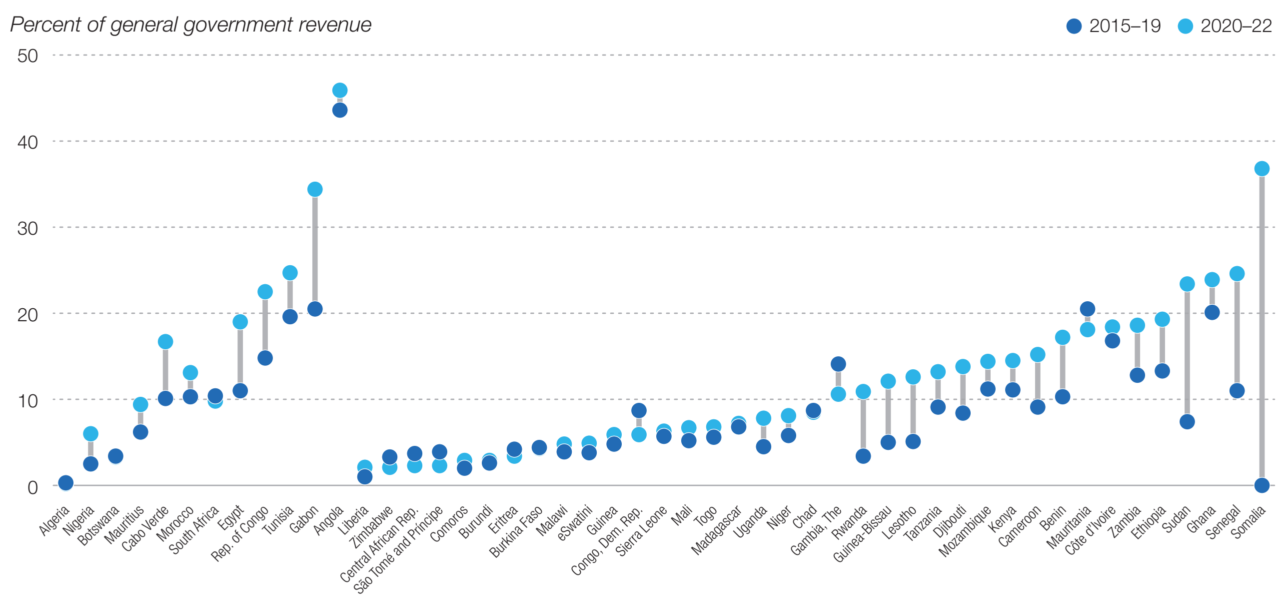
Source: Staff calculations using data from World Bank International Debt Statistics.

FIGURE 1.40 Interest rate on new external debt commitment, official



Source: Staff calculations using data from World Bank International Debt Statistics.

FIGURE 1.41 Debt service on external debt, in percent of general government revenue



Source: Staff calculations using data from World Bank International Debt Statistics.

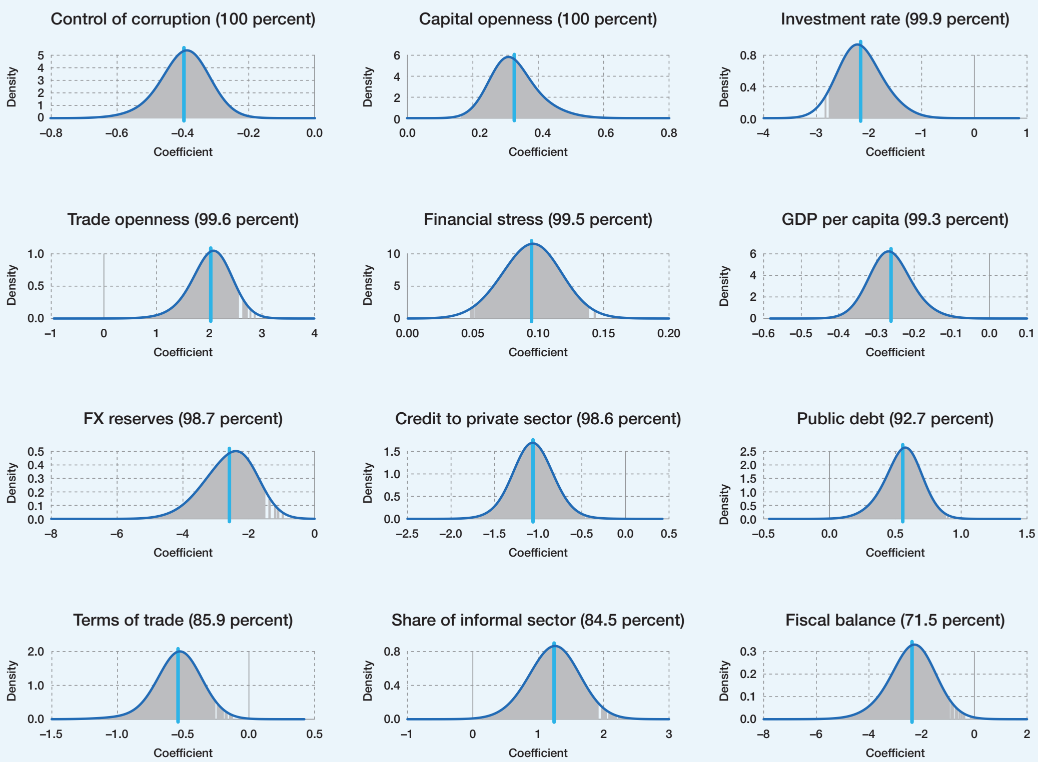
of GDP, compared with 4.5 percent for Asia and the Pacific and 3.9 percent in Latin America and below the global average of 5.8 percent. For all 49 countries, debt service cost was higher in 2020–22 (averaging 12.7 percent), than in 2015–19, (at 8.4 percent), except in Chad, the Democratic Republic of Congo, The Gambia, and Mauritania.

Debt service payment costs have increased significantly in tandem with the rising share of debt owed to private creditors. This is a cause for concern because current debt restructuring processes to reach agreement with private creditors have been protracted, creating uncertainty among borrowers and undermining credibility of the G20 Common Framework. In 2024, African

BOX 1.4 **The determinants of African sovereign yield spreads**

Sovereign bond spreads are influenced by a range of internal and external factors—related to macroeconomic, financial as well as political, institutional and governance conditions. The contribution and weight of each factor may differ significantly from one region to another, and modeling choices also influence the robustness of potential relationships. To address these issues and identify key determinants for African countries, we use the BMA method by estimating all possible combinations of determinants to rank them by order of importance (box figure 1.4.1). Figures in brackets for each variable give the probability of explaining the default risk by such variable. By order of importance, control of corruption, degree of capital account openness, investment-to-GDP ratio, the degree of trade openness, financial stress, the level of the country's development, the ratio of foreign exchange reserves to GDP, and credit to the private sector are the most robust factors explaining sovereign risk. They appear to be robust, with a probability close to 100 percent in explaining the default risk of African countries. In addition, the debt-to-GDP ratio, terms of trade shocks, and size of the informal sector in the economy explain sovereign risk with a probability of more than 80 percent.

BOX FIGURE 1.4.1 **The most robust determinants of sovereign yield spread and the cumulative density function of their coefficients**



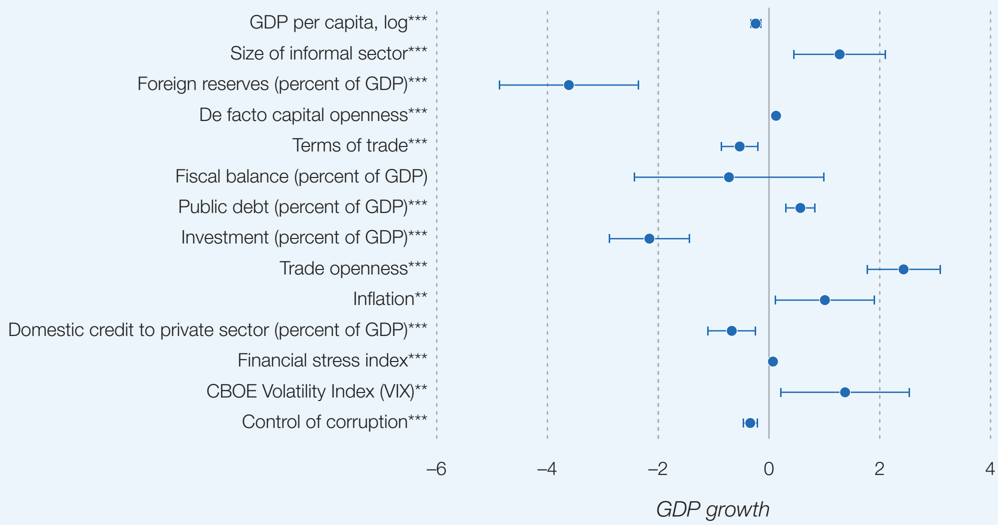
Source: Staff calculations.

Using this information, we then perform panel OLS regressions over the period 2014–22 for the 16 African countries for which data are available (box figure 1.4.2).

(continued)

BOX 1.4 **The determinants of African sovereign yield spreads** *(continued)*

BOX FIGURE 1.4.2 **Impacts of the most robust determinants on the yield spread**



Results from the model are intuitive. Factors that drive interest rate spreads down are GDP per capita, size of foreign exchange reserves, terms of trade, investment, domestic credit to the private sector, and control of corruption. A higher GDP per capita translates into higher incomes and therefore a greater ability to tax incomes and generate the fiscal revenues needed to service the debt. Large foreign reserves and favorable terms of trade are signs of the strength of external positions and trade competitiveness, both of which contribute to strong income growth and fiscal receipts. High levels of investment and credit to the private sector reveal a forward-looking economy devoting resources to capital accumulation, infrastructure, and productivity growth, all of which present favorable risk assessment by investors. Finally, less corruption is associated with more functional and accountable fiscal authorities, and therefore presents probability of a lower risk premium, as found by the OLS model.

By contrast, factors contributing to rising interest rate spreads are public debt as a percentage of GDP, inflation, capital and trade openness, the size of the informal sector, and the financial stress and VIX indexes. The higher ratio of public debt means more fiscal revenues will be devoted to interest and debt repayments, making additional loans more risky and therefore more expensive. Similarly, higher inflation is often associated with debt monetization, which is also a sign of excess government spending translating into a higher risk premium. The size of the informal sector is both a drag on fiscal revenues and associated by investors with a riskier investment environment, converting into a higher risk premium too. Greater financial stress around the world means an Increase in risk-averse behavior materializing into investors asking for higher yields in compensation for their investment. As for capital openness, it may be interpreted as a sign of vulnerability to sharp swings in capital flows that risk destabilizing the economy. Finally, trade openness may reflect the importance of primary commodity exports in the country's GDP, which is also a risk factor due to fluctuating commodity prices.

countries are expected to spend around $74 billion on debt service, up from $17 billion in 2010, of which $40 billion is owed to private creditors, representing 54 percent of total debt service (figure 1.42). Refinancing risks could further increase in 2024, especially for countries with large bullet redemptions including Angola ($6.4 billion), Kenya ($5 billion), Côte d'Ivoire ($2.6 billion), and Nigeria ($2.5 billion). For 2025, private creditors will account for more than 50 percent of total debt service payments coming due. The implication of the dominant share of private creditors in future debt service is that debt restructuring mechanisms under the G20 Common Framework should strive to bring private creditors onboard. Indeed, except for Chad, which has reached an agreement with its main creditors, including the largest private creditors such as the Swiss commodities trader Glencore, and Zambia, which has recently reached agreement with bondholders. Progress for Ghana was only with official creditors, and progress under way for Ethiopia will be with official creditors only.

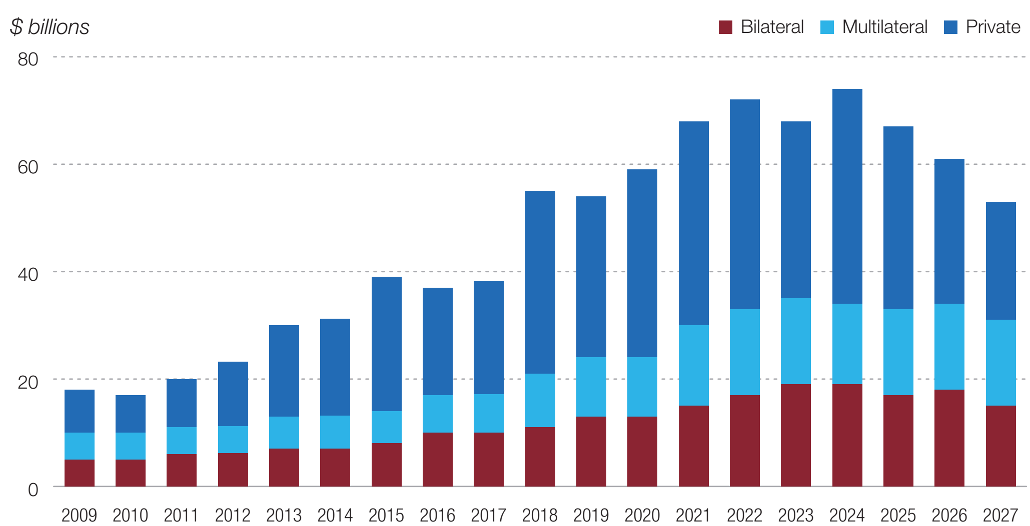
While the build-up in public debt in Africa has been associated with a surge in public investment, there is also evidence that low efficiency of public investment has weakened the growth benefits of such debt in Africa.[16] Africa has a public investment efficiency gap of 39 percent, higher than Europe (17 percent) and Asia (29 percent). Low efficiency implies that growth benefits of debt-financed public investment are not sufficient to generate revenue streams to liquidate the debt and finance new investments. High debt service, already absorbing a higher proportion of government revenue, could have a negative feedback effect on growth, as evidenced from Latin America's "lost decade" suggests.

During the Latin American debt crisis of the 1980s, many countries in the region could not service their foreign debt and went through painful fiscal adjustment, including cutting spending on infrastructure, health, and education. This resulted in high unemployment rates, steep per capita income declines, and stagnant or negative growth.[17] Africa's record growth since the 1990s epitomizes a similar experience to that of Latin America. Figure 1.43 shows a negative relationship between debt service costs and GDP growth rates. In other words, countries that had higher debt service costs experienced lower GDP per capita growth. In some countries, GDP per capita growth was negative. For instance, in Zambia, where the average debt service-to-GDP ratio was 6.6 percent between 1993 and 2022, GDP per capita growth averaged –2.1 percent a year. And for Côte d'Ivoire, whose external debt service-to-GDP ratio averaged 7.3 percent, growth in per capita income was –2.3 percent.

The high debt burden and weak revenue performance limit public sector investment capacity

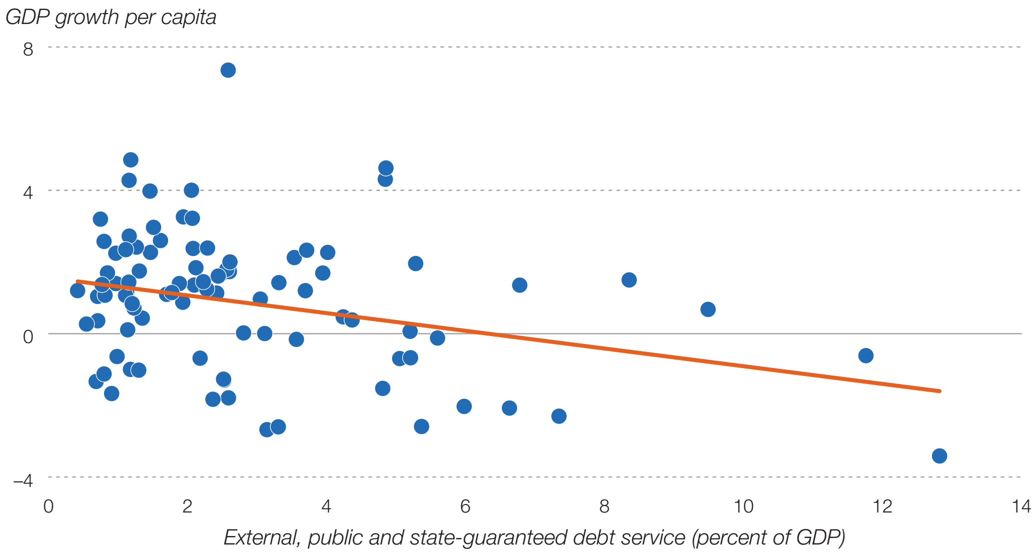
In 2024, African countries are expected to spend around $74 billion on debt service, up from $17 billion in 2010, of which $40 billion is owed to private creditors, representing 54 percent of total debt service

FIGURE 1.42 Composition of debt service by creditor, 2009–27



Source: Staff calculations based on data from International Debt Statistics (IDS) database.

FIGURE 1.43 Debt service cost and GDP per capita growth in selected African countries



Source: Staff calculations.

While debt restructuring mechanisms have been slow in the past, there is some glimmer of hope drawing on lessons from Zambia's experience with the slow pace in Framework implementation

in Africa. So, restoring debt sustainability could expand fiscal space but will require debt reprofiling or an outright restructuring for some countries. Although the G20 has facilitated the restructuring of official external debt through the Common Framework, the process has been characterized by significant delays and challenges recorded calls for urgent action to fast-track Framework implementation. This will encourage faster resolution through broader participation of debtor countries and creditors, especially private lenders. While debt restructuring mechanisms have been slow in the past, there is some glimmer of hope drawing on lessons from Zambia's experience with the slow pace in Framework implementation. Zambia reached agreements with main creditors—official lenders and bondholders, after protracted delays, joining Chad. This gives some optimism for progress with other countries that applied for external debt treatments under the Framework. Already, there is a significant improvement with Ghana's recent experience, and there is hope that the process might be shorter for other countries, including Ethiopia. For Zambia, it took close to three years from November 2020 to March 2024 to reach agreement while for Ghana it took less than a year from April 2023 (table 1.1).

The delays in debt restructuring mechanisms call for reform of the current global debt architecture

Given the systemic delays in concluding the debt restructuring process, there is need to overhaul the G20 Common Framework to create a functional debt resolution mechanism for countries in need. With private creditors accounting for more than 50 percent of the next two years' debt service payment, debt restructuring mechanism should succeed in bringing private creditors around the negotiation table. Key proposals include forming an expanded creditor committee with private lenders to smoothen coordination challenges and establishing a Comparability of Treatment formula to minimize technical disputes. Bolder use of the IMF's Lending into Official Arrears Policies can also reduce the leverage of holdout creditors. Proposals under the Global Sovereign Debt Roundtable—co-chaired by the IMF, the World Bank, and India (immediate past G20 Presidency)—will be critical in addressing shortcomings in the current debt restructuring processes. Finally, establishing a Multilateral Creditor Club, acting in partnership with debtors, could also improve the coordination of future debt restructurings and oversee outstanding global debt challenges.

TABLE 1.1 Recent cases of debt restructuring in Africa

Country	Dates	Parameter	Process
Chad	Launched January 2021 Agreement reached November 2022	External debt	Chad's public debt, at 56 percent of GDP in 2021, became unsustainable following the COVID-19 pandemic, volatility in oil prices, heightened insecurity, and a food crisis. Chad was the first country to reach an agreement with its creditors under the G20 Common Framework. • Creditors committed to reconvene and provide debt treatment, including for 2025–28, if necessary. • A large private creditor, Glencore, agreed to reprofile part of the debt service due in 2024. Official creditors will contribute if this is not sufficient to bring the debt service to revenue ratio below 14 percent in 2024.
Ghana		Domestic and external debt	A large fiscal expansion in response to the COVID-19 crisis put Ghana's public debt on an unsustainable trajectory, with the debt-to-GDP ratio reaching almost 90 percent of GDP at the end of 2022 and interest payments representing almost half of government revenue. An IMF program was requested in July 2022 and debt restructuring announced in December. • Domestic debt (48 percent of GDP at the end of 2022) was restructured through voluntary exchange (creditors were offered a menu of new instruments with longer maturities) and was completed by most financial institutions in February 2023. • External debt accounted for 40 percent of GDP at the end of 2022: Ghana applied to the Common Framework and official creditors formed a creditor committee in April 2023, providing financing assurances for the IMF to provide fresh financial support in May 2023. • In January 2024, Ghana reached agreement with official creditors on debt treatment under the G20 Common Framework.
Zambia		External debt	Zambia fell into arrears on external debt service after several years of large fiscal and external imbalances, a drop in copper prices in 2015–16, droughts, and the COVID-19 pandemic put public debt on an unsustainable path. Total public debt peaked at 150 percent of GDP and external public debt at 96 percent in 2020. The country defaulted on its eurobonds in November 2020, after losing market access. • Zambia sought a Common Framework treatment in January 2021, and an IMF-supported program was approved by the Board of the IMF in August 2022. • Official creditors agreed on a debt treatment in June 2023 which allowed the second disbursement of the IMF financing. The agreement specifies a baseline treatment, and a contingent treatment that would be automatically triggered if the assessment of Zambia's economic performance and policies improves, allowing for better terms for creditors. • Discussions with private creditors started in September 2023 • In March 2024, Zambia reached an agreement with external bondholders on a restructuring of $3 billion.
Ethiopia		External debt	Ethiopia requested treatment under the Common Framework in February 2021, and an Official Creditor Committee was formed in September of that year. • An agreement was reached in November 2023 between the Ethiopian authorities and its official bilateral creditors for a time-bound debt service standstill due from 1 January 2023 to 31 December 2024. • Suspended payments will be repaid after a two-year grace period and over a three-year period from 2027 to 2029. • This debt standstill from Ethiopia's official bilateral creditors will provide time-limited liquidity relief ahead of discussions on a wider debt treatment. Those discussions will gain momentum as soon as the Ethiopian authorities and the IMF have agreed the parameters for an IMF program. • In the context of a wider debt treatment, the efforts made by official bilateral creditors over the debt standstill period will be taken into account under the principles of Comparability of Treatment.

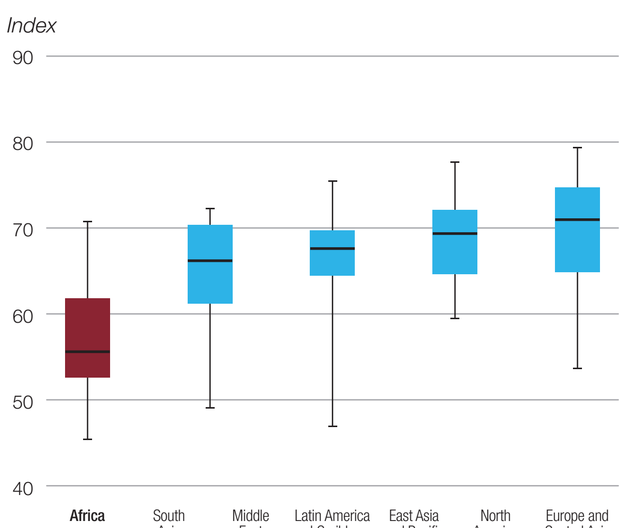
Source: IMF 2023 and African Development Bank staff.

LINKAGES BETWEEN AFRICA'S TRANSFORMATION EFFORTS AND THE INTERNATIONAL FINANCIAL ARCHITECTURE

Despite the remarkable resilience of African economies amid domestic and external shocks, most African countries are mired in low income and plagued by widespread poverty and inequality

African economies have remained resilient despite the debilitating impact of the COVID-19 pandemic, the tightening of global financial conditions, the spillover effects of Russia's invasion of Ukraine, subdued global growth, and persistent climatic threats. However, this commendable achievement hides a less gleaming picture: most African countries are mired in low income and plagued by widespread poverty and inequality, compared with other world regions. So, despite its strong recent growth performance, Africa's structural transformation has remained slow and uneven (chapter 2), and the continent has been slow to move up the global value chains and catch up with other regions of the world, create decent jobs and sustain development for shared prosperity.

FIGURE 1.44 SDG composite index in Africa and other world regions, 2022



Note: The SDG Index aggregates data on individual SDGs into a composite index. The plot excludes extreme values (values below the 5th and above the 95th percentiles).

Source: Staff calculations based on Sachs et al. (2023).

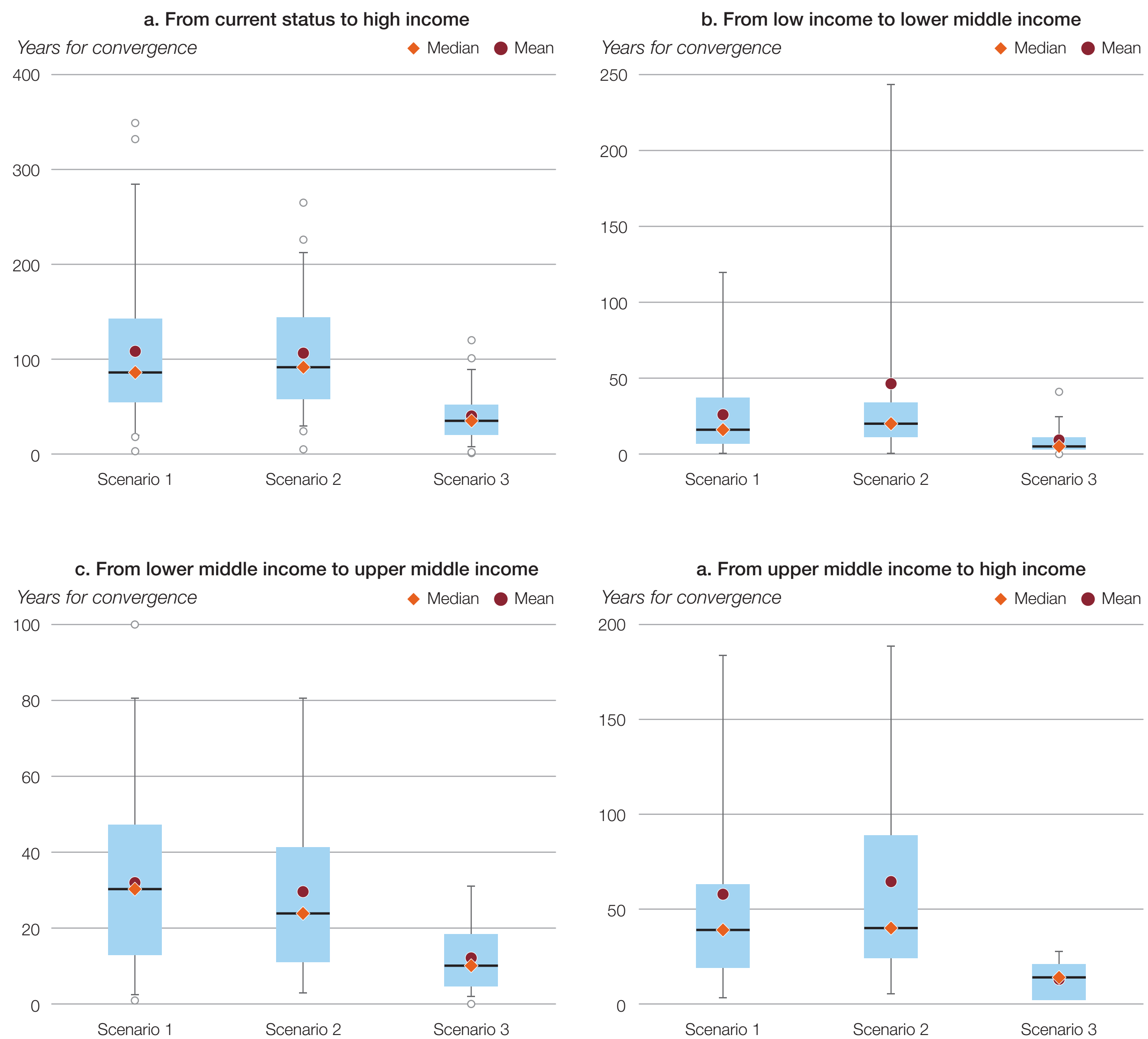
As a result, the continent is off-track in achieving almost all SDG targets by 2030. If no action is taken for course correction, including to reversing the steepening poverty curve, close to 9 out of 10 (or 87 percent) of the world's extremely poor people will be in Africa by 2030.[18]

Furthermore, Africa remains the second-most economically unequal region in the world, after Latin America and the Caribbean.[19] Over 600 million people on the continent currently have no access to electricity and more than 600,000 die annually from indoor air pollution associated with use of biomass (charcoal) for cooking.[20] The median composite SDG index score—a measure that tracks performance across all SDG areas—for African countries is the lowest among its peers, at about 56 by 2022, which implies that the continent is about 44 percent short of reaching the SDGs by 2030 (figure 1.44). In contrast, the median score is 69.4 in Latin America and the Caribbean and 78.5 in Europe and Central Asia.

The evident desynchronization between economic growth performance and sustainable development suggests that Africa's current development model is not fit for purpose

The existing development model, which relies heavily on resource extraction without value addition, urgently requires a complete overhaul if the continent is to catch up with other regions. The urgency is such that, under a business-as-usual scenario, it could take today African countries more than a century on average (108 years, for a median of 86 years) to transition to a high-income status (see figure 1.45a, scenario 1). Even in the most optimistic scenario—a country's per capita GDP grows annually according to its highest rate ever achieved since 2010 (figure 1.45a, scenario 3)—it could still take on average about 40 years to become a high-income country, well after the deadline of the 2030 Global Agenda and around the African Union's Agenda 2063 implementation deadline. While moving from a low- to a middle-income status (figure 1.45b) could be faster (on average, in about 26 years in scenario 1 and 9 years in scenario 3), crossing the middle-income segment is more challenging as it could take on average 58 years to transition from the upper middle- to the high-income status (figure 1.45d, scenario 1).

FIGURE 1.45 **Years of economic convergence of African countries to high-income status under various scenarios**



Note: Years of convergence refer to the number of years required for African countries to cross the World Bank's current thresholds for country income groups: $1,136 to move from low-income countries (LICs) to lower middle-income countries (LMICs), $4,466 from LMICs to upper middle-income countries (UMICs) and $13,846 to be classified as high-income countries (HICs). In scenario 1, per capita GDP in each African country is assumed to grow according to the post-COVID-19 (2022–25) average growth rate. In scenario 2, pre-COVID-19 average annual growth rate of per capita GDP (2010–19) is considered while in scenario 3, the highest per capita GDP growth reached by each African country since 2010 is used. Countries with negative growth rates under various scenarios were excluded in the figures. Hollow dots refer to outliers (values below the 5th and above the 95th percentiles).
Source: Staff calculations.

There is therefore a hugely potential risk that most African countries which have managed to reach the middle-income status remain stuck in a middle-income trap—a situation whereby a country, after developing quickly, experiences a sharp, sustained drop in economic growth, typically because of a reduction in the rate of productivity expansion.[21] Furthermore, evidence of the past four decades indicates that upward movements in income classification are not widespread across the continent: only 28 African countries (or 52 percent) managed to move at least once to a higher income category, out of which 18 countries also moved downward at least once over the same period (figure 1.46). This implies that the remaining 26 African countries (or 48 percent) have been trapped in their income status over the past four decades. The middle-income trap could further widen the gap between Africa and its high-income peers and thus consign its people to perpetual poverty.

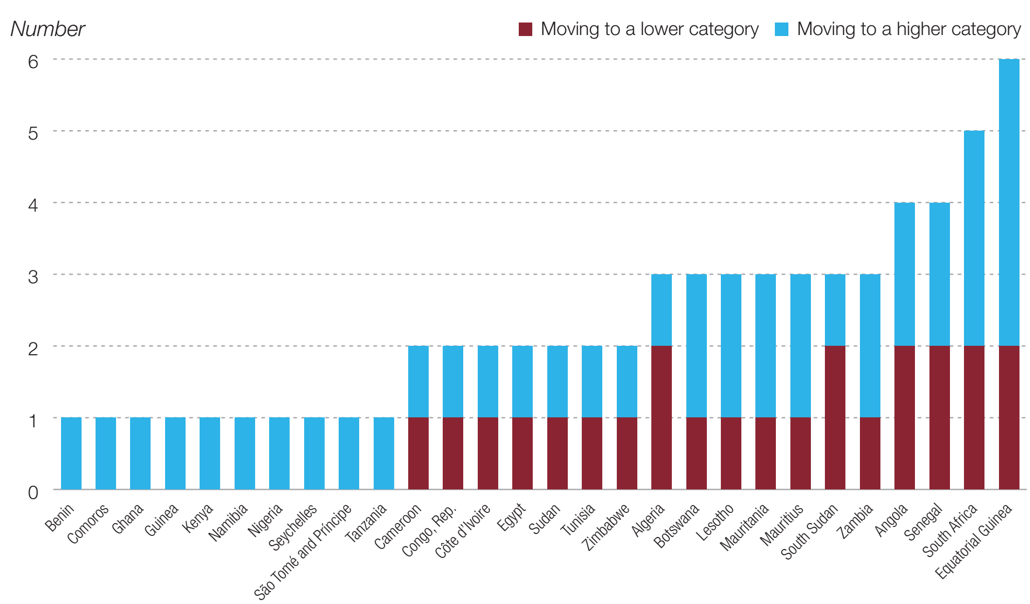
Accelerating structural transformation efforts and financing its implementation will be key to unlocking Africa's development potential

The structure of African economies has not significantly changed over the past two decades, with agriculture, industry, and services sectors accounting on average for respectively 16 percent, 33 percent, and 51 percent of Africa's GDP over 2000–22. This is similar to the levels achieved in the 1990s. Although there is evidence of some ongoing structural transformation process across the continent (see AfDB 2024), its current pace remains insufficient to induce profound changes in Africa's development landscape. The speed of this structural transformation will be a key factor that will differentiate countries that will successfully sustain their development path from unsuccessful ones.[22] For that, it is important to understand both internal and external factors behind slow progress in structurally transforming Africa's economies. Identifying the main pull and push factors of structural transformation will help guide evidence-informed policymaking to put the continent on a sustainable development path (chapter 2).

While well-designed structural reforms are important to boost the level and sustainability of economic growth, their implementation depends partly on scaling up financing for structural transformation and enhancing spending efficiency. Boosting domestic resource mobilization plays a critical role in that regard as African governments are primarily responsible for financing their development. At the median, African governments currently collect only about 13.6 percent of GDP in tax revenues, while the median tax-to-GDP ratio in other developing countries is 15.4 percent and reaches 21.1 percent in HICs (figure 1.47a). It will thus be important to mobilize more resources

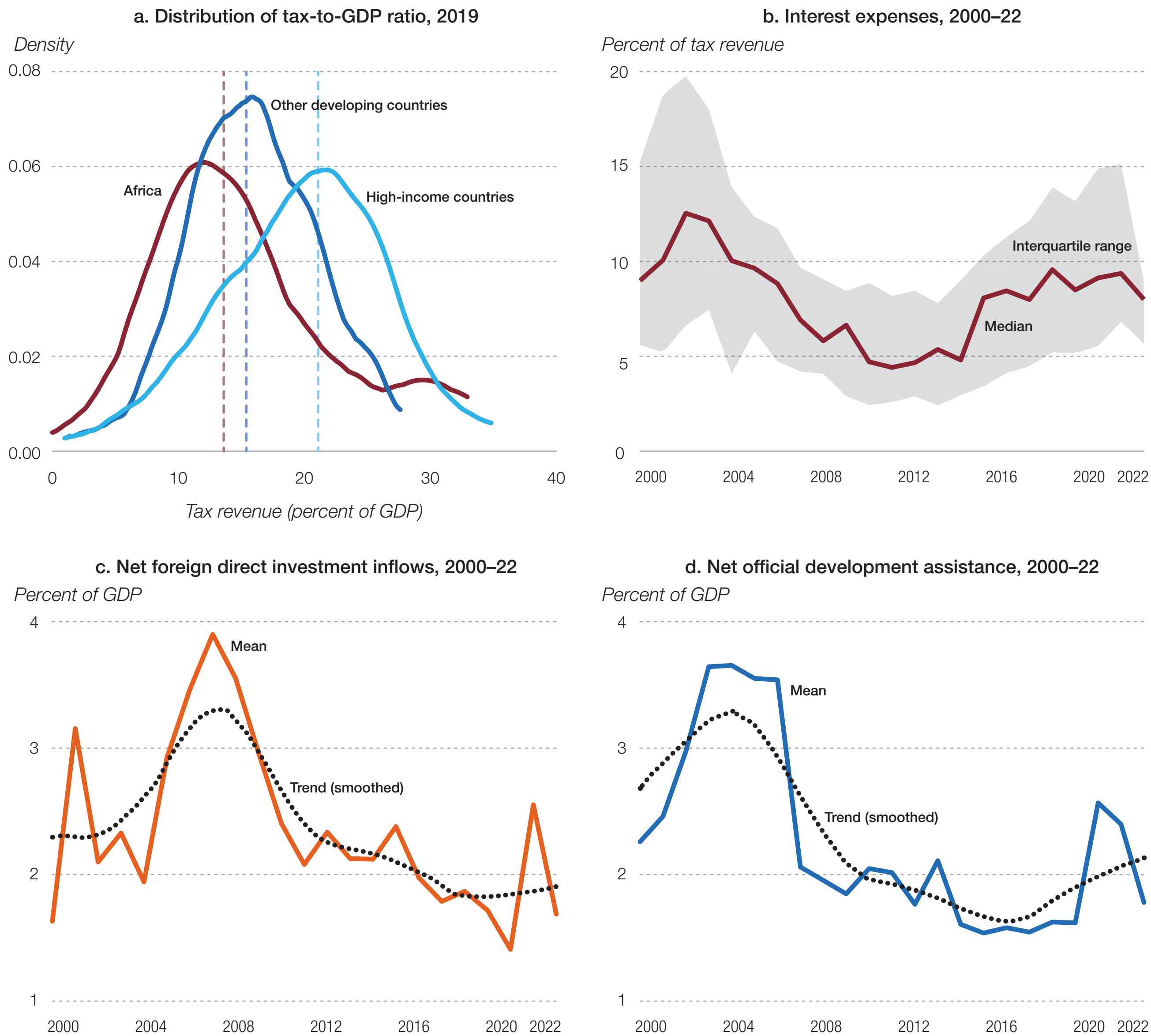
The structure of African economies has not significantly changed over the past two decades, with agriculture, industry, and services sectors accounting on average for respectively 16 percent, 33 percent, and 51 percent of Africa's GDP over 2000–22

FIGURE 1.46 **Dynamics of country income classification changes in Africa, 1987–2022**



Note: Figure reports the number of times each country moved to another income group (LICs, LMICs, UMICs, and HICs) since 1987 based on World Bank's income thresholds for the corresponding year. African countries not reported are those that remained in the same income group over the 1987–2022 period.
Source: Staff calculations.

FIGURE 1.47 Domestic resource mobilization, private investment and international support fall short of Africa's development finance needs



Note: Other developing countries refer to all non-African countries not classified as high-income countries using the World Bank's current country income classifications. Interest payments include interest payments on government debt—including long-term bonds, long-term loans, and other debt instruments—to domestic and foreign residents.

Source: Staff calculations.

domestically for structural transformation knowing that, at the median, around 11 percent of collected tax revenues on the continent are allocated annually to the payment of interest on government debt to domestic and foreign residents (figure 1.47b).

These huge interest payments—in part a result of the high cost of sovereign borrowing due to high perceived risks associated with African markets and poor credit ratings in international markets —crowd out financing of public investments in critical sectors such as education, health, infrastructure, etc. With appropriate reforms, there still is considerable room for a gradual increase of tax revenues in Africa insofar as evidence has shown that the tax capacity—the predicted maximum taxation in an economy given its macroeconomic, demographic, and institutional features—was about 23 percent of GDP in low-income countries, most of which are African.[23] While the appropriate level of taxation is determined by each country's characteristics, fast-tracking structural transformation will ultimately depend on a country's ability to increase its tax capacity.

Private flows—particularly in the form of FDI —can further make a significant contribution to scale up financing and support faster transfer of technology and skills, job creation, and innovation, important ingredients to accelerate Africa's structural transformation. So far, the potential of external private finance for structural transformation remains however largely unrealized. Net FDI inflows to Africa as a percent of GDP has been volatile and mostly declining since the global financial crisis of 2007–08 (figure 1.34 and figure 1.47c). While international support could have also helped fill the continent's development finance gap, net inflows of ODA to African countries as a percent of their GDP have followed a declining path, limiting the scope for donor inflows to finance new SDG-related projects (Figure 1.34 and figure 1.47d). In addition, as highlighted in the AEO 2022, only a handful of developed countries have met the United Nations' target for developed countries to allocate at least 0.7 percent of their gross national income (GNI) to ODA, beyond other global financing commitments. Boosting both external private finance and donor inflows as well as increasing access to concessional financing—critical to reduce debt vulnerabilities—will require reform of the international financial architecture in a way that supports Africa's structural transformation efforts (chapter 3).

Better identification of inflationary forces in Africa is needed, as is deepening domestic financial markets to foster monetary policy transmission

POLICY RECOMMENDATIONS

Following the strong recovery a year after the COVID-19 pandemic, economic performance in Africa has slowed due to a variety of factors, including persistently high food and energy prices as a result of Russia's ongoing invasion of Ukraine, subdued performance of the export sector due to weak global demand, the impact of climate change and extreme weather events, and political instability and conflict in some African countries. Addressing these constraints to accelerate structural transformation and put Africa back on the path to achieve the SDGs requires implementing a mix of measures in the short, medium, and long terms. These include a judicious mix of fiscal and monetary policies aimed at promoting macroeconomic stability, advancing structural reforms in the areas of revenue mobilization and structural transformation, and remaining committed to reforming the international financial architecture to help increase Africa's capacity to tap additional sources of financing. financing without burdening current and future generations.

Short-term policy measures

A more tailored monetary policy is needed to tackle persistent inflationary pressures

The persistence of inflation in Africa amid upside risks to inflation and weakening currencies warrants tailored monetary policy adjustments. In most economies, central banks have typically tried to keep policy rates high enough to ensure that inflation expectations remain well anchored. In particular, monetary policy stance can be more accommodative in economies where core inflation is moderate and headline inflation is driven mostly by temporary supply shocks. Given the importance of supply-side shocks behind Africa's recent inflation bout, high interest rates may indeed not be optimal in all countries and risk depressing demand excessively. Better identification of inflationary forces in Africa is therefore needed, as is deepening domestic financial markets to foster monetary policy transmission. Fiscal dominance and central bank financing of the fiscal deficit, which undermines the central banks' credibility to fight inflation, should also be contained, ensuring that monetary and fiscal policy are moving in the same direction.

To adequately reduce inflationary pressures, African countries should also remove hurdles preventing domestic supply from responding to higher prices—and to boost labor productivity via infrastructure and human capital investment. They should accelerate the implementation of the mechanisms for dampening the effect of supply shocks, such as greater diversification and better infrastructure that support productivity growth in agriculture and manufacturing. In particular, successful disinflation may require incentivizing business investment to protect future productive capacity. Given prevailing financial conditions, if bolder and more transformative policies are not implemented, the current aggressive monetary policy stance in Africa could lead to further slowdowns in Africa's growth and debt and debt servicing spiraling out of control.

Promoting local production and diversifying import sources are key to addressing food prices

Supporting African smallholder farmers can trigger an agricultural revolution to feed Africa, especially in urban areas. African countries need to provide farmers with broad access to affordable finance, improved food production technologies (especially certified seeds adapted to extreme climatic conditions), and large-scale systematic extension and mechanization services to increase food production and thus stabilize food prices in the short to medium term. In the long term, economic diversification and the strengthening of intra-African trade should enable African countries to become self-sufficient in food. This will be crucial for strengthening economic resilience to future shocks. The African Continental Free Trade Area offers significant opportunities for trade diversification and the development of trade networks in key agricultural sectors.

Reducing debt burdens through governance reforms to strengthen debt management capacity

Recent debt trends in many African countries have revived the need for strong governance reforms to strengthen debt management capacity. Good governance and strong institutional capacity prevent "below the line" operations that undermine debt reduction efforts and ensure that countries strengthen their buffers and deleverage in good times. To achieve this, there is need to build strong budgetary institutions that support efficient mobilization of domestic resources at scale, use them prudently, and conduct sound public expenditure and debt management surveillance. In addition, a stronger link between debt, growth, and governance would help maximize the growth dividend of debt-financed public investment. Countries also need to increase debt transparency by improving the collection, reporting, and management of debt statistics and strengthening the monitoring of state-owned enterprises to reduce fiscal risks from undisclosed debt and contingent liabilities. Good governance will also form the basis for broader economic reforms.

Addressing exchange rate pressures should be a key short-term priority

The rapid depreciation of exchange rate in some African countries has continued despite various policies implemented to stem the tide. Yet exchange rate policy can be a powerful instrument to fight inflation and stimulate economic growth. In countries with floating exchange rates, currencies should be allowed to adjust as much as possible in line with developments in other macroeconomic fundamentals, as attempts to resist movements based on fundamentals could have unintended adverse consequences on growth. In countries with pegged exchange rates, monetary policy must be aligned with that of the anchor country to maintain external stability and avoid further losses in foreign exchange reserves as countries seek to preserve parity and protect the domestic currency from depreciating. Structural reforms to implement a strategic industrial policy to accelerate economic diversification and strengthen the export sector, as well as fiscal consolidation when the budget deficit increases pressure on the exchange rate, should be implemented simultaneously with monetary policy measures to increase resilience to shocks.

Supporting African smallholder farmers can trigger an agricultural revolution to feed Africa, especially in urban areas

Policies for the medium to long term

Reforming the current global financial architecture to make it fit for African countries' financing needs

In most African countries, debt servicing costs have risen, straining public finances, and limiting the scope for government infrastructure spending and investment in human capital, which maintain the continent in a vicious cycle that traps Africa in low growth trajectory. One reason for the increased vulnerabilities is the failure of the global financial architecture to provide financing for countries most in need of resources for development. As African countries continue to face financing challenges, mainstream financial institutions need to rethink their role and financing model. The proposed Triple Agenda of the G20 highlights the various benefits of a reformed global financial architecture to make it more responsive in mobilizing and channeling finance for the SDGs. Reforming the global financial architecture and expanding the representation of developing countries will improve decisionmaking, increase transparency, and reduce the cost of capital. The resulting additional finance mobilized for development could help alleviate fiscal pressures on African countries, promote macroeconomic stability, boost market confidence, and reduce borrowing costs.

Reforming the global financial architecture and expanding the representation of developing countries will improve decisionmaking, increase transparency, and reduce the cost of capital

Scaling up domestic resource mobilization is a must for African countries to accelerate Africa's structural transformation

As outlined in the Addis Ababa Action Agenda (2015), there is broad consensus that successful implementation of the 2030 Global Agenda and the African Union's Agenda 2063 requires greater mobilization and more effective use of domestic public resources. According to some estimates, corruption costs Africa $148 billion every year and about $90 billion leaves the continent annually in the form of illicit financial flows. Fighting illicit financial flows is therefore critical to addressing the challenge of domestic resource mobilization. This includes strengthening the rule of law by building a strong and independent judiciary and investing in the training of judges, prosecutors, and police officers to assist them in investigating and prosecuting corruption cases. In addition, anticorruption institutions need to be strengthened by establishing specialized anti-corruption agencies with sufficient resources and genuine independence to investigate and prosecute offenders.

While these reforms are necessary to fight illicit capital flows, a multidimensional approach is needed to combat them effectively. This includes tightening financial regulations by placing the burden of transparency and accountability obligations on financial institutions to prevent illicit capital flight. In addition, strengthening border controls and institutional capacity, as well as international cooperation, are also crucial for tracking illicit capital flows and recovering stolen assets. Countries should also apply innovative approaches, including financial surveillance technologies such as blockchain and artificial intelligence, to monitor financial transactions and detect suspicious patterns of capital movements.

In addition to implementing reforms to mobilize more domestic resources, countries must also promote measures aimed at curbing wastage of public resources and improving the efficiency of public spending. Current expenditure, including government employee salaries, must be controlled, while capital expenditure must be channeled into growth-enhancing investments. Inefficient operating expenditure must be reduced. The use and spread of digital technologies in public administration could help save money and improve the efficiency of tax administration. Countries must also make political stability and the rule of law key pillars in strengthening institutions and the mode of governance. Reducing the demographic dependency rate by creating conditions for youth employment to increase the size of the active population could also help increase the tax base to complement traditional measures to improve collection of tax revenue.

Creating an enabling environment is crucial for attracting and scaling up external financial flows as complementary sources of financing Africa's economic transformation

Although domestic resources will remain an integral and larger part of financing Africa's economic transformation, external financial flows will be essential as complementary sources of funding development needs. Africa has performed relatively well in attracting foreign direct investment (FDI), but much of this investment has been in extractive sectors and limited to few, and mostly large economies. African economies therefore need to attract more FDI and, almost more important, create the conditions for its stability to reap the greatest benefits for growth. Stylized facts and empirical evidence show that FDI volatility and lack of private sector financing are two major impediments to the development of African manufacturing. African countries therefore need to create a favorable environment to better attract foreign investment. This includes promoting political stability, the absence of violence and conflict, good governance, and price stability. Official development assistance (ODA) has not proven to be an effective ally in reducing debt in African countries. This suggests that most African countries may have fallen victim to an aid syndrome that has led to either increased spending or less significant mobilization efforts, or a combination of both. Official development assistance to African countries therefore needs to be rethought if it is to achieve its objective of freeing recipient countries from the aid dependency. It should focus more on the transfer of skills and technologies to increase the ability to mobilize domestic resources. Donors also need to pay more attention to ensuring that ODA is used effectively and efficiently, focusing on key sectors that have a significant impact on public revenue generation.

Given the uneven performance and the very tight timeframe to achieve the SDGs, accelerating structural reforms to build resilient economies should be a top priority

The persistent growth volatility that Africa has experienced in the aftermath of the COVID-19 pandemic, coupled with the decline in income growth, clearly calls for prioritizing structural reforms to strengthen the continent's resilience to shocks. Therefore, in countries where the volatility in growth is largely attributed to energy monopolies, which is a key driver for inefficiency in electricity generation and associated shortages, liberalizing the energy sector should be a priority. And in an environment where development financing gaps remain large and financing conditions tight, reprioritizing fiscal spending should redirect expenditure toward growth-enhancing public investment projects. Countries also need to prioritize climate-adaptation policies to improve resilience to climate-related disasters and hence strengthen resilience. In countries where domestic demand is weak, policymakers need to implement reforms such as reducing regulatory barriers and improving public service with the aim of attracting private investments. This will provide an enabling environment for job creation and improving household incomes. Finally, accelerating diversification of economies through production and trade activities will help build resilience to navigate the negative effects emerging from global tensions.

Accelerating structural transformation efforts and financing its implementation will be key to unlocking Africa's development potential

Although there is evidence of some ongoing structural transformation across the continent, its current pace remains insufficient to induce profound changes in Africa's development landscape. Identifying the main pull and push factors of structural transformation will help guide evidence-informed policymaking to put the continent on a sustainable development path. While well-designed structural reforms are important to boost the level and sustainability of economic growth, their implementation depends partly on scaling up financing for structural transformation and enhancing spending efficiency. Boosting domestic resource mobilization plays a critical role in that regard as African governments are the primary responsible for financing their development. Private flows—particularly in the form of foreign direct investment—can further make a significant contribution to scale up financing and support faster transfer of technology and skills, job creation, and innovation, important ingredients to accelerate Africa's structural transformation.

Official development assistance to African countries therefore needs to be rethought if it is to achieve its objective of freeing recipient countries from the aid dependency

ANNEX 1.1A REAL GDP GROWTH *(percent)*

	2022	2023 estimated	2024 projected	2025 projected
Central Africa	**5.1**	**4.3**	**4.1**	**4.7**
Cameroon	3.6	3.8	4.1	4.4
Central African Rep.	0.5	1.0	2.3	3.1
Chad	3.4	4.3	5.2	5.3
Congo, Dem. Rep.	8.8	7.5	5.7	5.6
Congo, Rep. of	1.7	3.9	4.3	4.4
Equatorial Guinea	3.7	–5.7	–5.0	2.7
Gabon	3.0	2.3	2.8	2.9
East Africa	**4.5**	**1.5**	**4.9**	**5.7**
Burundi	1.8	2.8	4.6	5.9
Comoros	2.6	3.1	4.0	4.6
Djibouti	3.7	7.3	6.2	6.6
Eritrea	2.6	2.9	2.9	3.1
Ethiopia	6.4	7.1	6.7	6.7
Kenya	4.8	5.2	5.4	5.6
Rwanda	8.2	8.2	6.5	6.8
Seychelles	15.0	2.5	4.0	4.3
Somalia	2.4	2.8	3.7	3.8
South Sudan	–2.9	–0.4	–5.0	1.0
Sudan	–1.0	–37.5	–5.9	0.5
Tanzania	4.7	5.3	5.7	6.0
Uganda	6.3	4.6	6.0	7.0
North Africa	**4.6**	**4.1**	**3.6**	**4.2**
Algeria	3.6	4.2	4.0	3.7
Egypt	6.7	3.8	3.3	4.5
Libya	–3.7	12.6	7.9	6.2
Mauritania	6.4	3.4	4.2	5.5
Morocco	1.3	3.2	3.5	3.8
Tunisia	2.5	0.4	2.1	2.9

	2022	2023 estimated	2024 projected	2025 projected
Southern Africa	**2.8**	**1.6**	**2.2**	**2.7**
Angola	3.0	0.9	2.7	4.3
Botswana	5.5	2.7	4.0	4.3
Lesotho	1.3	0.9	1.7	2.2
Madagascar	4.3	4.4	4.5	5.3
Malawi	0.9	1.5	3.3	3.8
Mauritius	8.9	7.0	4.9	3.7
Mozambique	4.2	5.0	5.2	5.2
Namibia	5.3	4.2	2.6	3.3
São Tomé and Príncipe	0.1	0.5	1.2	2.1
South Africa	1.9	0.6	1.3	1.6
eSwatini	0.5	4.8	4.9	3.6
Zambia	5.2	5.8	4.5	4.5
Zimbabwe	6.1	5.0	2.0	3.5
West Africa	**3.9**	**3.6**	**4.2**	**4.4**
Benin	6.3	6.4	6.5	6.2
Burkina Faso	1.5	3.6	4.1	4.3
Cabo Verde	17.4	4.6	4.7	4.8
Côte d'Ivoire	6.2	6.5	7.1	6.9
Gambia, The	4.9	5.6	6.1	5.8
Ghana	3.8	2.9	3.4	4.3
Guinea	4.0	5.7	4.2	5.4
Guinea–Bissau	4.2	4.3	4.7	5.2
Liberia	4.8	4.5	5.2	6.2
Mali	3.7	4.3	4.7	5.3
Niger	11.9	2.5	10.5	7.7
Nigeria	3.3	2.9	3.2	3.4
Senegal	3.8	4.1	9.3	10.2
Sierra Leone	3.5	2.6	4.7	5.2
Togo	5.8	5.6	5.3	6.0
Africa	**4.1**	**3.1**	**3.7**	**4.3**

Source: African Development Bank statistics.

ANNEX 1.1B OUTLOOK FOR KEY MACROECONOMIC INDICATORS FOR 2024 AND 2025

	Real GDP growth		Inflation		Current account balance		Fiscal balance	
	2024	2025	2024	2025	2024	2025	2024	2025
Algeria	4.0	3.7	6.8	5.7	1.0	–0.2	–11.1	–12.0
Angola	2.7	4.3	18.1	12.4	5.1	3.5	–0.9	–1.8
Benin	6.5	6.2	2.2	2.4	–4.4	–4.2	–3.8	–3.3
Botswana	4.0	4.3	4.5	4.0	1.1	1.2	–1.8	–0.3
Burkina Faso	4.1	4.3	2.1	2.2	–6.5	–5.4	–6.0	–5.4
Burundi	4.6	5.9	22.0	12.6	–6.8	–6.2	–4.4	–3.8
Cabo Verde	4.7	4.8	2.2	2.0	–6.8	–6.2	–3.1	–2.3
Cameroon	4.1	4.4	6.3	4.3	–1.9	–1.6	–0.5	–0.2
Central African Rep.	2.3	3.1	4.1	3.4	–9.0	–9.9	–2.8	–1.9
Chad	5.2	5.3	3.4	3.2	1.3	0.8	2.7	2.2
Comoros	4.0	4.6	3.1	2.0	–5.8	–5.3	–3.6	–2.7
Congo, Dem. Rep.	5.7	5.6	17.0	10.0	–4.5	–3.6	–2.0	–1.1
Congo, Rep.	4.3	4.4	3.4	3.2	3.2	2.3	4.0	2.6
Côte d’Ivoire	7.1	6.9	3.5	2.8	–6.9	–6.1	–4.2	–3.0
Djibouti	6.2	6.6	1.7	2.0	20.0	19.6	0.4	–0.2
Egypt	3.3	4.5	35.8	22.7	–3.0	–3.2	–7.2	–6.3
Equatorial Guinea	–5.0	2.7	4.7	2.6	–3.5	–5.1	2.7	–3.7
Eritrea	2.9	3.1	4.1	3.9	12.4	13.0	0.6	0.8
Ethiopia	6.7	6.7	21.0	15.8	–2.0	–1.2	–2.7	–2.5
Gabon	2.8	2.9	2.5	2.3	–0.9	0.5	–1.1	–0.7
Gambia, The	6.1	5.8	15.9	11.0	–7.6	–5.6	–2.7	–2.9
Ghana	3.4	4.3	20.9	11.1	–1.9	–2.3	–4.9	–4.2
Guinea	4.2	5.4	10.8	10.4	–10.3	–9.6	–2.6	–2.4
Guinea-Bissau	4.7	5.2	5.4	3.2	–5.2	–3.3	–3.6	–3.1
Kenya	5.4	5.6	6.2	5.5	–4.6	–4.5	–5.9	–5.0
Lesotho	1.7	2.2	5.5	5.0	–4.2	–5.4	–0.4	–3.3
Liberia	5.2	6.2	8.4	5.7	–23.7	–24.6	–2.6	–3.3
Libya	7.9	6.2	2.8	2.6	24.5	22.3	4.2	8.7
Madagascar	4.5	5.3	8.1	7.5	–4.4	–4.0	–4.1	–4.6
Malawi	3.3	3.8	27.3	14.3	–8.2	–9.5	–8.7	–7.6
Mali	4.7	5.3	2.0	1.8	–6.4	–5.9	–4.3	–3.4
Mauritania	4.2	5.5	4.7	4.2	–8.5	–7.4	–2.0	–1.6
Mauritius	4.9	3.7	5.8	5.0	–4.2	–4.5	–4.5	–4.3
Morocco	3.5	3.8	4.1	3.8	–0.4	–0.9	–4.4	–4.2
Mozambique	5.2	5.2	5.0	4.6	–38.1	–43.0	–3.4	–1.3
Namibia	2.6	3.3	4.6	4.4	–9.6	–8.5	–4.2	–4.0
Niger	10.5	7.7	3.5	3.1	–7.8	–8.7	–4.2	–3.1
Nigeria	3.2	3.4	31.6	20.7	3.0	3.6	–4.3	–4.1
Rwanda	6.5	6.8	7.0	5.2	–10.9	–10.7	–6.4	–5.9
São Tomé and Príncipe	1.2	2.1	16.1	7.2	–11.4	–9.0	–3.3	–2.9

(continued)

	Real GDP growth		Inflation		Current account balance		Fiscal balance	
	2024	2025	2024	2025	2024	2025	2024	2025
Senegal	9.3	10.2	4.9	3.3	–10.9	–8.3	–4.0	–3.2
Seychelles	4.0	4.3	1.4	2.2	–7.2	–7.2	–1.5	–1.3
Sierra Leone	4.7	5.2	33.6	20.2	–4.2	–2.1	–2.8	–2.4
Somalia	3.7	3.8	4.8	4.3	–10.4	–10.2	–0.3	–1.4
South Africa	1.3	1.6	4.8	4.5	–2.9	–3.2	–4.3	–4.2
South Sudan	–5.0	1.0	17.5	18.0	–7.0	–4.0	–6.0	–2.0
Sudan	–5.9	0.5	157.9	85.6	–6.5	–5.2	–6.3	–2.8
eSwatini	4.9	3.6	4.8	5.1	3.9	2.9	–2.2	–1.7
Tanzania	5.7	6.0	3.3	3.4	–4.0	–4.2	–2.5	–2.5
Togo	5.3	6.0	2.7	2.1	–3.1	–3.0	–6.6	–4.0
Tunisia	2.1	2.9	7.1	6.7	–3.3	–4.0	–6.5	–6.0
Uganda	6.0	7.0	4.5	5.0	–8.3	–8.8	–4.2	–3.6
Zambia	4.5	4.5	9.3	7.0	3.3	8.4	–5.2	–3.4
Zimbabwe	2.0	3.5	24.9	17.4	0.7	0.2	–1.7	–1.5

Note: GDP growth and inflation are in percent, while current account balance and fiscal balance are in percent of GDP. This heatmap plots the countries' outlook for selected key macroeconomic indicators. Countries are ranked in three criteria: "green" for good performers, "yellow" for fair performers and "red" for weak performers. Real GDP growth above 6 percent are coloured green, 4–6 percent are coloured yellow and below 4 percent are coloured red. Inflation rates below 5 percent are coloured green, 5–9.9 percent are coloured yellow and double digit are coloured red. Current account surplus is coloured green, deficits below 5 percent are coloured yellow and above 5 percent are coloured red. Fiscal deficits below 3 percent are coloured green, 3–5 percent are coloured yellow and above 5 percent are coloured red.

ANNEX 1.2 COUNTRY GROUPINGS

Oil exporters
Algeria, Angola, Cameroon, Chad, Republic of Congo, Egypt, Equatorial Guinea, Gabon, Libya, Nigeria, South Sudan

Other resource-intensive
Botswana, Burkina Faso, Central African Republic, Democratic Republic of Congo, Ghana, Guinea, Liberia, Mali, Namibia, Niger, Sierra Leone, South Africa, Sudan, Tanzania, Zambia, Zimbabwe

Non-resource-intensive
Benin, Burundi, Cabo Verde, Comoros, Côte d'Ivoire, Djibouti, Eritrea, Ethiopia, The Gambia, Guinea-Bissau, Kenya, Lesotho, Madagascar, Malawi, Mauritania, Mauritius, Morocco, Mozambique, Rwanda, São Tomé and Príncipe, Senegal, Seychelles, Somalia, eSwatini, Togo, Tunisia, Uganda

Tourism dependent
Cabo Verde, Comoros, Mauritius, São Tomé and Príncipe, Seychelles

Low income
Burkina Faso, Burundi, Central African Republic, Chad, Democratic Republic of Congo, Eritrea, Ethiopia, The Gambia, Guinea, Guinea-Bissau, Liberia, Madagascar, Malawi, Mali, Mozambique, Niger, Rwanda, Sierra Leone, Somalia, South Sudan, Sudan, Togo, Uganda

Middle income
Algeria, Angola, Benin, Botswana, Cabo Verde, Cameroon, Comoros, Republic of Congo, Côte d'Ivoire, Djibouti, Egypt, Equatorial Guinea, Gabon, Ghana, Kenya, Lesotho, Libya, Mauritania, Mauritius, Morocco, Namibia, Nigeria, São Tomé and Príncipe, Senegal, Seychelles

Sub-Saharan Africa
Angola, Benin, Botswana, Burkina Faso, Burundi, Cabo Verde, Cameroon, Central African Republic, Chad, Comoros, Democratic Republic of Congo, Republic of Congo, Côte d'Ivoire, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, Gabon, The Gambia, Ghana, Guinea, Guinea-Bissau, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mauritius, Mozambique, Namibia, Niger, Nigeria, Rwanda, São Tomé and Príncipe, Senegal, Seychelles, Sierra Leone, Somalia, South Africa, South Sudan, Sudan, eSwatini, Tanzania, Togo, Uganda, Zambia, Zimbabwe

ANNEX 1.3 EMPIRICAL EVIDENCE OF THE IMPACT OF ODA ON THE CONTROL OF PUBLIC SPENDING AND DEBT

	OLS regressions			FE regressions with CSD		
Variable	**Public debt (percent GDP)**	**Fiscal balance (percent GDP)**	**Expense control**	**Public debt (percent GDP)**	**Fiscal balance (percent GDP)**	**Expense control**
ODA-to-GDP ratio	1.895*** (0.253)	–0.671*** (0.224)	–0.329*** (0.109)	1.181*** (0.313)	–0.924*** (0.256)	–0.345** (0.146)
Manufacturing value added (percent GDP)	–1.927*** (0.213)	0.240*** (0.074)	0.029 (0.096)	–2.236*** (0.364)	0.930** (0.427)	0.185 (0.276)
Reserves-to-GDP ratio	–0.624*** (0.078)	0.059** (0.025)	0.213*** (0.047)	–0.889*** (0.260)	0.047 (0.055)	0.140** (0.063)
Inflation rate	0.335*** (0.101)	0.002** (0.001)	0.001 (0.004)	0.223*** (0.069)	0.002** (0.001)	0.000 (0.003)
GDP per capita growth	–0.817** (0.388)	–0.090 (0.214)	0.675*** (0.159)	–0.817* (0.417)	0.143 (0.183)	0.667*** (0.169)
Bank credit to private sector	0.264*** (0.060)	–0.176*** (0.041)	–0.213*** (0.037)	–0.936** (0.403)	–0.362*** (0.109)	–0.545*** (0.164)
Constant	0.740*** (0.054)	0.012 (0.018)	0.915*** (0.019)	1.108*** (0.146)	–0.018 (0.064)	0.969*** (0.068)
Observations	1,291	1,489	1,489	1,291	1,489	1,489
R-squared	**0.207**	**0.083**	**0.090**			
Country FE	No	No	No	Yes	Yes	Yes
Control for CS correlations	No	No	No	Yes	Yes	Yes
Number of groups				51	52	52

Note: Standard errors are in parentheses. These are robust to general forms of cross-sectional (spatial) and temporal dependence (autocorrelation). *, **, and *** denote significance at the 10, 5, and 1 percent confidence level, respectively.

Source: Staff calculations.

ANNEX 1.4 METHODOLOGY FOR ESTIMATING CURRENCY MISALIGNMENTS

Exchange rate misalignments or currency misalignments represent deviations of real effective exchange rates from their equilibrium level. To the extent that they reflect significant distortions, exchange rate misalignments can have serious adverse consequences on economic growth and development. Several approaches for assessing the extent of exchange rate misalignments coexist in the literature, each referring to a specific definition of equilibrium exchange rates or pertaining to a different time horizon.[24] In this investigation, we rely on the *Behavioral Equilibrium Exchange Rate (BEER)* approach to assess equilibrium real exchange rates since it is a good alternative to PPP-based measures or normative approaches —such as the *Fundamental Equilibrium Exchange Rate (FEER)* approach.[25] The calculation of equilibrium exchange rates requires identifying the long-term equilibrium trajectories of economies which depend on several fundamentals. The *BEER* approach here appears less normative and more pragmatic as it does not require estimate or to make assumptions on the long-run values of the economic fundamentals. Instead, it aims to relate the dynamics of the real exchange rate to that of its fundamentals. This approach is relatively simple and easy to implement and requires few data.

On the operational side, the equilibrium real exchange rate, within the *BEER* approach framework, is assessed through the estimation of a long-run relationship between the real exchange rate and a set of fundamentals—variables influencing the real exchange rate in the long run. This set of fundamentals derives from various theoretical models. Among many, the works of Edwards (1988, 1994) and Hinkle and Montiel (1999) have provided suitable theoretical and empirical frameworks to investigate equilibrium real exchange rates and their fundamentals in developing and emerging countries. We consider four fundamentals that have found to be the most important fundamentals of real effective exchange rates for African economies: the relative productivity of the tradable sector, the net foreign asset position, the terms of trade, and the government consumption. Hence, the long-run relationship to be estimated is the following:

$$reer_{it} = \mu_i + \beta_1 rprod_{it} + \beta_2 nfa_{it} + \beta_3 tot_{it} + \beta_4 gov_{it} + \varepsilon_{it} \qquad (1)$$

where $I = 1, \ldots, N$ and $t = 1, \ldots, T$ respectively indicate the individual and temporal dimensions of the panel. $reer_{it}$ is the real effective exchange rate (in logarithms, an increase in the index indicates a real appreciation); $rprod_{it}$ stands for country i's relative productivity against its trading partners and serves as a proxy of the Balassa-Samuelson effect (also expressed in logarithm); nfa_{it} stands for the net foreign asset position (in percent of GDP); tot_{it} refers to the terms of trade; gov_{it} stands for the government expenditure (in percent of GDP).[26] μ_i are the country fixed effects and ε_{it} is the error term. The improvement of these four fundamentals is expected to appreciate the equilibrium real exchange rate.

First, the Balassa-Samuelson effect describes the convergence process of an economy which results in an appreciation of its real exchange rate through a larger productivity growth in the domestic traded goods. If the real appreciation is in line with the stage of development, the currency of the country will then not necessarily be overvalued.

Second, the connection between real exchange rates and net foreign assets derives from the intertemporal budget constraint which links external assets, real exchange rate and trade balance together, documented by Lane and Milesi-Ferretti (2002). When a country runs a current account deficit, it is building up liabilities to the rest of the world. Solvency requires that the country be willing and able to (eventually) generate sufficient current account surpluses to repay what it has borrowed to finance the current account deficits. Therefore, a country running a current account deficit (borrowing more) may have an overvalued currency: indeed, it should register a more depreciated real exchange rate in order to restore external equilibrium. Conversely, net creditor countries may have an undervalued currency and experience real exchange rate appreciations:

their trade deficit will be indeed offset by investment income on their net foreign asset position.[27]

Third, the impact of changes in the terms of trade on the equilibrium real exchange rate is theoretically ambiguous. On the one hand, an improvement of the terms of trade (an increase in the relative price of exports to imports) leads to a substitution effect. Domestic agents shift their demand toward imported goods and, as a result, the domestic currency will be overvalued: it will have to depreciate to restore the external equilibrium. On the other hand, an income effect due to the improved current account may generate higher demand for non-traded goods. Consequently, prices in the nontraded goods sector tend to rise as well as the general price level, leading in turn to an appreciation of the equilibrium real exchange rate. Empirically, it has been documented that the negative substitution effect of change in terms of trade is not large enough to outweigh the income effect. This is so because imports and domestic goods are imperfect substitutes. It follows therefore that the net result of an increase in the relative price of exports to imports will be an appreciation of the equilibrium real exchange rate.

Finally, the impact of changes in government consumption is also theoretically ambiguous but empirical studies have proven a positive relationship. Indeed, as government consumption is biased toward non-traded goods, a rise in government consumption leads to an increase in the relative price of non-tradable goods and causes the equilibrium exchange rate to appreciate. On the other hand, a growing budget deficit might lead to a depreciation of the real exchange rate.

Following the estimation of equation (1), currency misalignments are obtained from the difference between the observed real effective exchange rate ($reer_{it}$) and its equilibrium level ($reer_{it}$*)—i.e. the fitted value of the real effective exchange rate derived from the estimation of equation (1):

$$Mis_{it} = reer_{it} - reer^*_{it} \qquad (2)$$

Defined in such a way, a negative sign indicates an undervaluation whereas a positive sign indicates an overvaluation of the real effective exchange rate. Estimating the long-term relationship of equation (1) using the Pooled Mean Group (PMG) estimator gives the results in Annex table 1.4.1. The signs of the coefficients associated with the different fundamentals are consistent with predictions. Misalignments are estimated by considering the equilibrium exchange rates calculated from these results. Once the misalignments are estimated, we examine their impact on per capita economic growth in Africa through the following equation (3):

$$Growthpc_{it} = \alpha_i + \delta_1 Mis_{it} + \delta_2 Debt_{it} + \delta_3 Invest_{it} + \delta_4 Tradeopen_{it} + \varepsilon_{it} \qquad (3)$$

Mis represents misalignments (as a percentage), *Debt* is public debt (as a percentage of GDP), *Invest* represents investment (as a percentage of GDP) and *Tradeopen* is the rate of openness to trade measured by the sum of exports and imports relative to GDP.

ANNEX TABLE 1.4.1 Estimation of the exchange rate equilibrium relationship

Variable	(1) Long-run dynamics	(2) Short-run dynamics
EC term		–0.135*** (0.0186)
Relative productivity	0.501*** (0.0415)	–0.0468 (0.0511)
Net foreign asset	0.197*** (0.0368)	0.215*** (0.0423)
Terms of trade	0.145*** (0.0488)	–0.0588 (0.0381)
Government expenditure	0.758*** (0.270)	0.339 (0.235)
Constant		0.658*** (0.0955)
Observations	1,900	1,900

Note: Standard errors are in parentheses. *, **, and *** denote significance at the 10, 5, and 1 percent confidence level, respectively.

Source: Staff calculations

ANNEX TABLE 1.4.2 Impact of exchange rate misalignments on per capita growth in Africa

Variable	(1)	(2)	(3)
External debt (percent of GDP)	−0.015*** (0.004)	−0.015*** (0.004)	−0.014*** (0.003)
Investment (percent of GDP)	0.048*** (0.012)	0.048*** (0.012)	0.045*** (0.011)
Trade openness	0.031*** (0.011)	0.032*** (0.011)	0.030*** (0.011)
Exchange rate misalignments	−0.014*** (0.004)		−0.031*** (0.010)
Manufacturing value added (percent of GDP)			−0.034 (0.029)
Undervaluation		0.001 (0.004)	
Overvaluation		−0.029*** (0.011)	
Undervaluation × Manufacturing VA (percent of GDP)			0.221*** (0.069)
Overvaluation × Manufacturing VA (percent of GDP)			0.039 (0.102)
Constant	−0.344 (0.677)	−0.087 (0.667)	0.363 (0.764)
Observations	1,653	1,653	1,653
Number of groups	44	44	44
Country FE	Yes	Yes	Yes
Control for CS correlations	Yes	Yes	Yes

Note: Standard errors are in parentheses. These are robust to general forms of cross-sectional (spatial) and temporal dependence (autocorrelation). *, **, and *** denote significance at the 10, 5, and 1 percent confidence level, respectively.
Source: Staff calculations.

NOTES

1. Agreed wording at the 2022 AfDB Group Annual Meetings in Ghana. Algeria, China, Egypt, eSwatini, Namibia, Nigeria, and South Africa entered a reservation and proposed “Russia–Ukraine Conflict.”
2. AfDB 2024.
3. OPEC+ is an expanded collation of the 13 members of the OPEC and 11 other non-OPEC members.
4. Zhang and Reyes 2023.
5. Jaramillo et al. 2023.
6. See among others, Elbadawi et al. (2012), Couharde and Sallenave (2013) and Giordano (2023).
7. UNCTAD 2023.
8. A recent study by Moody’s Analytics reveals that Africa (5.5 percent) has the lowest default rates in long-term infrastructure projects compared with other regions of the world (5.9 percent for Western Europe, 8.8 percent for Asia, and 12.9 percent for Latin America).
9. UNCTAD 2023.
10. IMF 2019.
11. Schlegl, Trebesch, and Wright 2019.
12. African Sovereign Debt Justice Network 2024.
13. Onu 2024.
14. Gbohoui et al. 2023.
15. Gbohoui et al. 2023.
16. AEO 2021.
17. Carrasco 1999.
18. Wadhwa 2018.
19. Mo Ibrahim Foundation 2023.
20. Fisher et al. 2019.
21. Agénor 2017.
22. McMillan et al. 2014.
23. Akanbi et al. 2021.
24. MacDonald 2000; Driver and Westaway 2004.
25. Clark and MacDonald 1998.
26. Data on real effective exchange rates are from Bruegel. Relative productivity is computed as the relative real GDP per capita of country *i* vis-à-vis 186 trade partners. Data are from the CEPII (EQCHANGE). Net foreign asset position data are from Lane and Milesi-Ferretti (2023) and terms of trade and government spending are from the World Development Indicators.
27. The *BEER* approach allows taking into account stock effects through the dynamics of the net foreign asset position and of the stock of capital.

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TAKING STOCK OF AFRICA'S ECONOMIC TRANSFORMATION PROGRESS

2

KEY MESSAGES

- **African economies have exhibited remarkable resilience amid multiple shocks, but their structural transformation has been slow and uneven.** Real gross domestic product (GDP) is growing but so is the continent's population. Thus, while real GDP grew on average at 3.8 percent annually over the four decades preceding the COVID-19 period—surpassed only by developing Asia—Africa's real GDP per capita has been consistently growing at one of the slowest rates in the world since the 1980s. Moreover, the structure of most African economies has not changed much since the 1990s, such that traditional sectors have continued to drive Africa's growth and employment. For instance, the agriculture sector, which employs 42 percent of Africa's workforce, is still 60 percent less productive than the whole economy, leaving most African workers stuck in a low-productivity sector and unable to earn enough to escape poverty.

- **In effect, Africa has been transforming without a marked level of industrialization but through a low-skill services sector, mainly because of low manufacturing activity.** The expansion in services employment, which contributed to growth-enhancing structural change, has been matched by a sharp decline in the share of employment in agriculture. This transformation has occurred through the reallocation of economic activities from agriculture to other relatively low-productivity sectors, notably personal and retail services, rather than to more productivity-enhancing manufacturing. But this type of sectoral reallocation has a limited impact on structural transformation. Hence, despite the recent momentum in overall services growth, only 30.1 percent of Africa's services exports in 2022 (20.7 percent in 2005) were in high-skilled services, such as insurance, pensions, finance, and information and communication technology (ICT).

- **Institutions matter for structural transformation, and countries with well-defined and functioning institutions that invest in productivity-enhancing soft and hard infrastructure have transformed their economies.** Empirical evidence suggests that, by being able to reduce transaction costs and information asymmetry, politically stable and less corrupt countries managed to crowd in private investments, boost productivity, stimulate growth, and increase real incomes for households and firms. Countries with high-quality public services coupled with policy consistency are also the most likely to transform their economies because of the citizenry's buy-in of structural and other growth- and employment-promoting reforms. These countries perform relatively well in transforming their economies, efficiently allocating more resources to critical sectors such as education, energy, transport infrastructure, and ICT, which have large potential to foster structural transformation. Quality infrastructure—soft and hard—reinforces the transformational benefits of policy consistency and robust institutions.

- **Recent evidence of growth in high-skill services suggests that the sector can be an engine of Africa's productivity growth, if well harnessed.** In addition to promoting manufacturing to drive Africa's development, there is an emerging pattern suggesting that Africa's industrial policy could also focus on the services sector given its capacity to absorb a large pool of labor and drive future jobs growth. African countries could therefore nurture the services sector and leverage its main features—smaller size firms, high productivity, and greater labor intensity relative to manufacturing—to develop a services-led growth model. This model should include the promotion of tradable and nontradable services such as tourism, business, finance, and ICT, which could bring in foreign exchange to finance Africa's structural transformation.

Domestic resources alone will be insufficient in many African countries to fill their financing gap for structural transformation by 2030

- **Africa will need to close an annual financing gap of about $402 billion by 2030 to fast-track its structural transformation and catch up with high-performing developing countries from other regions.** This financing gap presupposes that the continent prioritizes investment needs in education, energy, productivity, and infrastructure, relating to key Sustainable Development Goals (SDGs) more directly relevant to improving structural transformation. Mobilizing additional resources domestically—including by leveraging investment in the continent's huge endowments in natural resources, especially in critical and rare earth minerals—coupled with enhanced efficiency of public spending, could help bridge a large part of this financing gap.

- **Yet, domestic resources alone will be insufficient in many African countries to fill their financing gap for structural transformation by 2030.** Many African countries have limited fiscal space and low tax capacity, and the private sector remains very risk averse and its participation relatively small, especially toward investment in critical sectors for structural transformation. Thus, given the short period before the SDG deadline, a majority of countries may fail to mobilize domestically such enormous resources to close their financing gap by 2030. For those countries, scattered across the continent's five regions, a more reasonable target and combination of financing options would be to allow for a gradual but steady structural transformation process over a longer period to ensure the mobilization of both domestic and external resources. Regardless of the targeted deadline, however, increased participation of the private sector will be crucial to supplement public resources.

- **Accelerating the pace of Africa's structural transformation will thus require a multipronged approach to enable countries to:**
    - *Establish and institutionalize endogenous development plans and policies tailored to areas of comparative advantage as priorities and implement them consistently, while avoiding policy reversals that tend to disrupt progress.* To address their development challenges, African countries should not outsource their development plans. Instead, they need to take full ownership by harnessing local knowledge of their economies and socio-cultural conditions and other unique areas of comparative advantage, within the national, regional, and global contexts. Continuous and systematic implementation of public policies will create certainty and stability to attract domestic and foreign capital into areas supportive of the structural transformation agenda.
    - *Scale up investments to build requisite human capital suited to local realities, circumstances, and development priorities.* Countries need to scale up investments in education at all levels to build and improve the quality and relevance of technical and soft skills required to drive their development agenda tailored to local contexts and

circumstances. This will require prioritizing systems of learning and curriculum that enhance productivity growth in sectors of comparative and competitive advantages. Domestication of the education and learning and training systems, including the language of teaching, will be crucial to improve the quality and relevance of the education curriculum and to leverage the fourth industrial revolution and ICT boom. Policy priorities should include establishing innovation centers of excellence, in collaboration with host universities and technical and vocational training centers; developing demand-driven skills training programs to better align education and training systems to labor markets and thus reduce widespread skills mismatches; strengthening public–private partnerships to align skills acquisition of graduates with labor market needs; and franchising their education system in partnership with global universities to help build world class education institutions.

- *Scale up domestic resource mobilization and prioritize prudence in public finance management.* Policy priority should be given to improving domestic resource mobilization and prudence in public financial management through, among others, the digitalization of tax administration. This will improve the transparency of the tax system, widen the tax base, enhance enforcement, mitigate compliance risks, and ultimately stimulate voluntary compliance. It will require increasing nontax revenues from property income, royalties, fines, penalties, forfeits, and business permits and enhancing the formalization of the informal economy. And it will require strengthening the social contract through enhanced provision of public goods and services to address widespread implicit taxation and increase voluntary compliance.
- *Build and deepen national and regional markets for goods, services, capital, and finance.* Developing domestic and regional financial and capital markets will reduce countries' dependence on external markets and thus minimize vulnerability to global shocks. Deepening domestic financial markets will require implementing policies to improve property rights' regimes, diversifying the supply of financial products and services in the banking sector, and regionalizing financial markets through legal harmonization and cross-listing of assets at the regional level. Capital market development will require creating an enabling policy and regulatory environment to mobilize at scale and channel resources held by pension funds, insurance companies, and collective investment schemes for financing structural transformation. In this regard, the AfCFTA and the 2022 launch of the Pan-African Payment and Settlement System (PASS) can be a game changer if fully implemented and domesticated by all African countries. Leveraging the PASS, the AfCFTA could further foster domestic and regional economic and financial integration and accelerate structural transformation. Such intra-African "friend-shoring" will help protect the continent from global shocks and strengthen regional value chains while deepening domestic markets. African countries could also facilitate, without nepotism, the emergence of national champions tasked with leading the economic diversification process and fostering the creation of backward and forward linkages with smaller firms, which will result in deepening domestic markets. Policies such as preferred procurement to encourage domestic production and growth of small and medium enterprises and local content and franchising policies to create incentives that will attract investment from multinational corporations, need to be prioritized. Proactive pursuit and promotion of franchising and leveraging the technological know-how of foreign firms can also promote cross-border investment among African countries to complement local content policies and requirements, especially where capacity—technical and financial—is lacking. But to maximize the

Deepening domestic financial markets will require implementing policies to improve property rights' regimes, diversifying the supply of financial products and services in the banking sector, and regionalizing financial markets through legal harmonization and cross-listing of assets at the regional level

By creating a conducive business environment and providing carefully crafted and targeted fiscal incentives, African countries could stimulate the private sector—domestic and external—to invest more in critical sectors of the economy

benefits of franchising, countries must identify domestic capacity gaps and select franchising models that suit their own contexts and serve best their interests.

- *Create targeted and streamlined incentives to catalyze private capital flows to support countries' endogenous development plans in key sectors for structural transformation.* By creating a conducive business environment and providing carefully crafted and targeted fiscal incentives, African countries could stimulate the private sector—domestic and external—to invest more in critical sectors of the economy. Indeed, the potential of the private sector to contribute to Africa's transformation is huge: global assets under management amounted to $98 trillion at end-2022[1] and are expected to reach $145.4 trillion by 2025.[2] In addition, remittances—the largest and most stable source of external funding in Africa—are an important source of external financing. Their function in promoting investment for Africa's transformation can be enhanced through, for instance, diaspora bonds and "remittance securitization." The key policy actions to leverage the private sector investments, including in mobilizing climate finance, were provided in the Bank's African Economic Outlook 2023.
- *Invest in natural capital accounting beneficiation and conservation and include them in the system of national accounts to expand the size of the economy.* Much of Africa's natural capital resources remains largely unexploited, and the values or services they provide are typically poorly measured and sometimes completely unmeasured as part of African countries' wealth. As a result, the value of African economies continues to be underestimated amid the abundance of green wealth. Investing in the measurement and valuation of natural capital and integrating them in the system of national accounts will help estimate the true value of Africa's green wealth,[3] expand its GDP, and improve conservation.
- *Invest in youth entrepreneurship development programs to harness Africa's demographic dividend.* The youth are Africa's greatest asset, which, if well harnessed, could speed up structural transformation. By 2030, one in four youth in the world will be African, and if well nurtured, this youthful population can drive the continent's future economic growth and its structural transformation. However, reaping the benefits of the demographic dividend from African youth would significantly depend on investment in human capital development and creating economic and job opportunities for the youth.

- *Launch an ambitious national infrastructure program for broad-based policy implementation to accelerate structural transformation.* While in the long term, all types of infrastructure are important, in the short term, countries need to prioritize which infrastructure to build depending on their geographic situation and level of development and concentrate limited resources on creating "islands of excellence" with dense and sector-specific infrastructure to boost productive capacities and competitiveness. Priority could be given to the energy sector, which is most likely to achieve a high social rate of return, and to the transport sector, which is especially important for landlocked countries in creating linkages to coastal countries with seaports. Given the significant transformational impact of digitalization, investing in the ICT sector will close the existing digital divide between African countries and the rest of the world. An ambitious national digitalization program in Africa will increase economy-wide competitiveness, enhance the efficiency and transparency of policy implementation, improve domestic resource mobilization, curb illicit capital flows, address widespread market inefficiencies, facilitate proper measurement and valuation of natural capital, and support the competitiveness of youth-led businesses.
  - *Take proactive actions to harness governance of macroeconomic policies and*

business environment to improve risk profiling and perceptions and attract innovative global capital and financial instruments to build capacity in project preparation. The lack of investment-ready project pipelines is often cited among the most important impediment not only to unlocking private finance but also leveraging existing innovative finance instruments. Large infrastructure projects have extensive development and gestation periods and often entail multifaceted feasibility studies and expert transaction advice. Many African governments and local private sector players lack the capabilities, as well as the resources, to design and implement infrastructure projects with commercial potential. Building capacity in project preparation and implementation is therefore crucial.

INTRODUCTION

Many African countries have sustained unprecedentedly high economic growth over the past four decades, with some routinely ranked among the world's 10 fastest-growing economies. This chapter analyzes the extent to which this period of high growth has been accompanied by structural transformation,[4] often defined as the shift of workers from activities and sectors with low average labor productivity to those with high average labor productivity, thus contributing to an increase in average labor productivity for the overall economy.[5]

The analysis in this chapter is akin to the one laid out by Stiglitz (2018), of a multipronged strategy that encompasses all sectors of the economy, specifically including agriculture and services, while recognizing the need for a country to earn foreign exchange through exports and to upgrade its skills via training and technological transfer. Further, the approach acknowledges often-overlooked transformations that can have an important impact on productivity. The starting point for this observation is the idea that structural transformation—within or across sectors—is beneficial in that it is productivity enhancing.

To describe these transformations, the analysis relies on a recent work by Gollin and Kaboski (2024), which reviews an emerging literature that focuses on a set of related patterns of change that accompany the process of growth and development. Instead of focusing entirely on the sectoral dimensions of structural change, this new work considers a broader set of transformations encompassing within-sector transformations likely to raise productivity, such as the movement of people from rural to urban locations; a shift in the locus of production from home to market (and market to home); and a change in the legal structures of work from informal to formal firms and from self-employment to wage employment. This literature opens the door to a more nuanced understanding of the growth process and a wider set of potential policy levers, especially for Africa, where informal, home-based, and other nonmarket activities remain a dominant feature of most economies.

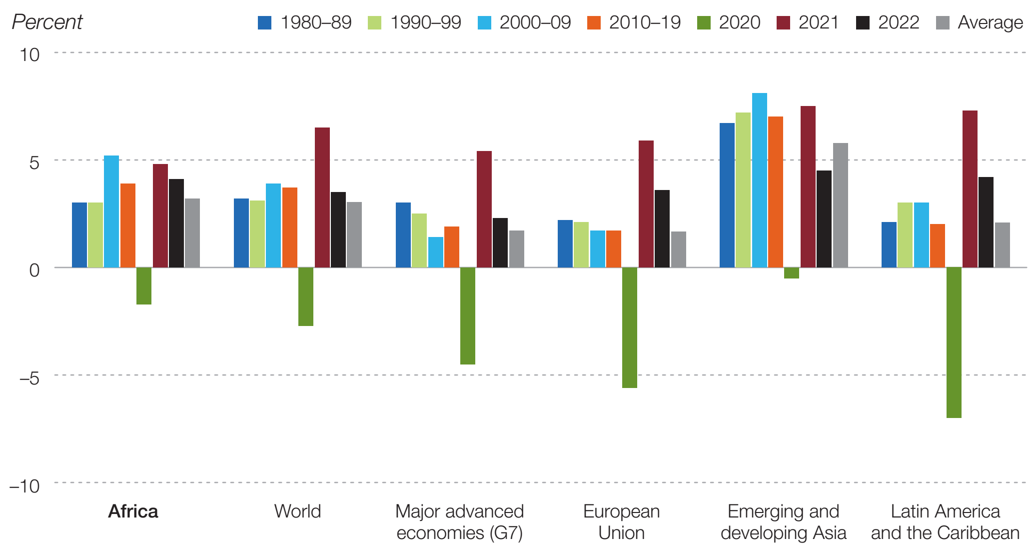
AFRICA HAS PERFORMED REMARKABLY WELL IN REAL AGGREGATE GROWTH BUT NOT IN REAL PER CAPITA TERMS

To the surprise of many observers, and in contrast to narratives of stagnation, Africa's overall economic performance was strong over the four decades preceding the COVID-19 period, with real GDP growing on average at 3.8 percent annually (figure 2.1). The region has also proved resilient to recent shocks including the COVID-19 pandemic and effects of geopolitical tensions: while the growth rate of real GDP decelerated to –1.7 percent in 2020 (the second-lowest decline in the world, after emerging and developing Asia), it rebounded strongly to 4.8 percent in 2021 before slipping to 4.1 percent in 2022, weighed down in part by the effects of Russia's invasion of Ukraine and associated increases in food, fertilizer, energy, and other commodity prices.

Africa has proved resilient to recent shocks including the COVID-19 pandemic and effects of geopolitical tensions

The 1980s and 1990s marked the continent's worst decades of real GDP growth and weaker per capita income growth with attendant deterioration in people's conditions. The average annual real GDP growth rate of the continent in the two

FIGURE 2.1 Africa's real GDP growth compared with the world and world regions, by decade



Note: The decades are based on simple averages.

Source: African Development Bank statistics and IMF World Economic Outlook database.

Africa's overall economic performance was strong over the four decades preceding the COVID-19 period, with real GDP growing on average at 3.8 percent annually

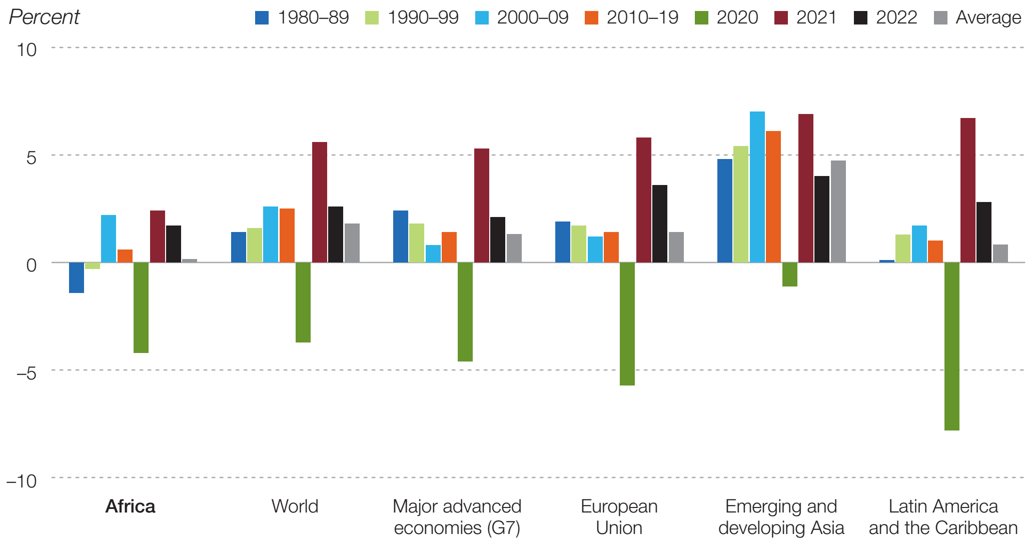
decades was 3.0 percent, a remarkably low value for a continent aiming to catch up to other regions. This performance was attributed to the severe debt crisis that affected numerous African countries, resulting in a weaker investment climate, a lack of trade credit, and a reduction in foreign direct investment, culminating in growth stagnation.[6] Other structural problems, such as poor macroeconomic policies and a heavy reliance on exports of a narrow range of primary products, amid low and falling primary commodity prices, also mattered.[7] Indeed, the 1980s has been termed Africa's "lost decade."[8]

Real GDP growth accelerated again in subsequent decades, with average annual growth rates rising to 5.2 percent in the 2000s before declining to 3.9 percent in 2010–19. By many measures, the mid-1990s to the 2000s marked the continent's boom period. This performance was underpinned by sizable debt relief provided by the international community in the 2000s,[9] combined with the benefits of macroeconomic and structural reforms of the 1990s and the 2003–08 commodity price super-cycle. This period also saw a significant reallocation of labor out of agriculture, most to services but some also to manufacturing.[10]

Relative to other world regions, Africa has therefore done well in real GDP growth during the last two decades. For instance, except for Asia's performance in the 2000s, the growth of Africa's real GDP exceeded those of other world regions in the 2000s and 2010s. Despite recording the first economic recession in more than half a century, Africa was also one of the world regions least affected by the COVID-19 pandemic in terms of growth. Its recovery from the pandemic-induced recession was not only swift but also robust, thanks to steely policy implementation.

In per capita terms, by contrast, Africa's growth performance has not been encouraging (figure 2.2). Africa's average real GDP per capita growth contracted in the 1980s and 1990s, before recovering in the 2000s, and sustaining the momentum in the decade preceding the outbreak of COVID-19. At the height of COVID-19 in 2020, real GDP per capita growth dipped sharply to –4.2 percent, stoking fears of a return to negative growth reminiscent of the 1980s and 1990s. The post-COVID period, however, shows a quick growth rebound in annual real GDP per capita growth, if still trailing that in all other regions.

FIGURE 2.2 Africa's real GDP per capita growth compared with the world and world regions, by decade



Note: The decades are based on simple averages.
Source: African Development Bank statistics and IMF World Economic Outlook database.

STRUCTURAL TRANSFORMATION IN AFRICA: DRIVERS, OPPORTUNITIES, AND BOTTLENECKS

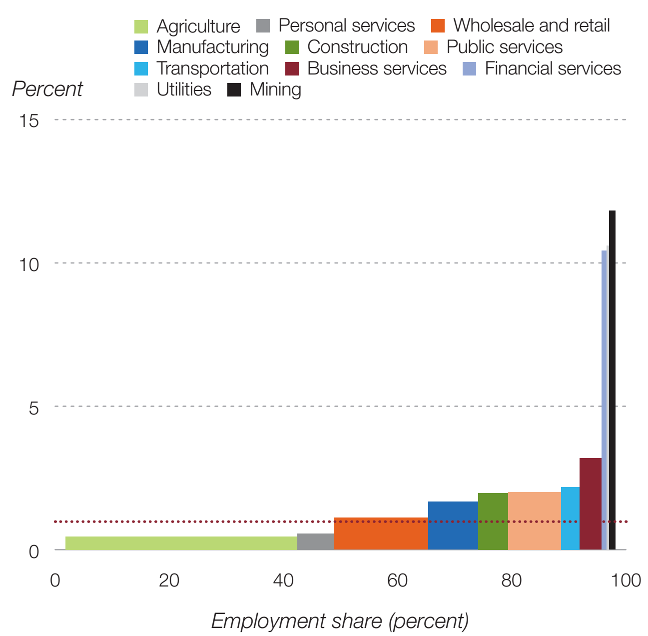
The role of structural change in Africa's recent growth

Similar to other developing regions, Africa is characterized by significant labor productivity gaps between sectors

A frequent finding of the structural change literature is that developing countries display large gaps in labor productivity between sectors.[11] On the one hand, these productivity gaps point toward potential allocative inefficiency;[12] on the other, in the sense of Lewis (1954), the gaps suggest that there may be potential for growth through reallocating labor from less to more productive sectors.[13] This growth is reinforced to the extent that there is also growth *within* sectors, in addition to structural change. Productivity within sectors can increase through capital investment, technological innovation, and intra-industry efficiency gains arising from trade.

Figure 2.3 depicts the relative labor productivity of 11 main sectors in Africa on the vertical axis and the employment share of each sector on the

FIGURE 2.3 Relative sectoral productivity and employment shares in selected African countries, 2018



Note: The figure uses the unweighted average of 21 African countries in the Economic Transformation Database (ETD) for a more detailed sectoral breakdown: Botswana, Burkina Faso, Cameroon, Ethiopia, Egypt, Ghana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Morocco, Namibia, Nigeria, Rwanda, Senegal, South Africa, Tanzania, Tunisia, Uganda, and Zambia.
Source: Staff calculations using the Economic Transformation Database (Kruse et al. 2023).

horizontal axis. Relative productivity is calculated as the ratio of each sector's labor productivity to the average labor productivity of the economy. The horizontal dashed red line represents the productivity level of the economy. The figure highlights significant labor productivity gaps across sectors. Such productivity gaps are not, however, peculiar to Africa—figure A2.1.1 shows similar productivity gaps for developing Asian countries.

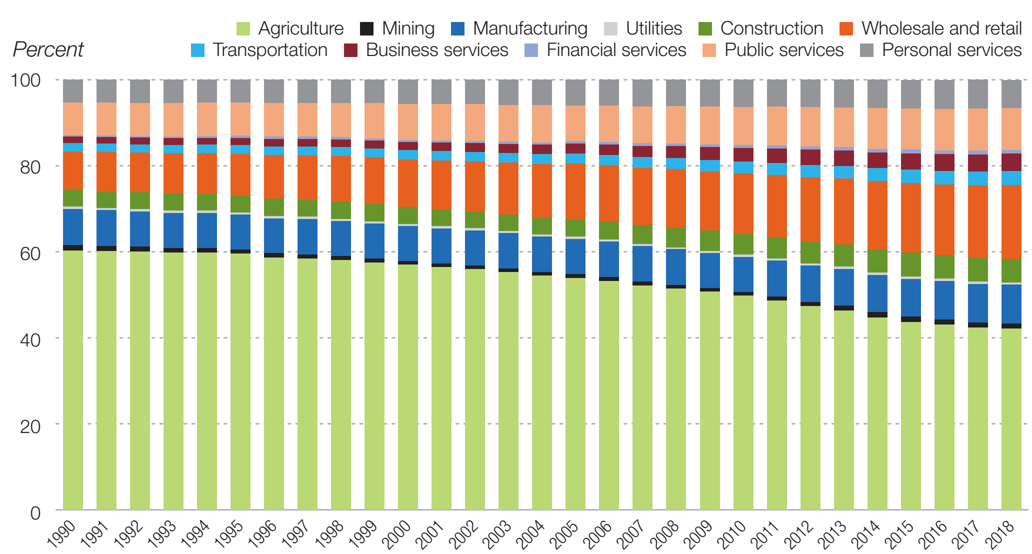
The agriculture sector, which employs 42 percent of the workforce in Africa, is 60 percent less productive than economywide productivity. This may not be surprising, given the level of mechanization and dependence on rainfed production of Africa's agriculture, mostly in rural areas, populated by smallholder farmers. Conversely, mining, utilities, and financial services, which together employ about 3 percent of the workforce, are more than 10 times more productive than the average for the economy. Between these two extremes lies the wholesale and retail sector, which has productivity similar to that of the whole economy, while manufacturing, business services, public services, transport, and construction all have productivity above the economywide average.

The agriculture sector, which employs 42 percent of the workforce in Africa, is 60 percent less productive than economywide productivity

Agriculture, personal services, and wholesale and retail together employ two-thirds of the total workforce but are the least productive sectors in Africa (with relative productivity of 1 or below). Only one-third of the workforce is employed in sectors with productivity above the economywide average. This suggests that there may be some scope for gains in aggregate productivity from the reallocation of labor across sectors. Admittedly, not all the highest-productivity sectors have much potential to absorb additional labor, but even modest movements out of the lowest-productivity sectors seem likely to generate some growth.

For example, while sectors like business and financial services are more productive than manufacturing, their absorption capacity for low-skilled workers is much lower than manufacturing's. The employment share of agriculture decreased from 60 percent in 1990 to 42 percent in 2018 (figure 2.4). More than 8 percent of those workers transitioned to wholesale and retail, with an additional 2 percent moving to personal services. This suggests that more than half of the workers moving out of agriculture were transitioning to sectors whose productivity was either (wholesale

FIGURE 2.4 Sectoral employment shares in selected African countries, 1990–2018



Note: The figure shows the unweighted average of 21 African countries in the Economic Transformation Database: Botswana, Burkina Faso, Cameroon, Ethiopia, Egypt, Ghana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Morocco, Namibia, Nigeria, Rwanda, Senegal, South Africa, Tanzania, Tunisia, Uganda, Zambia.
Source: Staff calculations using the Economic Transformation Database (Kruse et al. 2023).

and retail) the same as or (personal services) lower than that of the whole economy.

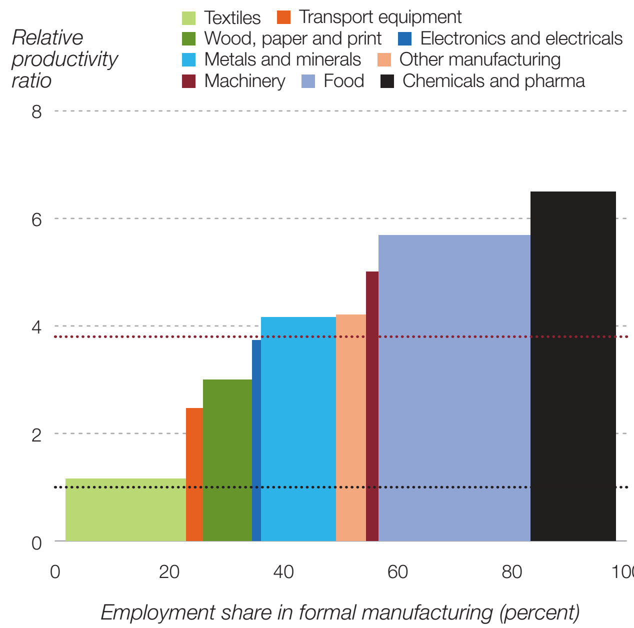
The employment share of the manufacturing sector, traditionally associated with structural change due to its high capacity for absorbing low-skilled workers, increased by only 0.6 percentage points between 1990 and 2018, to only 9.0 percent. A positive development is that tradable and relatively productive services, such as transport, business, and financial services, together accounted for 4.4 percent of the workers who moved out of agriculture. Construction and public services accounted for the remaining 3.6 percent.

Beyond absorbing fewer workers in recent years, manufacturing's relative productivity is below that of tradable services, such as business and financial services. Moreover, Africa's manufacturing is characterized by a growing number of small and informal firms that experience employment growth but little or negative productivity growth.[14] Manufacturing is also heterogeneous for productivity and employment absorption capacity. For example, while the textile sector is relatively labor intensive but has low productivity, the chemical and pharmaceutical sector, which is capital and technology intensive, has higher productivity.

Figure 2.5 displays the relative productivity level of (formal) manufacturing industries and their share of employment, and shows that all manufacturing industries have a productivity level above the economywide average, ranging from 1.15 times higher in textiles to 6.5 times higher in chemicals and pharmaceutical industries. The average productivity of the formal manufacturing sector is also 3.8 times (shown by dark red dotted line) that of the aggregate economy, and it is significantly higher than that of the aggregate manufacturing sector (inclusive of small and informal manufacturing), which is only 1.9 times that of economywide productivity (shown by black dotted line).

Extensive research has identified key factors that have contributed to the historical significance of manufacturing in the economic progress of today's middle- and high-income countries. These factors include the sector's high potential for productivity due to technological advances, increasing returns to scale, and the ability to trade its products.[15] Additionally, manufacturing has demonstrated substantial linkage effects

FIGURE 2.5 Productivity differences in selected African countries' manufacturing industries



Note: African countries covered in the 2-digit manufacturing database are Botswana, Cameroon, Ethiopia, Egypt, Ghana, Kenya, Malawi, Mauritius, Morocco, Namibia, Nigeria, Senegal, South Africa, Tanzania, Tunisia, and Uganda. The figure shows the unweighted average of these 16 countries. The relative productivity is the ratio of each sector's productivity to the average productivity of the economy.

Source: Staff calculations using the Economic Transformation Database and its 2-digit manufacturing database.

with other segments of the economy,[16] absorbed large swaths of low-skilled workers,[17] and tended to converge toward the productivity levels of advanced economies given the transferability of production-related knowledge.[18]

This characterization oversimplifies, however, the evolving nature of sectoral activities. For example, the rapid technological advances seen in recent decades have greatly altered employment absorption within large manufacturing firms, particularly for low-skilled workers.[19] Conversely, many nonmanufacturing sectors have undergone transformation. In Africa, Newfarmer et al. (2018) highlight the emergence of nonmanufacturing "industries without smokestacks," which increasingly exhibit the set of characteristics traditionally associated with manufacturing. These sectors include agroindustrial and horticultural value chains, as well as trade and business services, particularly in ICT. The tourism sector also falls in this category. Such shifts in fundamental sectoral characteristics may diminish the traditional distinction between manufacturing and services sectors, in particular on productivity, thus elevating the role of the latter in modern structural change.

Even within sectors such as wholesale and retail trade or retail food services, the evidence is clear that—in rich countries, at least—there is potential for rapid productivity growth through economies of scale and scope. Businesses like McDonald's, Walmart, and Amazon show the potential for services firms to grow through standardization of products, economies of scale, and complex organizational structures. It would surely be a mistake to imagine that productivity growth in services is limited to a small set of high-value sectors.

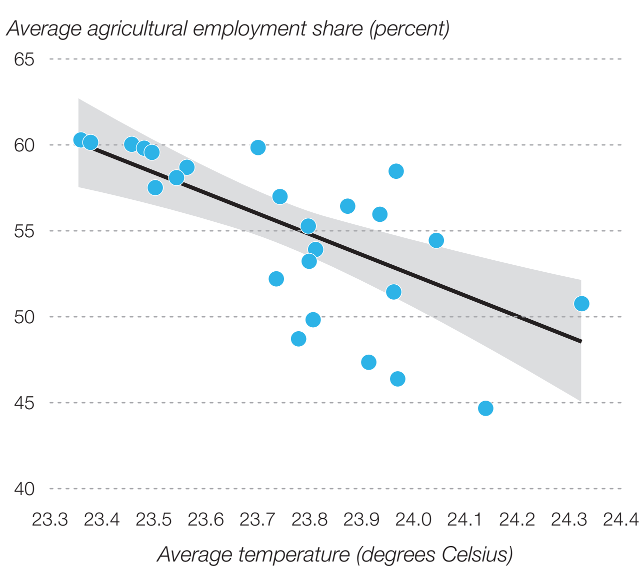
Countries with higher mean temperatures in Africa have fewer workers in agriculture

Africa's structural change is also characterized by the reallocation of economic activities from agriculture to other relatively low-productivity sectors

A second characteristic of Africa's structural change in recent decades, as observed from the graphs above, is the reallocation of economic activities from one low-productivity sector—agriculture—to other relatively low-productivity areas, such as personal and retail services. More than half of the workforce leaving agriculture are entering these activities. These are potential sectors well suited to workers leaving agriculture—skills requirements are not very different, and capital requirements are small.

But there is a possibility that some of the movement out of agriculture reflects "push" factors rather than "pull" factors. For instance, climate change may be acting as a push factor, driving people out of agriculture. Evidence suggests that countries with higher mean temperatures in Africa have fewer workers in agriculture (figure 2.6). Indeed, a 1-degree increase in temperature is associated with more than a 10-percentage point decrease in the agricultural employment share. Policies for addressing effects of climate change should therefore be an integral part of African countries' endogenous development strategies with the support of the international climate finance system (see chapter 3, this report, for more details). Further, evidence also suggests that recurrent conflicts across the continent, particularly in regions such as the Sahel and the Horn of Africa, have further served as a push factor out of agriculture. Data for 1980–2016 show that one-third of conflicts in Africa have been preceded by a natural disaster within seven days,[20] which exacerbated food insecurity and disrupted agricultural value chains. In addition, findings suggest that agricultural production may fall heavily in regions affected by conflict, due to adverse effects on labor supply, access to land, access to credit, and/or direct effects on capital such as theft and destruction.[21]

FIGURE 2.6 Climate change and agricultural employment shares in Africa, 1991–2018



Source: Staff calculations using data from Economic Transformation Database (Kruse et al. 2023) and data from Acevedo et al. (2020).

African economies' slow transformation means that close to half of the continent's countries are "structurally underdeveloped"

Based on their sectoral employment shares, African economies can be categorized by their stage of structural transformation.[22] The first set are those where agriculture is still the largest sector by employment share in the most recent period with data. These economies are considered *structurally underdeveloped*. The next set of economies are those where more people are employed in services than in agriculture, with agriculture the second-largest sector—*structurally developing*. The final set are those with more people employed in manufacturing/industry than in agriculture—*structurally developed*.

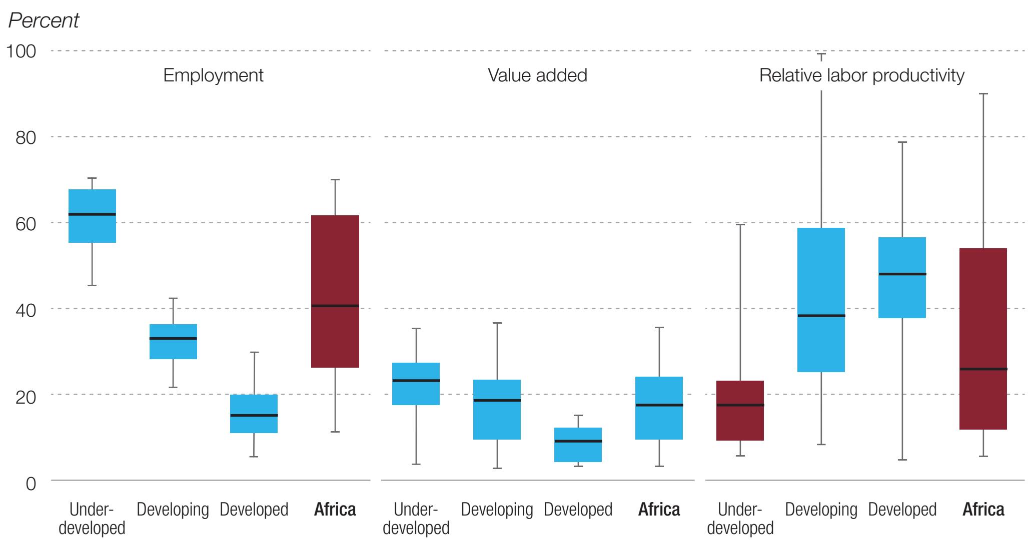
Twenty-five African countries (46.3 percent) are still structurally underdeveloped (per the latest data), based on sectoral employment shares, with agriculture absorbing at the median 61.9 percent of total employment in 2021, more than 21 percentage points higher than the median continental value of 40.6 percent (figure 2.7). These countries are still at the early stages of structural transformation, with large productivity gaps across sectors—median agricultural labor productivity is only 17.5 percent that of non-agriculture sectors, with a median share of agriculture in GDP at about 23.2 percent. In only about one-fifth of African countries do industrial workers outnumber agricultural workers. In these structurally developed countries, agricultural value added accounts for only 9.1 percent of GDP, the lowest share among countries, and its productivity is close to half (48 percent) that of non-agriculture sectors.

Besides the above differences, these three categories of countries also present distinct economic features (figure 2.8). A typical structurally underdeveloped African country is a low-income economy with a median per capita GDP of $882 in 2021, respectively more than two and four times less than the level of structurally developing ($2,066) and structurally developed ($3,754) countries (figure 2.8a). Structurally underdeveloped and developing countries are further characterized by a low Economic Complexity Index (ECI), an indicator that measures how diversified and complex the export basket of a country is (figure 2.8b). Against their peers, this implies that these countries are home to a low diversity of productive know-how—in particular, complex specialized know-how—and thus struggle to produce a wide diversity of sophisticated, high-value products.

This low ECI is confirmed by their level of export concentration in a few products, giving them a high Export Concentration Index (figure 2.8c), thereby making them more vulnerable to global shocks than structurally developed countries where exports are more homogeneously distributed among a series of products. Both structurally underdeveloped and developing countries show relatively weak governance quality (figure 2.8d), on

Only twelve African countries are structurally developed, based on sectoral employment shares

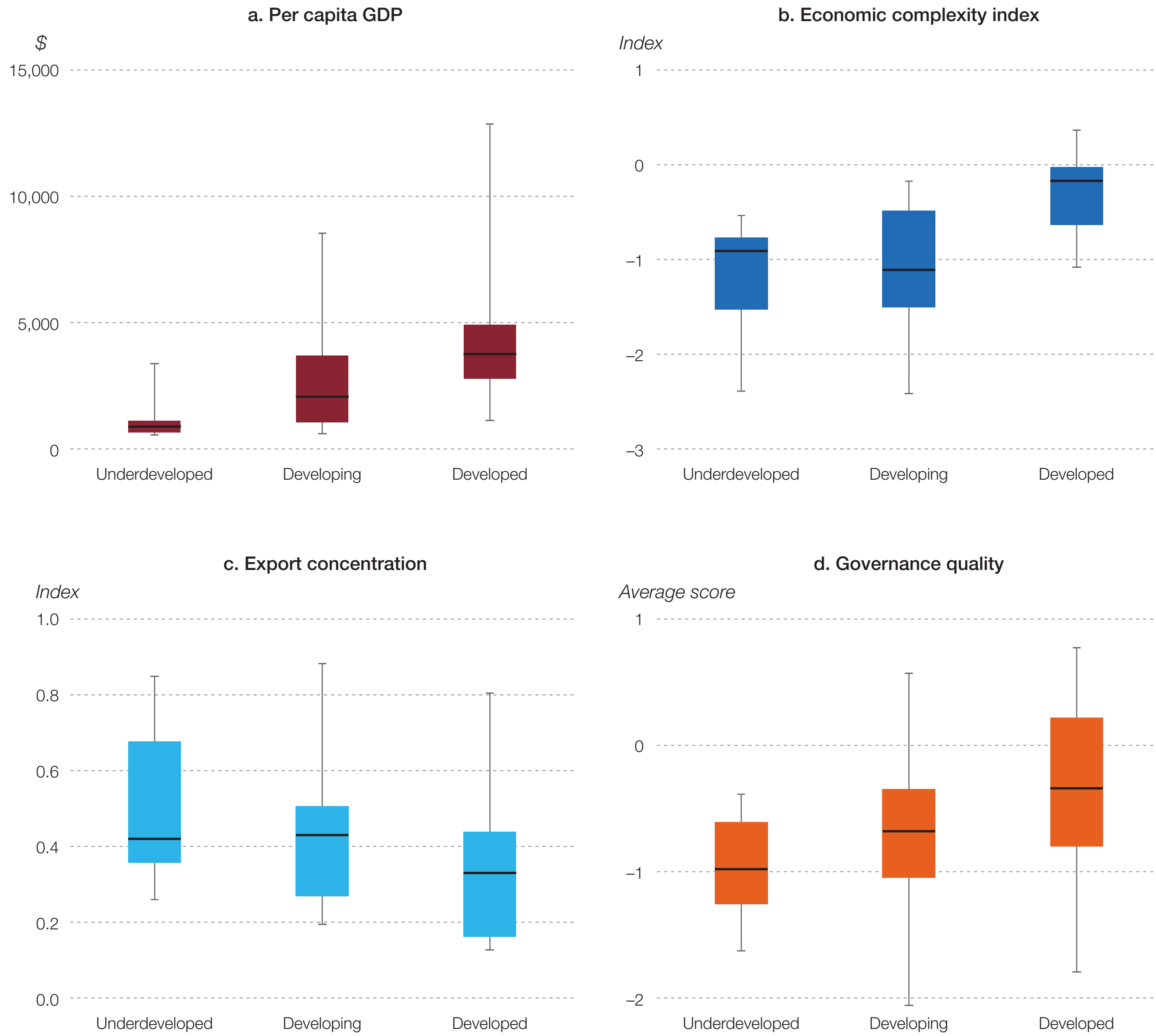
FIGURE 2.7 Agricultural employment, value added, and relative labor productivity by stages of structural transformation in Africa, 2021



Note: Employment and value added are expressed as a percentage of total employment and GDP, respectively. Relative labor productivity is the ratio of labor productivity (value added per worker) in agriculture to non-agriculture sectors (industry and services). Median values are reported. Latest available years are used.

Source: Staff calculations based on World Bank and ILO databases.

FIGURE 2.8 Key features of African countries by stages of structural transformation, 2021



Note: The Economic Complexity Index summarizes countries' collective productive knowledge based on the diversity of exports and their ubiquity (number of countries that export the product). The Export Concentration Index, also called the Herfindahl-Hirschmann Index, is a measure of the degree of product export concentration. An index value closer to 1 indicates that a country's exports are highly concentrated in a few products. Values closer to 0 reflect exports are more homogeneously distributed among a series of products. Governance quality is the average value of the following World Bank governance indicators: control of corruption, government effectiveness, political stability and absence of violence/terrorism, regulatory quality, rule of law, and voice and accountability. Each governance indicator ranges from –2.5 to 2.5.

Source: Staff calculations using databases from the Harvard University Atlas of Economic Complexity, UNCTAD, and the World Bank's World Development Indicators.

control of corruption; government effectiveness; political stability and absence of violence/terrorism; regulatory quality; rule of law; and voice and accountability. This undermines their economic growth and development prospects[23] and their ability to withstand negative growth shocks.[24]

The number of countries within each category has not been static over the past three decades, however. The number of structurally underdeveloped countries has been declining, from 40 (or 75.5 percent of African countries) in 1991 and 38 countries (or 71.7 percent) in 2000 to 26 countries or less since 2015 (figure 2.9), suggesting that structural transformation may be underway. Over the same period, the number of structurally developing countries increased from five (9.4 percent) to 17 (31.5 percent).

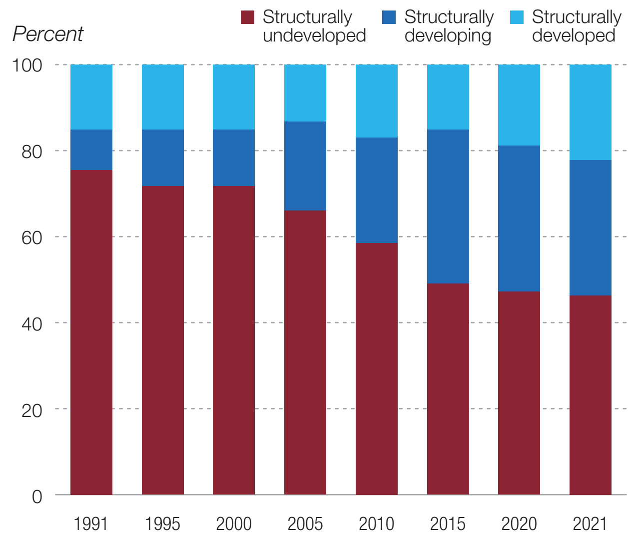
Quantifying the role of structural transformation in Africa's economic growth

Labor reallocation from agriculture to services has fed into growth-enhancing structural change in Africa

The implication of reallocating labor mainly from agriculture, where productivity is below the economy's average, to services, where productivity is above that average, has fed into growth-enhancing structural change in Africa, although this has occurred within the context of moderate productivity performance. Figure 2.10 shows the decomposition of labor productivity in Africa and other developing regions, per McMillan and Rodrik's methodology (box 2.1). Labor productivity in Africa grew at 1.5 percent a year in the 1990s, approximately 3 percent in the 2000s, and 2 percent in the 2010s. This growth is attributed primarily to productivity growth within agriculture, combined with structural change. About half of the labor productivity growth in the 2000s and 2010s is attributed to structural change.

Productivity growth within non-agriculture sectors is limited, particularly in the 2010s, which is consistent with the argument that when labor and other resources shift from less productive sectors (such as agriculture, in Africa) to more productive activities (mostly services, in Africa), the economy grows even in the absence of within-sector productivity growth.[25] The structural change effect is, however, self-extinguishing if non-agriculture sectors do not experience rapid productivity growth.[26] If the current pattern of less dynamic productivity growth within non-agriculture sectors continues, overall labor productivity growth will eventually stall in Africa. Policies aimed at boosting productivity within modern sectors such as manufacturing and

FIGURE 2.9 Percentage of African countries by stages of structural transformation, 1991–2021



Source: Staff calculations based on World Bank and ILO databases.

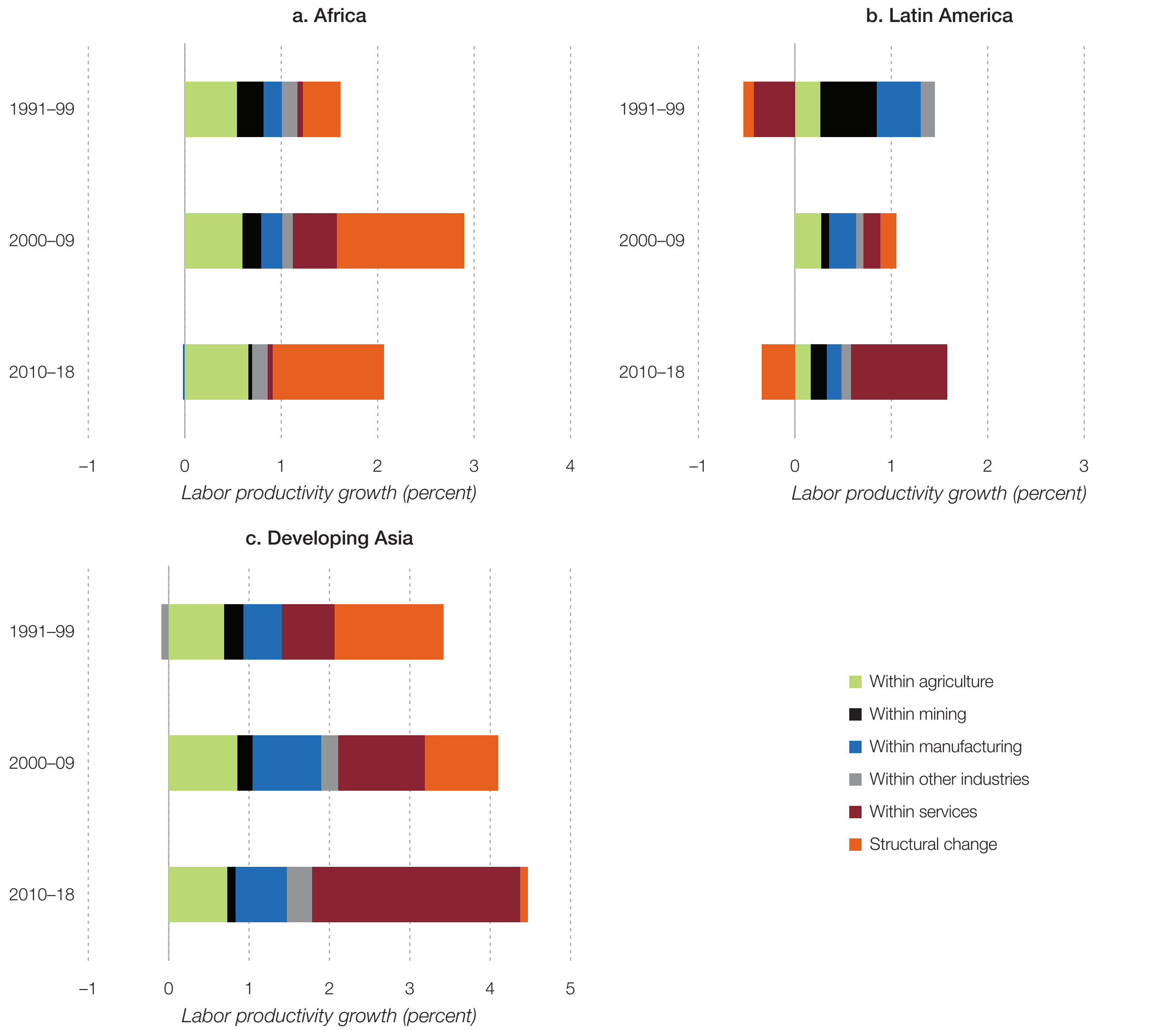
services are therefore imperative for maintaining Africa's structural transformation.

Africa's structural change is stronger than that in developing Asia and Latin America, especially in the 2000s and 2010s, but developing Asia demonstrates stronger labor productivity growth due to robust within-sector productivity growth (see figure 2.10). Surprisingly, structural change in developing Asia has been limited in the past decade. Even more concerning, structural change was growth reducing in Latin America in the 1990s and 2010s, partly reflecting moves to liberalize trade and rationalize manufacturing.[27] In developing Asia and Latin America, the "within" component dominates the contribution of structural change to annual labor productivity growth. Conversely, in Africa, the contribution from structural change dominates, contributing about 56 percent of total annual labor productivity growth in the 2010s, which is not surprising given that African countries have, on average, the highest shares of employment in agriculture. Growth could, though, be accelerated if within-sector productivity grew.

Patterns of structural change by income groups, resource groups, and regions of Africa

The Economic Transformation Database (ETD) data used to compute structural change covers only 21

FIGURE 2.10 **Structural change in Africa and other developing regions, 1991–2018**



Note: The figure shows the unweighted average of 21 African countries in the Economic Transformation Database; the unweighted average of 14 developing Asian countries: Bangladesh, Cambodia, China, India, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Nepal, Pakistan, Philippines, Sri Lanka, Thailand, and Viet Nam; and the unweighted average of 9 Latin American countries: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, Mexico, and Peru.

Source: Staff calculations using the Economic Transformation Database (Kruse et al. 2023).

out of the 54 countries in Africa, but these countries account for more than three-quarters of the continent's population and GDP.[28] To provide a more comprehensive analysis, this section incorporates sectoral value-added data from the World Development Indicators (WDI) and sectoral employment data from the International Labour Organization (ILO), both covering 48 African countries.

A limitation of the sectoral value-added data from the WDI is that they are aggregated into only three broad sectors: agriculture, industry, and services. Unlike the ETD, WDI data do not distinguish between manufacturing, mining, and other industries. Still, the data cover diverse groups of countries by income, resources, and regions. Using these data, this section now explores how

BOX 2.1 Decomposition of labor productivity: methodology

The decomposition method is based on McMillan and Rodrik (2011). As explained above, labor productivity can grow in two ways. First, productivity can grow within sectors through capital investments, technological innovations, efficiency gains arising from intra-industry trade, and reduction of misallocation within sectors. Second, productivity can grow through the reallocation of labor from low- to high-productivity sectors—the "structural change" component.

Aggregate labor productivity growth at time is defined as the weighted sum of sectoral productivity, with the weights being the employment shares, that is:

$$p_t = \sum_i p_{it} s_{it} \tag{1}$$

where p_{it} is labor productivity of sector i in time t given by $p_{it} = VA_{it} / l_{it}$, with VA_{it} being sector i's real value-added and l_{it} being the number of persons employed in sector i at time t. s_{it} is the sectoral employment share defined as the ratio of each sector's employment to the total employment of the economy at time t. Equation 1 can be decomposed as:

$$p = \frac{\Delta p}{p_{t-1}} = \sum_{i=1}^{N} \left[\frac{(p_{it} - p_{it-1}) s_{it-1}}{p_{t-1}} \right] + \sum_{i=1}^{N} \left[\frac{(s_{it} - s_{it-1}) p_{it}}{p_{t-1}} \right] \tag{2}$$

where N is the number of sectors analyzed. The first term on the right-hand side is the *within* effect, and the second term is the "structural change" effect.

factors such as income level, geographic location, and resource endowments contribute to distinct patterns of structural transformation and economic growth across the continent.

By income group

Figure 2.11 illustrates productivity differences in low- and middle-income countries in Africa across three decades—the 1990s, 2000s, and 2010s. The figure shows that as the sample size increases from 21 (as in the ETD) to 48 (as in the WDI and ILO data), productivity growth decreases. Because the ETD covers mainly wealthier African countries, the above finding may imply weaker productivity growth in countries not included in the ETD. This observation is supported by the fact that when using the WDI and ILO data and restricting it to a subset of countries in the ETD sample, identical results are obtained.

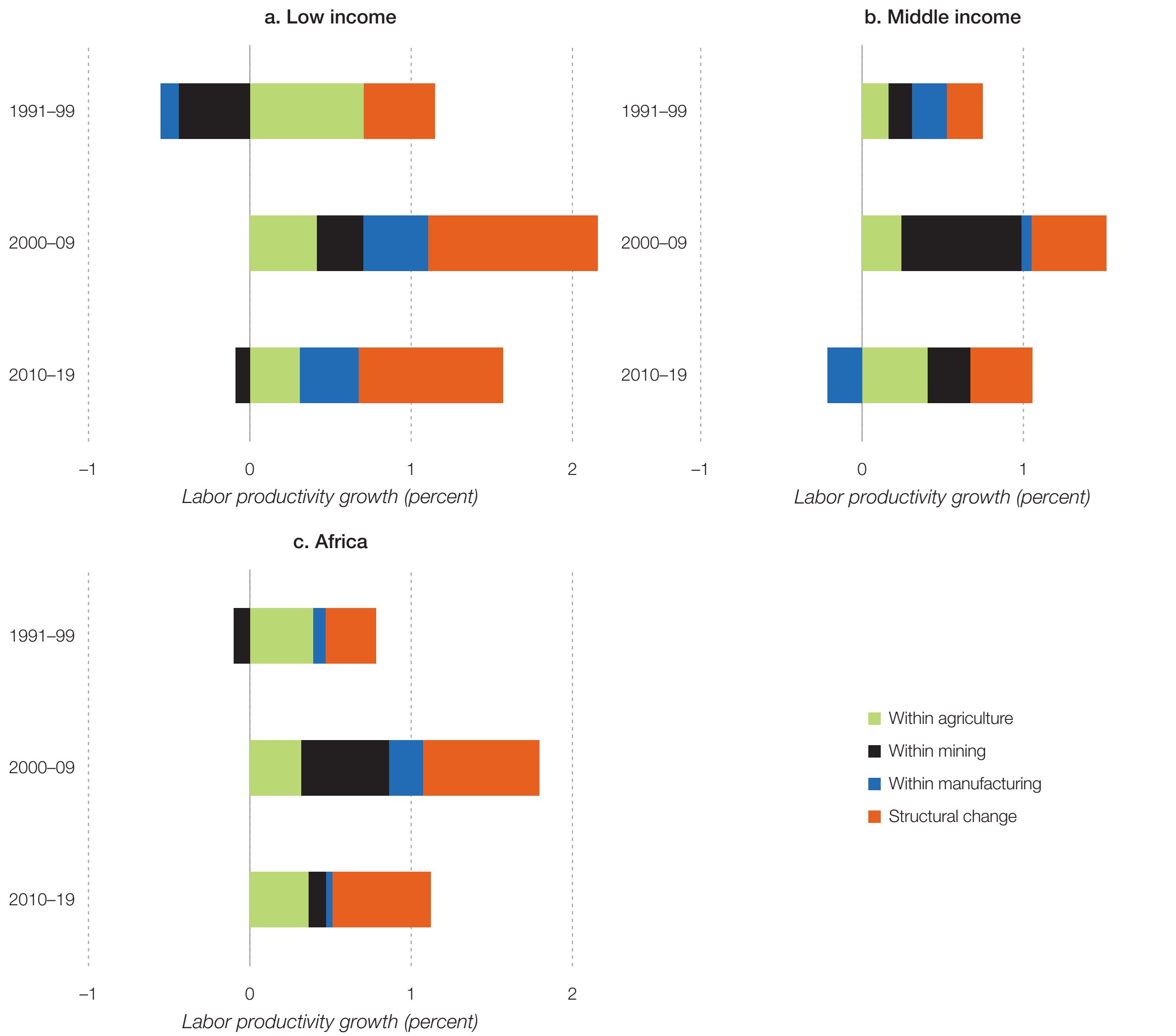
In addition, most countries not included in the ETD have a pegged exchange rate to the euro. While that provides stability and policy certainty, it renders the tradable sector uncompetitive, hindering structural change and productivity growth. Further, many of these countries are in the Sahel region, which is prone to extreme climate conditions, conflict, and other forms of fragility, rendering them less attractive to foreign investment.

As expected, structural change occurs more rapidly in low-income countries, particularly in the last two decades, as they are still at the early stages of structural transformation. Low-income countries typically have a high proportion of agricultural labor. According to Lewis (1954), this surplus agricultural labor tends to drive faster structural change. Another notable trend is that while productivity growth within industry is positive in low-income countries, it was negative in middle-income countries in the 2010s. Still, the evidence in Diao et al. (2021) indicates that productivity growth in formal manufacturing firms has been strong for both a low-income country (Ethiopia) and a lower-middle-income country (Tanzania). Together, the negative growth in the industrial sector points to the emergence of an informal manufacturing sector in Africa, with rapid employment growth but negative productivity growth.[29]

Resource group

Patterns of productivity growth among resource groups are also markedly different. In tourism-dependent countries, oil exporters, and other

FIGURE 2.11 Aggregate labor productivity growth: contribution from within and structural change, Africa and by income groups, 1991–2019



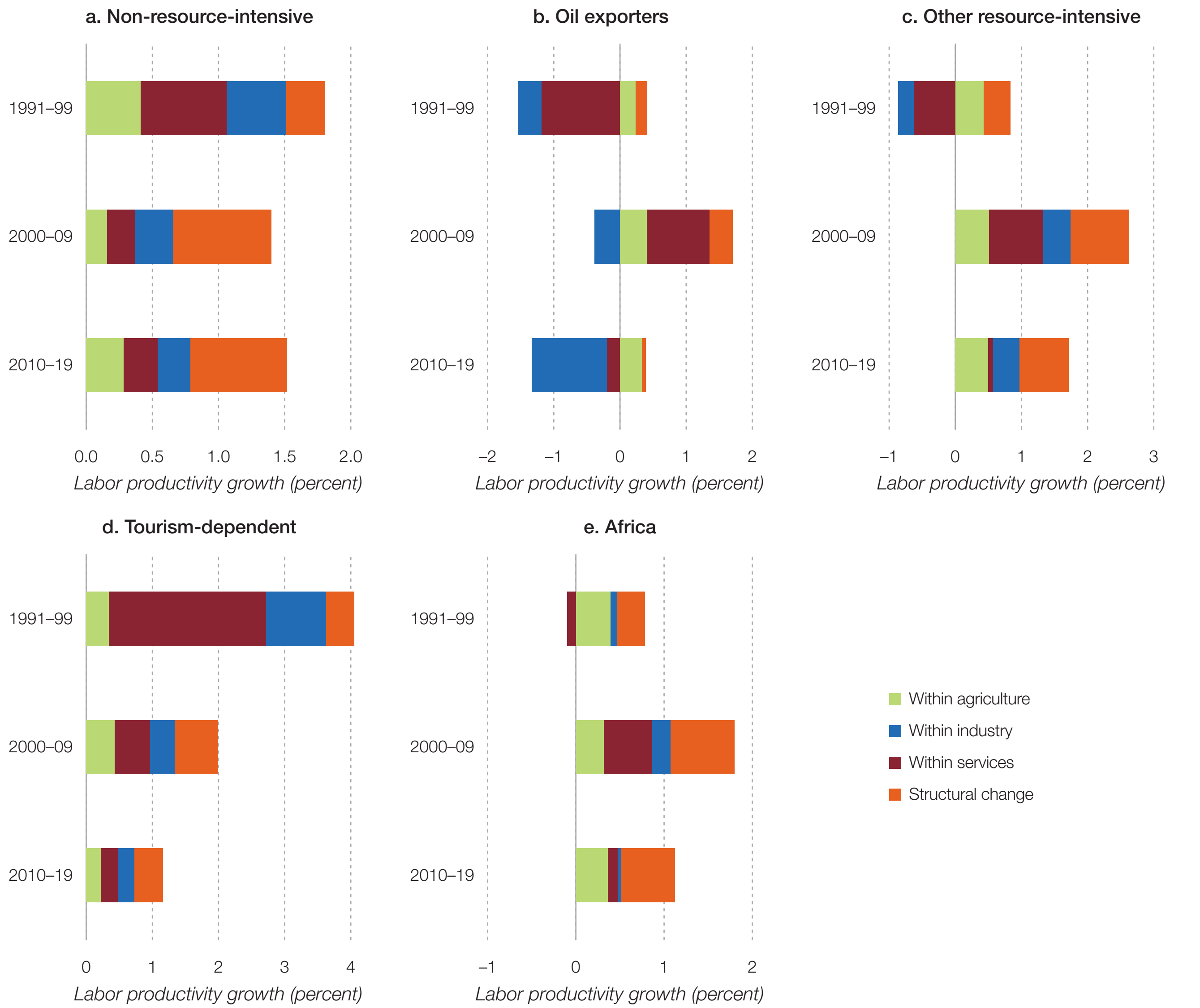
Note: See country classification in chapter 1 (annex A.1.2).

Source: Staff calculations using employment and value-added data from the ILO and WDI, respectively.

resource exporters, significant productivity growth stems from within-sector productivity growth, particularly within services for tourism-dependent countries and within natural resources for oil and other resource exporters. The contribution of structural change to productivity growth was particularly strong among non-resource exporters, especially in more recent years, signaling relative diversification and the attendant benefits to economic growth in these countries (figure 2.12).

Another highlight is the high volatility of growth in oil-exporting countries compared with non-resource exporters and tourism-dependent countries. During the last commodity price boom (2004–14), economic growth soared to a record high in resource-rich countries on the back of high commodity prices, but this growth proved fragile and heavily reliant on external factors. Since the decline in commodity prices after 2014, resource-rich African countries have experienced slower growth

FIGURE 2.12 Aggregate labor productivity growth: contribution from within and structural change, Africa and by resource groups, 1991–2019



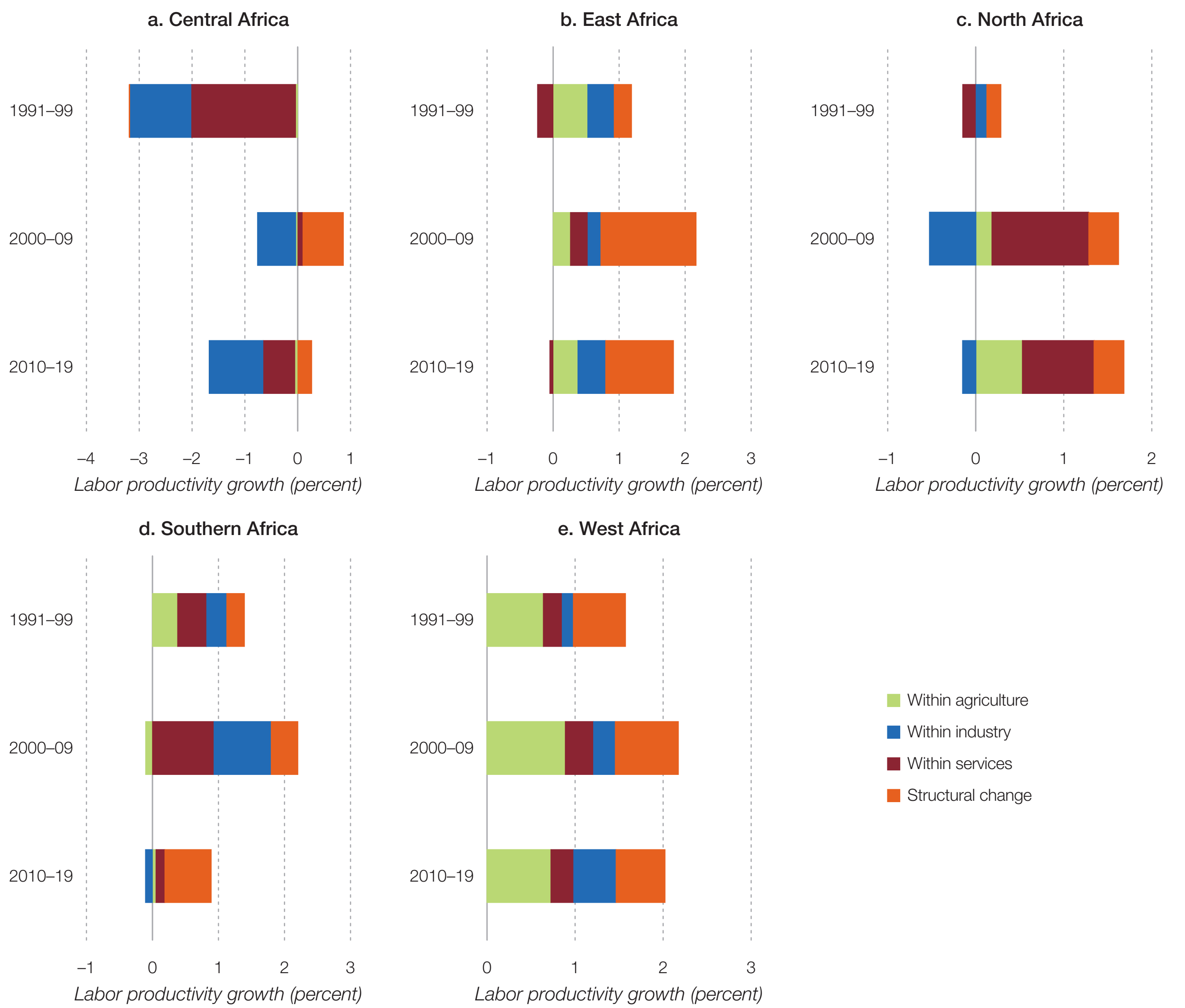
Note: See country classification in chapter 1 (annex A.1.2).
Source: Staff calculations using data from ILO and WDI.

than the regional average. Following the commodity price boom, annual GDP per capita growth in resource-rich countries averaged 2.5 percentage points less than in the boom years and 1.5 percentage points less than in non-resource-rich countries within the continent. This underscores the importance of decoupling growth from dependence on primary raw materials from natural resources, and instead, of focusing on promoting diversification, so as to enhance economic resilience.[30]

By African region

Across African regions, important differences in performance stand out (figure 2.13). The average growth rates of labor productivity from 1991 to 2019 show that Central Africa grew by –1.3 percent a year, East Africa 1.7 percent, North Africa 1.2 percent, Southern Africa 1.5 percent, and West Africa 2.0 percent. In Central, West, and North Africa, significant productivity growth comes from within sectors. For instance, in Ghana and Nigeria, two of West Africa's

FIGURE 2.13 Labor productivity growth decomposition by African region, 1991–2019



Source: Staff calculations using employment and value-added data from ILO and WDI, respectively.

largest economies, almost 100 percent and 80 percent, respectively, of average productivity growth comes from within-sector productivity growth. In the rest of West Africa, structural change tends to stand out more. For instance, although the within-sector effect looms larger in the growth process in Burkina Faso and Togo, the contribution from structural change still dominates, as in the Republic of Congo in Central Africa, despite a substantial contribution from within-sector productivity growth.

In East Africa, structural change contributes more than within-sector productivity growth to labor productivity growth, as in Rwanda and Tanzania, for instance, unlike Ethiopia and Uganda, where the contribution from within-sector productivity growth dominates. In Southern Africa, significant productivity growth comes from within sectors, with moderate contributions from structural change.

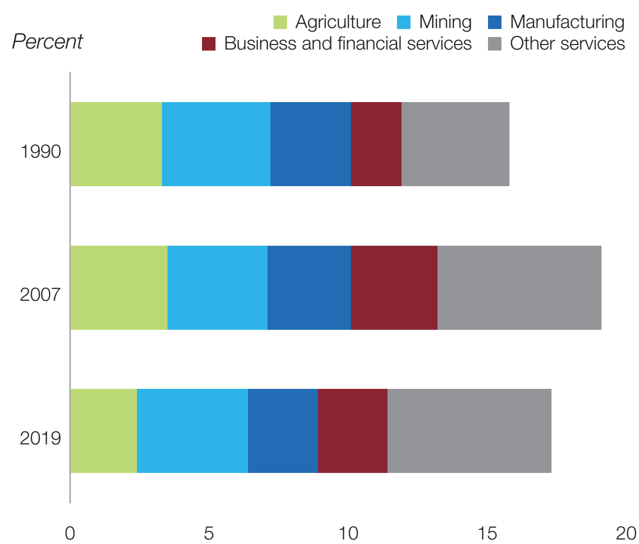
New evidence on the rapid growth in incomes and jobs embodied in services exports

Contrary to the mainstream view of development, which often emphasizes supply constraints, Goldberg and Reed (2023) highlight the significance of demand as a constraint to structural change in developing countries, particularly in Africa. They underscore the role of foreign demand and integrated markets in driving structural change in African countries, most of which are constrained by small market size. The authors do not, however, consider the possible effects of expanded market size through the AfCFTA, which could provide comparative advantages to the continent to fast-track structural transformation.

After around two decades of inward-looking development strategies, most African countries opened to regional and global markets in the 1990s. The question arises: has this newfound market access impacted sectoral exports, productivity, and job creation in Africa? Mensah and de Vries (2024) address this question using the newly released Africa Supply and Use Tables (ASUT) Database. They calculate the domestic value added and jobs embodied in exports using the hypothetical extraction method introduced by Los et al. (2016). This method considers the ratio of value added to gross output, and the ratio of employment to gross output, to compute the value added and the number of jobs embodied in exports, respectively. Figure 2.14 and table 2.1 show striking changes in these metrics by sector.

Figure 2.14 shows that the share of domestic value added embodied in exports is decreasing in agriculture, remaining largely the same in mining, slightly decreasing in manufacturing, and increasing in services. The results are consistent with the broad patterns of structural change documented above where services are the driving force behind African countries' recent structural changes. Mensah and de Vries (2024) observe that the rising share of domestic value added in manufacturing during the 2000s, followed by a decrease in the 2010s, is primarily driven by manufacturing activities anchored on natural resources, such as petroleum refining and fabricated metal products. This analysis suggests that the contribution from other manufacturing industries remains stagnant,

FIGURE 2.14 Sectoral domestic value added embodied in exports (percent of GDP), 1990, 2007, and 2019



Source: Reproduced from Mensah and de Vries (2024); see table 2.1 source.

TABLE 2.1 Number of jobs embodied in exports, 1990, 2007, and 2019

	Jobs induced by foreign demand (thousands)			Share (percent of total employment)		
Sector	**1990**	**2007**	**2019**	**1990**	**2007**	**2019**
Agriculture	6,406	10,430	7,858	6.3	6.6	3.2
Mining	1,895	2,715	2,392	1.9	1.7	1.0
Manufacturing	4,077	7,746	8,643	4.0	4.9	3.5
Business and financial services	106	425	1,106	0.1	0.3	0.4
Other services	1,146	3,027	6,545	1.1	1.9	2.6
Total	**13,628**	**24,343**	**26,544**	**13.3**	**15.5**	**10.7**

Source: Reproduced from Mensah and de Vries (2024). The value added and jobs embodied in exports are computed using the Africa Supply and Use Tables (ASUT) Database. The figure and table show the unweighted average of the 11 African countries covered in the database: Cameroon, Ethiopia, Ghana, Kenya, Mauritius, Nigeria, Rwanda, Senegal, Tanzania, South Africa, and Zambia.

a finding consistent with the general observation that the export-oriented sector of manufacturing is not expanding. Instead, most manufacturing firms are producing to meet local demand,[31] which could be dominated by food and food processing and allied subsectors, such as manufacturing of packaging products.

According to table 2.1, jobs embodied in exports nearly doubled over three decades, increasing from more than 13.6 million in 1990 to more than 26.5 million in 2019. The share of jobs embodied in exports decreased for all sectors except services, although the share of services started from a lower value. While the share of jobs embodied in services exports is increasing rapidly, the total share of jobs embodied in these exports (3 percent) is still lower than that of manufacturing (3.5 percent) and agriculture (3.2 percent).

A significant reallocation of workers from agriculture to other sectors, mainly services, has led to growth-enhancing structural changes in Africa

Despite benefiting from labor reallocation across sectors, productivity growth within Africa's services sectors remains lackluster

In summary, there has been a significant reallocation of workers from agriculture to other sectors, mainly services. This shift has led to growth-enhancing structural changes in Africa, as average productivity in services tends to be higher than that in agriculture—yet, productivity growth within services remains lackluster. The implication is that if productivity growth within services is not stimulated, structural change and overall labor productivity growth will stall in Africa. Manufacturing, traditionally associated with structural change, has played a limited role in Africa's structural transformation since 1990. Formal manufacturing, despite exhibiting superior productivity to nontradable services, is absorbing fewer and fewer workers as manufacturing evolves. The most productive manufacturing firms in Africa are increasingly using more capital than labor, in line with the labor-saving nature of emerging technologies.[32]

These patterns extend beyond value-added and employment data; they are also reflected in trade data. Input-output analysis suggests that domestic value added embodied in exports (as a percentage of GDP) and jobs embodied in exports (as a percentage of total employment) are increasing in services but decreasing in manufacturing. This evidence from Africa, along with established evidence from India,[33] suggests a need to rethink the role of manufacturing and services in Africa's economic development (section 2.4).

Main drivers of Africa's structural transformation

The main "pull" factors for Africa include a competitive exchange rate system, well-defined and functioning institutions, and gross fixed capital formation; stringent labor market regulations act as "push" factors

Recent evidence[34] based on analysis from 1990 to 2019 emphasizes the centrality of structural transformation—labor reallocation and within-sector productivity growth—in fueling Africa's economic growth, and having the largest impact on Africa's growth in the 1990s, a decade of subdued growth. The evidence also shows that it has greatly contributed to a reduction in extreme poverty and inequality in the continent.

The discussion in the previous section suggests that accelerated structural transformation could serve as a critical buffer, aiding countries to attain socioeconomic development much faster. This calls for an understanding of its main drivers to ensure the ideal policy initiatives that unlock the process. To uncover these drivers, the analysis now applies an exploratory regression approach on an unbalanced panel comprising 48 African countries in 2000–19 (table 2.2).

Column 1 shows the result when we regress the structural transformation variable on total natural resource rent (in percent of GDP). The coefficient of the variable turns out negative and statistically insignificant, indicating that natural resource dependence does not significantly drag structural transformation. Column 2 shows the result when an index of exchange rate undervaluation is included in the analysis.[35] The index follows Rodrik (2008), which measures price level as adjusted for the Balassa-Samuelson effect.[36] The variable enters the regression with a positive sign and is statistically significant at 1 percent. The finding aligns with McMillan et al. (2014), and implies that currency undervaluation (overvaluation) enhances (stymies) structural transformation.

Column 3 introduces an index of labor market regulation drawn from the Fraser Institute database

TABLE 2.2 **Determinants of structural transformation in Africa, 2000–19**

Dependent variable: Structural change term	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**
Total natural resources	–0.0056 (0.005)	–0.0038 (0.007)	–0.0144* (0.009)	–0.0128 (0.009)	–0.0130 (0.009)	–0.0141 (0.011)	–0.0141 (0.010)
Undervaluation index		0.5998*** (0.218)	0.7224*** (0.220)	0.7717*** (0.209)	0.7933*** (0.216)	0.8749*** (0.272)	0.8831*** (0.264)
Employment rigidity index			–0.0536** (0.023)	–0.0604** (0.025)	–0.0632** (0.026)	–0.0646** (0.027)	–0.0680** (0.031)
Governance quality				0.0271* (0.016)	0.0245 (0.016)	0.0254 (0.017)	0.0253 (0.017)
Gross fixed capital					0.1915** (0.093)	0.1966** (0.091)	0.1878* (0.095)
Human capital						0.2102 (0.442)	0.2988 (0.457)
ICT infrastructure							–0.0103 (0.018)
Constant	–1.5924*** (0.573)	–1.5809*** (0.577)	–1.1116** (0.528)	–2.0009** (0.968)	–2.5062** (1.065)	–2.7690*** (0.897)	–2.7955*** (0.877)
Observations	909	909	854	842	842	756	756
R–squared	0.427	0.430	0.436	0.441	0.441	0.444	0.444
Number of groups	48	48	46	46	46	41	41

Note: Standard errors in parentheses. (***), (**), and (*) respectively denote coefficients at 1 percent, 5 percent, and 10 percent significance levels. Each column contains unreported year dummies and regional dummies. The choice of the explanatory variables included in the regression is informed by the existing literature (see McMillan et al., 2014; van Neuss, 2018; Martins, 2019; Dappe and Lebrand, 2024), while the sample size and period of analysis are determined by data availability. Regression was done using the least squares dummy variable (LSDV) model with Driscoll-Kraay standard errors. See text for discussion of the columns.
Source: Staff calculations.

to capture its effect on structural change, which studies have shown to matter for structural transformation.[37] Higher values of the index imply stringent labor market regulation. Although such stringency benefits workers by guaranteeing job security, this often comes at the cost of limited labor mobility and hence job reallocation. It also binds employers to retain workers, regardless of their efficiency and contribution to labor productivity, which is costly to firms and a major drag on their productivity. With persistent cross-sector productivity gaps in multiple African countries, this suggests that this stringency is likely to impede structural transformation. The result confirms this expectation, as the estimated coefficient turns out negative and statistically significant at the 5 percent level.

Column 4 shows the result when accounting for institutional quality. The conventional view is that well-defined and functioning institutions can positively drive structural transformation by reducing transaction costs and information asymmetry.[38] The result confirms this view, as the estimated coefficient turns out positive and statistically significant. More generally, the result aligns with Mensah et al. (2016), which found that institutions, governance, and fiscal reforms are essential drivers of structural transformation in Africa. Column 5 introduces an index of gross fixed capital formation. The variable enters the regression with a positive sign and is statistically significant at 5 percent, indicating that gross fixed capital formation drives structural transformation.

CHARTING A NEW DEVELOPMENT STRATEGY FOR AFRICA

The development discourse on Africa has largely been shaped by external advice. For a long time, the Washington Consensus dominated the policy space on Africa's development. More recent evidence from some academics generally debunks this narrative, however, proposing a rethink of Africa's development model that focuses on the role of emerging new sources of growth. For example, evidence by Rodrik (2011) promoted manufacturing as the driver of economic growth, arguing that developing countries ignore the imperative of building a robust manufacturing sector at their own peril. More recently he has argued that, because the bulk of future jobs will more likely come from services, policymakers should focus also on industrial policy for that sector.[39] Stiglitz (2021) and Rodrik and Stiglitz (2024) further acknowledge the need to incorporate climate change and the changing geopolitical landscape into development strategies.

A substantial reversal of globalization has complicated the adoption of export-oriented strategies for low-income countries

The message on the importance of building a robust manufacturing sector has made its way into the development strategies of most African governments, most notably Ethiopia. And industrialization is one of the African Union's Agenda 2063 key pillars of development.[40] The confluence of empirical evidence on the changing nature of manufacturing and on the lack of job creation in formal manufacturing across Africa has given pause to a single-minded focus on development through industrialization.

The new model of development emphasizes the centrality of raising productivity growth while recognizing the diversity of countries across the continent. This perspective underscores the importance of tailoring development strategies to the realities of local and unique circumstances. While much attention is given to fostering quality employment through government intervention, it is crucial to recognize that many Africans are predominantly generating their livelihoods in the informal economy, mainly in services and without policy or fiscal support from the government.

This section, after reviewing the evidence on the significance of manufacturing in driving employment opportunities and productivity enhancement, considers a development strategy based on services, drawing on recent empirical work that has tried to measure services productivity. Subsequently, it delves into transformative processes that raise productivity, often overlooked within the discourse on development strategies. The upshot is that a development strategy that hinges on one sector alone is likely to disappoint, unlike one that focuses on more diversified sources of growth.

The role of manufacturing in Africa's development

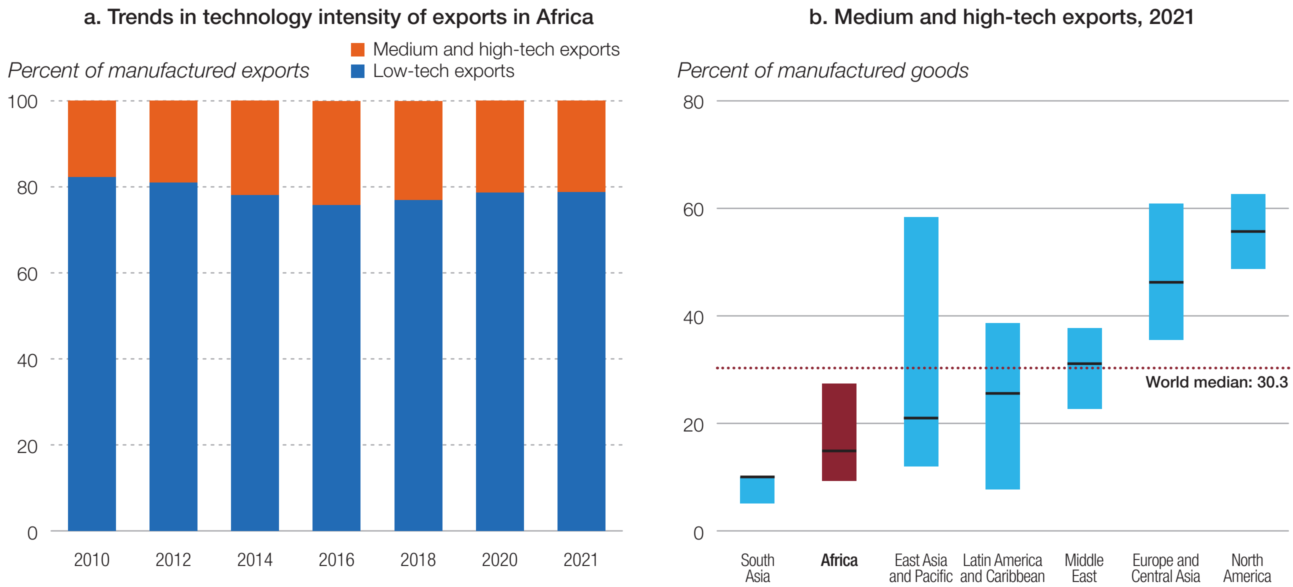
The traditional development path taken in the 19th and 20th centuries was for a shift of labor into manufacturing. For small and midsize economies, manufacturing was export focused, albeit with backward linkages and often including large features and components of import-substitution industrialization.[41] The world since then has of course changed enormously and in the 21st century this path is going to be harder to follow. Rodrik (2022) explains that the share of labor in manufacturing is peaking across the world—not just in Africa—at ever lower levels due to technological changes shifting the relationships between capital and labor in manufacturing, making capital a more effective substitute for low-skill labor and thus undermining the previous comparative advantage of labor-abundant countries in this sector.

In addition, a substantial reversal of globalization has complicated the adoption of export-oriented strategies for low-income countries. Global value chains are being rebuilt based on geopolitics.[42] The "friend-shoring" of supply chains, popularized since the COVID-19 pandemic and the race to vaccines, illustrates perfectly the strong interlinkages between global supply chains and geopolitics. It consists in shifting trade and supply chain networks toward multiple trusted countries that share similar political values, economic policies, and security interests, so that "friendly" countries can continue to securely extend market access, with lower risks to their economy, as well as to their trusted trade partners.

Structural transformation generally entails a gradual transition from resource-based and low-tech, to medium- and high-tech, activities. The latter are also the high-value-addition manufacturing processes with higher technological intensity and labor productivity.

An analysis of trends in export technology intensity shows that in Africa, trade in manufacturing was mainly driven by low-tech industries after 2010, hovering at about 75–83 percent of manufactured exports (figure 2.15a). Exports of

FIGURE 2.15 Manufacturing trade by technology intensity in Africa, 2010–21



Note: Interquartile range shown and median values reported in figure 2.15b.
Source: Staff calculations based on World Bank's World Development Indicators database.

medium- and high-tech activities, such as aerospace, computers, pharmaceuticals, scientific instruments, and electrical machinery, are emerging but have not gained sufficient traction in Africa, although the share increased from 17.7 percent in 2010 to 21.2 percent in 2021.

This pickup suggests that the structure of Africa's exports has yet to fully exploit the ongoing "fourth industrial revolution" and the technological advances it brings such as big data, the internet of things, machine learning, artificial intelligence, robotics, 3D printing, blockchains, biotechnology, nanotechnology, renewable energy technologies, and satellite and drone technologies. Africa's median share of medium- and high-tech exports (as a share of manufactured exports) is indeed among the lowest in the world, at 14.9 percent in 2021, well below the global median (30.3 percent) and other regions such as Latin America and the Caribbean (25.6 percent) and Europe and Central Asia (46.2 percent) (figure 2.15b).

McMillan and Zeufack (2021) argue that manufacturing remains important for African development. While acknowledging that this sector may create fewer jobs than in the past given rising capital intensity, in a review of 18 African countries they find that manufacturing employment has grown rapidly over the past 20 years, paired by steep increases in the number of small manufacturing firms set against limited employment gains in large firms but robust labor productivity growth in these large firms. Still, evidence from Ethiopia and Tanzania indicates that despite contributions to value-added and export growth, employment growth in formal manufacturing was subdued; instead, manufacturing grew rapidly in the informal sector, where productivity growth was minimal.[43] Informal manufacturing firms also tend to be small, have few workers, and are less capital intensive.

Special agro-industrial processing zones as a pathway toward an agro-led structural transformation in Africa

The expected outcome of a structural transformation process, already visible on the horizon in developed countries, is a state where agriculture as an economic activity has no distinguishable characteristics from other sectors, at least in labor and capital productivity, or the location of poverty.[44] At that stage, the gap in labor productivity between agricultural and non-agricultural workers would approach zero. This suggests that an agro-led structural transformation should be an integral part of Africa's development strategy, in particular given the enormous untapped agricultural potential and rising demand for food driven by the growing middle class in the continent.

Africa has more than 65 percent of the global available land for cultivation, providing a strong basis for countries to develop an agriculture-based industrial policy and prioritize agro-processing as one of the key foundations for industrialization. The current state of the sector, however—characterized by low uptake of modern inputs, weak mechanization, lack of access to credit and finance, insufficient farmer skills, inadequate land-tenure systems and property rights, and absence of strong backward and forward linkages with other sectors—has held the sector back from contributing to Africa's growth. A new focus is needed.

One promising way to improve agricultural productivity is by setting up Special Agro-Industrial Processing Zones

One promising way to improve agricultural productivity is by setting up Special Agro-Industrial Processing Zones (SAPZs). SAPZs aim to stimulate structural transformation in agriculture by connecting rural and urban development through the zones' ecosystem. These zones integrate smallholder farmers into value chains through logistics and infrastructure, linking them to agro-industrial processors and consumer markets. The resultant SAPZ-type growth poles have the potential to develop competitive export-oriented value-addition agribusinesses that have beneficial linkages to local producers and other sectors of the economy, and connections to regional and global supply chains.[45] To date, Africa has more than 60 agro-industrial zones, clusters, and parks, scattered across all five regions and covering all types of economic activities along agricultural value chains.

These special zones have proven successful models for economic transformation. For instance, the ARISE IIP business is operating the successful $1 billion forestry-based Nkok special economic zone in Gabon, with more than 100 international investors having placed more than $1.7 billion. Ethiopia has 24 industrial parks, some of which are supported by the African Development Bank (box 2.2). Evidence from Ethiopia and Morocco also shows that intermediary cities and agro-growth poles acting as processing and marketing hubs for agro-industrialization activities can lead to economic and social changes that make SAPZs attractive to local rural youth who otherwise might have moved to urban centers for work.[46]

Can services drive productivity growth in Africa?

The persistence of growth and structural transformation without industrialization,[47] along with new evidence on productivity in services,[48] has raised the question of whether services can also plausibly drive a development and growth strategy within Africa. The centrality of manufacturing has long been accepted by policymakers in both high-income and low- and middle-income countries, despite very limited evidence in the academic literature for the proposition that manufacturing is paramount for long-run growth. For instance, the United States economy has maintained an approximately constant long-run growth rate for the past 100 years even as the country has undergone massive deindustrialization. The same is true of many other high-income countries, where the shift from industry to services has not necessarily slowed economic growth.

Even in poorer countries, there is little evidence that productivity growth in manufacturing has been more rapid than that in agriculture or services.[49] In today's high-income countries, manufacturing has been associated with higher-quality jobs, perhaps because of the presence of organized labor and more easily enforced labor standards, but it is not clear that the quality of jobs is intrinsically related to the sector of production.

Data already suggest that services are becoming increasingly important in Africa's international trade. The median value of Africa's services trade reached 23.6 percent of its total trade in 2022, above the world average of 22.9 percent and only outpaced by the Middle East (25 percent) (figure 2.16a). Africa increased the value of its services trade more than fourfold between 2000 and 2022, from $66.4 billion to $269.4 billion (figure 2.16b). The sharp drop in services trade from $309.4 billion in 2019 to $224.3 billion in 2020 was primarily due to the stringent measures imposed by countries globally to contain the spread of the COVID-19 pandemic, which affected all sectors of the economy, but especially transport and travel. It also reflected the disruptions in supply chains, in which logistics are important.

BOX 2.2 The African Development Bank's leading role in establishing SAPZs across the continent

The Special Agro-Industrial Processing Zones (SAPZ) program is a flagship initiative of the African Development Bank (AfDB). The zones aim to bring together the production, processing, storage, transport, and marketing of commodities, including cotton and maize. This will increase productivity and competitiveness and reduce logistics costs. The AfDB envisages the SAPZs as new economic zones in rural areas to be fully supported by infrastructure (power, water, roads, digital infrastructure, and logistics) that will allow food and agribusiness companies to locate within such zones. This will put them close to farmers in production catchment areas, provide market offtakes for farmers, support processing and value addition, reduce food losses, and allow the emergence of highly competitive food and agricultural value chains.

The AfDB's flagship initiative has four broad components: (i) support for the development of enabling climate-adapted infrastructure for agro-industrial hubs; (ii) improved agricultural productivity and enterprise development to enhance value chains and job creation in the SAPZ catchment areas; (iii) support for the development of national agro-industrial zone policy and institutional development; and (iv) program coordination and management.

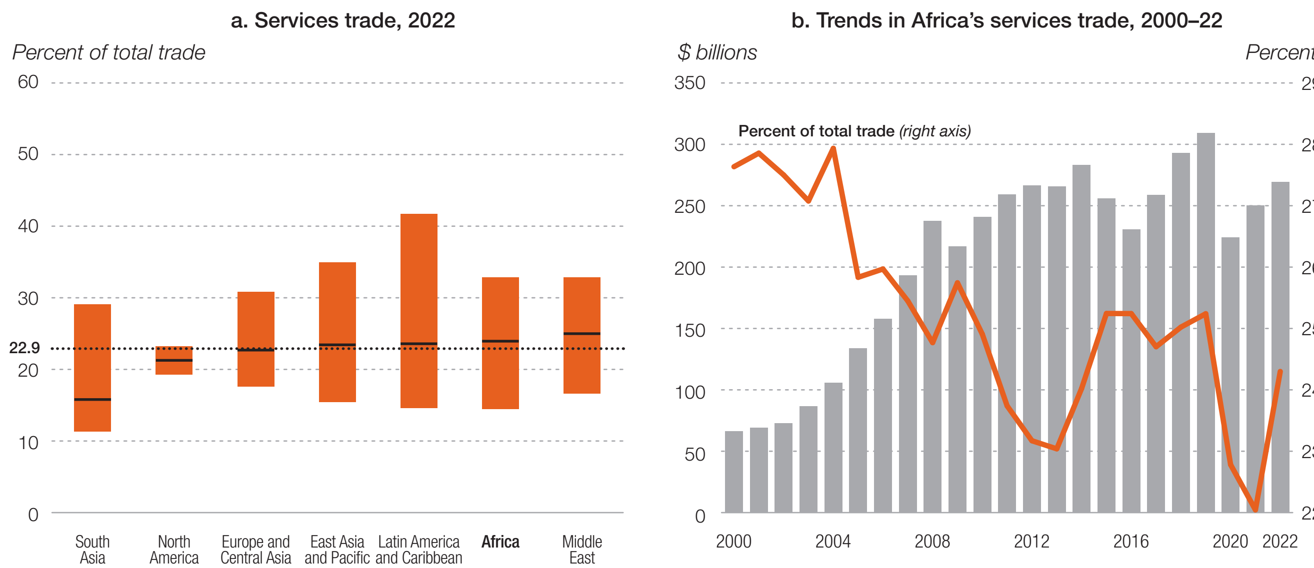
The AfDB is developing SAPZs in 18 African countries. Among the projects under implementation, there is one each in Côte d'Ivoire, Guinea, Mali, Madagascar, Nigeria, Senegal, and Togo, and four in Ethiopia. The SAPZ program in Nigeria is the largest, both in scale ($520 million, of which $210 million is provided by the AfDB) and scope. Phase 1 is being implemented over five years and began in 2022 in seven states: Cross River (cocoa, rice, and cassava); Imo (beef and dairy livestock); Kaduna (tomato, maize, and ginger); Kano (rice, tomato, groundnuts, and sesame oil); Kwara (livestock); Ogun (cassava, rice, poultry, and fisheries); and Oyo (cassava, soybean, and rice). It is also being rolled out in the country's Abuja Federal Capital Territory (beef and dairy livestock). The program will later be rolled out in more states. States participating in the first phase were chosen based on their readiness and to achieve a balance across Nigeria's six geopolitical zones.

In 2023, the AfDB, Afreximbank, Arise Integrated Industrial Platforms, the Islamic Development Bank Group, and the United Nations Industrial Development Organization (UNIDO) launched at the 2023 Africa Investment Forum (AIF) Market Days a new private sector–focused Alliance for SAPZs to bridge the critical financing gap in agriculture. The Alliance, comprising development financial institutions, the private sector, and development-oriented technical partners, will also help streamline the development and delivery of SAPZ projects. The AfDB committed $1.1 billion out of the $3 billion of new investment announced to transform Africa's underdeveloped rural areas into "agro-industrial corridors of prosperity." Meeting this financing goal is expected to deliver an additional 15 to 20 SAPZ projects across the continent and improve administrative, policy, and investment incentives.

Domestically, financial services grew strongly, underpinned by digital-led payment methods during the pandemic, as nonphysical contact measures were tightly enforced. A survey of 78 banks active in Africa showed both the resilience and enthusiastic engagement of Africa's financial sector to embrace digitalization during COVID-19.[50] While the share of services in Africa's total trade was declining before the pandemic, it has since gained momentum as economies recover, accounting for 24.3 percent of total trade in 2022, 2.2 percentage points higher than in 2021.

The possibility of a services-led growth model seems important to examine, therefore, given what appears to be a *de facto* process of services-sector expansion in low- and middle-income countries. Abstracting from the difficulties associated with measuring productivity in

FIGURE 2.16 Services trade in Africa and other regions of the world, 2000–22



Source: Staff calculations based on World Bank's World Development Indicators database.

services, several stylized facts about services in relation to manufacturing can be highlighted.[51]

First, firms in the services sector are smaller on average than manufacturing firms, and this gap is largest in rich countries.[52] Second, size matters less for productivity; in high-income countries, small services-sector firms are just as productive as their large counterparts within the sector. Third, physical capital is less important for services output than for manufacturing output. With the advent of digitalization, the barriers to productivity posed by lack of physical capital have broken down. And fourth, productivity growth within services-sector firms is similar to that in manufacturing. These features of the services sector appear to be good news for African countries where labor is abundant, capital is expensive, and skills levels are low.

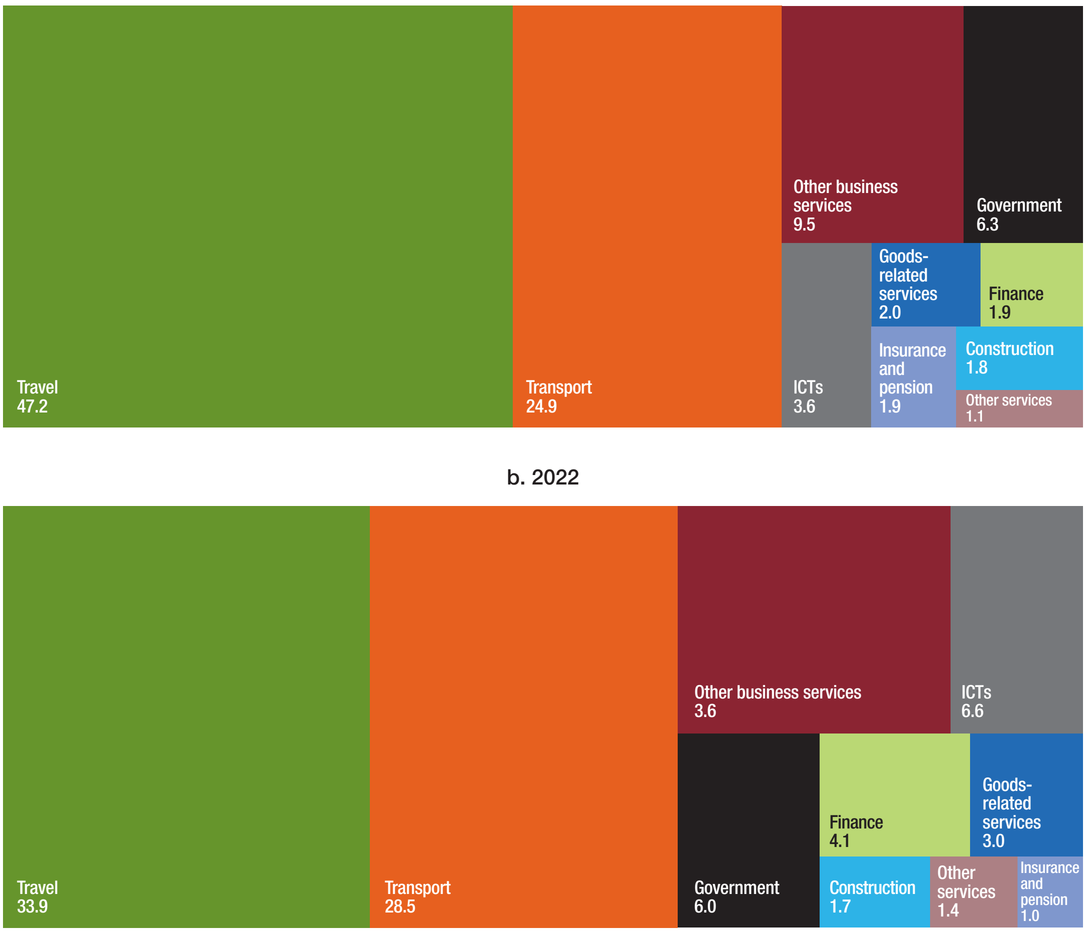
Africa's services sector is highly diverse, however, and can be clustered into three main categories:[53] traditional, high knowledge-intensive, and nonmarket services. Traditional services include transport, travel, and maintenance and repair services. High knowledge-intensive services are defined as activities and operations heavily reliant on professional and high-skill knowledge. They include, for instance, goods-related services such as manufacturing services (creating what is known as "servicification of industrialization"); construction; insurance and pension services; banking and financial services; ICT services; and consulting and other business services. Government goods and services are nonmarket services, and include public administration services, community services, and health and education services.

Africa's services exports are concentrated in traditional services sectors, mainly travel and transport, which are intensive in the use of low-skilled labor (figure 2.17). In 2005, they accounted for 73.1 percent of services exports, but their share dropped to 63.8 percent in 2022 as high knowledge-intensive services, in particular insurance, pension, finance, and ICT services, gained further traction, increasing from 20.7 percent in 2005 to 30.1 percent in 2022.

The predominance of traditional services in Africa's services trade may be explained partly by the high fragmentation of trade in professional, education, and health services stemming from restrictive policies that govern participation in these sectors, such as nationality requirements, regulatory heterogeneity for licensing, and educational qualifications—as well as the high cost of travel and visas. Medical tourism, though, is gaining traction in some African countries such as Tunisia and South Africa, with these countries earning substantial foreign exchange.

FIGURE 2.17 Sectoral distribution of services exports in Africa, 2005 and 2022

a. 2005



Note: Services are clustered into the followed subsectors: goods-related services, transport, travel, construction, insurance and pensions, finance, ICT, other business services (such as research and development or professional and management consulting services), government services, and other services.
Source: Staff calculations based on UNCTAD database.

Africa's services exports are concentrated in traditional services sectors, mainly travel and transport, which are intensive in the use of low-skilled labor

But a key question remains: Can the services sector, and in particular retail trade, also be a source of within-sector productivity growth, perhaps offering a viable development strategy for today's low-income countries? In particular, can services-led growth be generated beyond the high-skill tradable services in which African countries have little comparative advantage at present? One suggestive experience is that of India. In a recent study on services-led growth there,[54] the authors examined India's extraordinary growth performance of the past three decades. It is widely understood that India's growth has come from services rather than manufacturing, but most narratives have tended to assume that the key subsectors in which India has prospered have been high-skill tradable services, including digital-based exports. For instance, India has had well-documented successes in attracting call centers, data-entry services, software development, and other sectors that rely on a well-educated workforce and good digital connectivity. Somewhat surprisingly, however, the authors find that an even stronger source of growth has come from consumer-facing services in India, such as wholesale and retail trade, transport, and other nontradables. As in most African countries, consumer services account for the majority of services employment in India, and the study finds that productivity growth within this sector has been strong and robust.

An important question is the extent to which employment growth in consumer services is a *source* of growth—or simply a *consequence* of growth. Because the share of income spent on consumer services rises with income, increasing employment in consumer services could simply be a consequence of growth rather than a driver of sector-specific productivity gains. To untangle this, Fan et al. (2023) divide services into nontradable or consumer services (such as retail trade in local markets) and tradable or producer services (for instance, ICT). Using a new methodology that allows the authors to infer productivity growth from micro data on employment, wages, and human capital, they document that productivity growth in consumer services was an important driver of productivity growth and accounted for roughly one-third of aggregate welfare gains in India between 1987 and 2011. They also find that these productivity gains were unequal, and that welfare gains were generally concentrated among the consumers of these services, who tended to be richer consumers and those living in cities.

In Côte d'Ivoire, high-productivity firms in services hire more workers, especially low-skilled workers, than low-productivity firms in services.

Yet the India study leaves some important questions unanswered. First, what exactly was the source of the within-sector productivity growth in consumer services? One clue is that it occurred mainly in urban areas. One can imagine supermarkets and fast-food restaurants making services more productive through consolidation and economies of scale, relative to the highly fragmented industry structures that currently prevail. Is this the source of productivity growth? If not, what are the other sources of productivity growth within services? Understanding the sources of productivity growth in consumer services is of first-order importance for policymakers.

Second, how do the improvements in service productivity relate to public investments, policies, and other elements of structural transformation? This question has important implications for the potential replicability of India's experience in African countries. Does services-sector productivity growth require some set of accompanying changes in transport infrastructure, housing, energy use, diet patterns, or other dimensions of urbanization? There are reasons to think that India's experience is not unique and could apply to African settings. Although the case is not exactly parallel, recent evidence from Tanzania (box 2.3) during the COVID-19 pandemic is consistent with India's experience.

Another study, by Foltz and Jing (2023), uses Côte d'Ivoire's firm-level data for services and manufacturing to show that total factor productivity is 7 percent higher on average in services than in manufacturing. It also shows that high-productivity firms in services hire more workers, especially low-skilled workers, than low-productivity firms in services. They conclude that there is evidence consistent with the idea that the services sector is leading structural transformation and growth in Côte d'Ivoire.

While this evidence is encouraging, measuring total factor productivity is fraught with problems and so it remains hard to know how much these results can be applied elsewhere. Regardless, it is worth exploring whether it is possible to identify a causal pathway from productivity growth in consumer services (low-skilled, labor-intensive) to economywide growth in African settings. If the results of the India study hold up in the African context, Africa's development strategy and structural transformation should not be solely based on industrialization but should be extended to other productivity-enhancing sectors such as services.

There are other questions, too, about a development strategy led by productivity growth in nontradable services. One is how this approach would allow economies to earn the foreign exchange needed to service debt and to pay for imported goods. Productivity growth in nontradable services may suffice for creating jobs and for lifting aggregate output per worker, but it is not going to generate the hard-currency earnings essential for African countries.

But perhaps here the point is that the sectors bringing in foreign exchange do not need to be identical to those that generate employment and productivity growth. Primary product exports from mining and agriculture may remain key export sectors for African economies, even if they are not the sectors driving growth.

Another concern with services-led strategies may be their distributional consequences. India has only recently relaxed longstanding restrictions

BOX 2.3 Structural transformation in Tanzania: a tale of services-led growth

Tanzania's recent experience with structural transformation was broadly like those of other lower-middle-income countries, with the increase in the employment share of services roughly matching declines in agriculture's share. From 2006 to 2014 (the first period), business and trade services absorbed most of the labor shed by agriculture (6 percentage points of employment share out of 7). From 2014 to 2021 (the second period), labor flowed from services back to agriculture (2 percentage points), reflecting a contraction, especially in demand for services provided by hotels and restaurants during the COVID-19 pandemic. The employment share of manufacturing barely changed.

While productivity growth in services was negative over the first period, it turned positive in the second, dwarfing that in manufacturing. Infrastructure investments, which increased rural electrification eightfold and overall internet access sevenfold in less than a decade, were reportedly instrumental for this productivity growth. Tanzania's public gross fixed capital formation increased from 33 percent of GDP to 43 percent in the second period, and the subsequent improvements in transport and ICT helped boost market access and reduce operating costs.

However, a second reason for the strong performance in the services sector may be directly related to COVID-19. Also, during the second period, the share of employment in agriculture increased by 2 percentage points while the share of employment in nontradable services fell. Anecdotal evidence suggests that in Tanzania (as in many richer countries), migration out of cities and back to rural areas was one way of coping with COVID-19. The workers most likely to leave the city were probably informal workers in the services sector. While this was happening, and somewhat unrelated to COVID-19, the second period also saw a proliferation of small informal firms employing less than 10 workers, mostly in trade services. In 2013, about 145,000 firms were formally registered. By 2021, this number had increased to almost 400,000. Concurrently, the share of business and trade services in formal employment climbed from 10.5 percent to 26.1 percent and that of transport and communications from 18.5 percent to 27.6 percent. In short, services played a key role in Tanzania's recent economic growth.

Source: World Bank 2023.

on foreign direct investment in the retail sector, and many other sectors of consumer services retain some policy limits designed to protect small-scale "mom-and-pop" operations from competition with multinational firms.

This reflects a concern over the potential distributional consequences of opening the traditional services subsectors to competition. As seen in Fan et al. (2023), competition and productivity growth within services will normally tend to drive profit margins down and low-productivity firms out of business. While these outcomes may be desirable from a long-term perspective, the welfare impacts may be ambiguous or even negative.

This topic deserves further exploration. A discussion of services-led growth in Africa should certainly not neglect tradable services such as tourism, business and finance, and ICT. There are a wide range of skills required across these subsectors as well as public initiatives to train young Africans in the required skills. For example, tourism has emerged as a pivotal sector contributing to Rwanda's strong economic performance. The government, with the Mastercard Foundation, launched youth training in tourism, and it appears to be paying off (box 2.4).

Digitalization holds promise for supporting Africa's structural transformation, and although ICT does not employ a very large share of the labor force, digital services are critical to running all sorts of businesses and organizations, regardless of sector. Some countries, such as Kenya, have

BOX 2.4 Tourism and hospitality training in Rwanda

The tourism and hospitality sector has been growing in Rwanda and has emerged as a key contributor to the country's economic growth, employment generation, and development trajectory. Recognized for its stunning landscapes, diverse wildlife, and vibrant culture, Rwanda has increasingly positioned itself as a prime tourist destination in East Africa. According to the Rwanda Development Board (2021), the sector employed more than 164,000 people in 2020 with different education and skill levels.

With this growth, there has been a concerted effort to bolster the labor force within the sector through training initiatives and educational programs. Universities and vocational institutions have been extremely important in equipping individuals with the necessary skills and knowledge to thrive in the industry. These initiatives aim not only to meet the growing demand for skilled professionals in tourism and hospitality, but also to empower local communities by providing them with opportunities for meaningful employment and economic development.

One important initiative is the Hanga Ahazaza, also known as *Create the Future,* a Mastercard Foundation–supported initiative under the Young Africa Works project, which aims to reduce poverty. Hanga Ahazaza is a $50 million, five-year initiative for increasing job opportunities for young people through expanding tourism and hospitality, and for equipping 30,000 young people with skills in communication, customer service, digital literacy, and ICT. The initiative also supports small businesses in tourism and hospitality, business development skills, and access to financial services.

Hanga Ahazaza has partnered with 15 different institutions to ensure skills and knowledge transfer to youth. Cornell University's school of hotel management is among these 15, and provides online training programs.

Rwanda is also home to the University of Tourism, Technology and Business Studies, which has offered degree programs in hospitality and tourism since 2008, as well as short courses, including a nine-month program in food and beverage operations, and in front-office and housekeeping skills. Through the University's international job and internship exposure program, it helps its best students to go to some of the best hotels in Dubai or Qatar where they acquire the skills necessary to thrive in hospitality and tourism.

At least four other universities in Rwanda offer courses to prepare people to work in tourism and at least one—Mount Kenya University—a Bachelor of Science in tourism.

emerged as tech-hub leaders in Africa's ICT revolution (box 2.5), but the distance from the more advanced economies remains long, with Africa in the lowest bracket and far below the world average (figure 2.18).

Globally, the scope for services productivity growth seems enormous. Innovation and rising incomes are leading to consumers demanding far more services than ever. In the United States in 2022, services accounted for 66 percent of consumer spending, up from 42 percent in 1980 and 36 percent in 1960.[55] Moreover, technology has increased the range of services that can be traded, including ICT; business services including legal, design, and accounting; back-office work and finance; and operations through consumer support/call centers. Africa has scope to deal more in traditional services like tourism, international transport, distribution, logistics, and consulting. Historically nontraded services, such as education and health, can also be—and are increasingly being—exported, within Africa and to the rest of the world.

The role of non-sector-specific transformations

This chapter has thus far focused on structural transformation at the level of economic sectors.

BOX 2.5 **Kenya, the "Silicon Savannah" of Africa**

In the early 2000s, Nairobi emerged as Africa's technology epicenter, branded the "Silicon Savannah" after San Francisco's Silicon Valley. The defining feature of the Kenyan economy since 2000 has been the development of the information technology (IT) sector with the dual arrival of internet access and mobile telephones. In 2002, mobile phone penetration in Kenya stood at 9 percent. By 2018, it had reached 80 percent, against 89 percent in the United States. According to Wired magazine, Nairobi's tech sector was worth $1 billion; the city housed incubators like iHub and Nailab and at least 200 startups. Additionally, Nairobi has become a hub for Microsoft and IBM, which established research centers in Kenya and South Africa.

Mobile money transfers have facilitated innovation and growth in several related sectors, including remittances. For example, in 2017, Kenya received more than $2 billion in remittances, up 13 percent from 2016. And in 2018, M-PESA entered into an agreement with PayPal and Western Union, paving the way for further remittances through mobile banking. This reduced the cost of remittances to 1.7 percent per $200 transaction. Moreover, people receiving remittances on their mobile money account could buy government bonds through M-Akiba, helping investment.

Complementing the growth of mobile technology and platforms, Kenya also aimed to build one of the strongest ICT ecosystems in the region. In 2013, it launched its National Broadband Strategy to extend fiber optic cables across the country and install ICT centers at universities. By 2019, more than 250 government services were available digitally through the country's e-Citizen platform. The shift from cash to digital payments also led to an upsurge in tax and revenue collection. Following deployment of online tax systems, the Kenya Revenue Authority reported collecting Kshs 1.366 trillion ($13.2 billion) in the 2016/17 financial year —Kshs 115 billion ($1.1 billion) more than that collected in the year before online tax procedures were adopted.

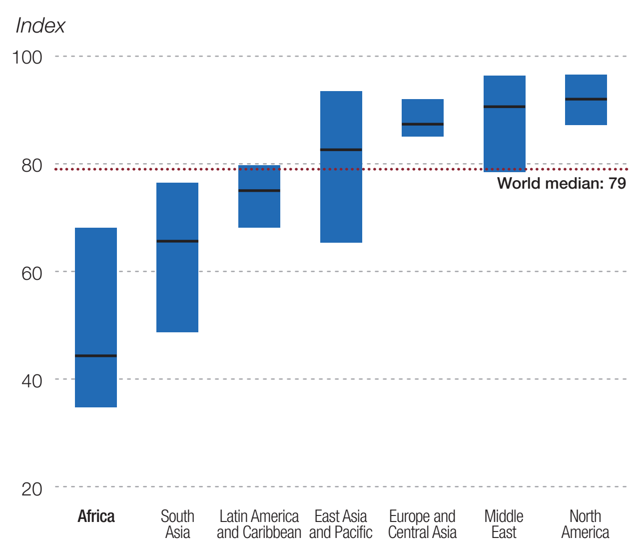
Source: Harvard Business School, Kenya and the Silicon Savannah, April 2023.

But recent thinking has emphasized that sectoral changes are only one part of the broader structural changes that accompany growth and development. Although policy conversations have focused on sectoral changes—especially industrialization—as the key drivers of structural transformation, they embed a strong assumption about the *direction* of causation.

At least to some degree, sectoral changes are themselves a response to other dimensions of transformation. For instance, people may move out of agriculture not in response to the availability of better jobs in industry or services, but because of the attractions of urban life relative to those in rural areas. In most cities in the developing world, a range of amenities are more readily available than in rural areas, such as access to (and quality of) healthcare and education, or the greater availability of water and electricity.[56]

Recent literature[57] thus considers structural transformation beyond sectoral changes. The spatial patterns of economies change during growth, both through urbanization and the growing spatial integration of economies. Localized autarkic modes of production (such as quasi-subsistence

FIGURE 2.18 **ICT Development Index by main region, 2021**



Note: The figure presents the interquartile range. Median values are shown. The ICT Development Index of the International Telecommunication Union (ITU) is harmonized between 0 and 100 and combines the following indicators: individuals using the internet (percent); households with internet access at home (percent); active mobile-broadband subscriptions per 100 inhabitants; 3G and 4G/LTE network coverage; mobile broadband internet traffic per subscription; fixed broadband internet traffic per subscription; mobile data and voice high-consumption basket price (percent of GNI per capita); fixed-broadband internet basket price (percent of GNI per capita); and individuals owning a mobile phone (percent).
Source: Staff calculations based on International Telecommunication Union (ITU) dataset.

agriculture) give way to more integrated domestic markets, allowing for economies of scale and specialization, as well as urbanization. On the production side, huge changes take place in the structure of production. Typically, the locus of production shifts from home to market.

This move is accompanied by changes in the scale of production (from micro to larger firms), in the complexity of management structures (from self-employment to multilevel hierarchies), and in the legal structure and visibility of firms (typically associated with moves from informality to formality). There may also be important changes in social norms, such as around the participation of women in labor markets, or around the cultural acceptability of economic profits.

Creating policy environments and infrastructure to support domestic market integration is not a substitute for international trade but it can be an important source of productivity growth for countries

If structural change encompasses these many other dimensions, and if these dimensions are in turn causally linked to sectoral change, economic growth, and development, the policy space for development is far broader than a focus on policies that promote industrialization or exports. As Gollin and Kaboski (2024) argue, the role of policy in driving economic growth must be understood far more broadly than choosing and supporting specific sectors of the economy. Although there may be a potential role for effective states in prioritizing certain sectors, there are many other margins on which policy can affect the economy's growth potential.

Some of these margins are not usually seen as obvious candidates for growth policy, and may be actively rejected by finance ministries that see fiscal costs rather than growth benefits. For instance, improvements in business-to-business infrastructure—some of them as simple as formalizing street addresses—can support the development of deeper input-output structures in an economy. Programs that support the provision of safe childcare may increase women's labor market participation, not only expanding the size of the workforce, but also driving up demand for market services that substitute for what is often women's work in the home. Reducing transport and search frictions in labor markets may allow for better matching between firms and workers, expanding productivity across sectors. In the same vein, reducing frictions in housing markets may allow people to achieve better matches between home and work locations, in ways that have beneficial effects on productivity and economic transformation.

Many of these policies are not explicitly linked to specific sectors. The argument here differs from an older conversation about whether governments should pursue "soft" or "hard" industrial policy, that is, promoting industrialization by providing infrastructure and investing in education (soft), rather than promoting specific industries (hard). The difference in the current discussion is that it does not identify industrialization as the target, or even as a useful metric, of success. The goal instead is to create a functioning economy with lower frictions and greater internal integration. Rather than choosing specific directions for sectoral change, the idea is to make it easier for land, labor, capital, and talent to move into productive uses, and to reduce misallocation of these resources.

Moreover, rather than focusing explicitly on the export of final goods, the new literature emphasizes the potential gains within domestic economies, including those from deepening the extent of market integration, such as the one brought about by the AfCFTA. Exporting low-skill manufactured goods may be a good source of hard currency earnings, but if all the intermediate inputs are imported, the value addition and technology transfer are limited; essentially, countries hosting this kind of activity are mostly exporting labor, almost as though they were sending international migrants out of the country. By contrast, policies that focus on reducing spatial and institutional frictions within the economy can have important benefits across sectors. By promoting the creation of value chains within the domestic economy, such policies can support market integration with concomitant gains through specialization and exchange. These value chains often include extensive services-based components, such as the linkage of retail supermarkets or retail food services (restaurants) to the production, packaging, storage, and transport of domestically produced agricultural goods.[58]

Creating policy environments and infrastructure to support domestic market integration is not a substitute for international trade but it can be an important source of productivity growth for countries. To the extent that they may have other sources of foreign exchange through mining or primary products exports, it may be possible to drive the productivity growth of the economy through nontradable sectors, so long as the external macro position can be sustained through other means. In short, policy has focused for a long time on the idea that low- and middle-income countries need to achieve productivity growth through the same sectors that generate export earnings; if those two objectives can instead be separated, there is scope for a broader set of development strategies.

FINANCE TO FAST-TRACK AFRICA'S STRUCTURAL TRANSFORMATION: HOW MUCH IS AT STAKE?

Financing needs and financing gap

AfDB estimates point to a financing gap of $402.2 billion annually by 2030 to fast-track Africa's structural transformation and catch up to high-performing developing countries from other regions

Better access to finance is one of the key "pull" factors of structural transformation in Africa—as highlighted in previous sections. This implies that African countries will urgently need to mobilize huge resources to fast-track structural transformation and sustain the momentum of development. The rest of this chapter uses a benchmark approach linked to SDGs to estimate the financing needs and resulting financing gap for Africa's structural transformation. The interconnectedness and synergy among SDGs mean that they all contribute directly or indirectly to that transformation in developing countries. Some SDGs are, however, more directly linked to achieving the transformation and require far more financial investment than others, in particular, Goals 4 (Quality education), 7 (Energy), 8 (Productivity), and 9 (Infrastructure).

The methodology in annex 2.2 quantifies the annual financing needs and financing gap to achieve high performance across these four sectors. For each sector, it is assumed that SDG performance is a function of a set of specific input variables such as education spending per student, electric power consumption per capita, gross domestic expenditure on research and development (GERD) per capita, road density, and the like. The median level of these inputs is computed for non-African developing countries that perform well today on the four SDGs, with performance measured by corresponding SDG index scores.

For each African country, annual financing needs and the associated financing gap are calculated for both the 2030 Agenda for Sustainable Development and the African Union's Agenda 2063 by assigning these median input levels and controlling for other factors such as projected demographics (population size and composition, and so on) and the level of GDP per capita. The approach is not intended to estimate the level of financing needs and financing gap to meet the SDG targets by 2030 or 2063, but rather to estimate how much African countries need to spend —and the financing gap to be filled—if they aim at reaching the same level of performance as other developing countries in sectors critical for structural transformation.

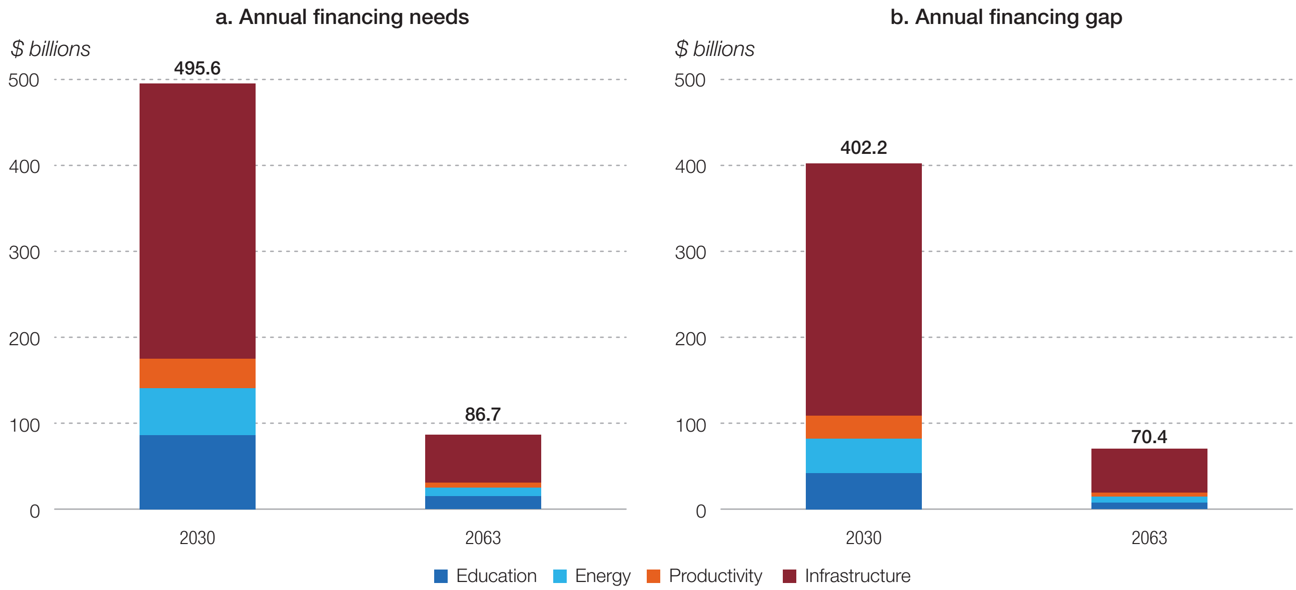
Africa needs to close an annual financing gap of $402.2 billion, or about 13.7 percent of Africa's projected 2024 GDP, until 2030 to accelerate its structural transformation process

Using this benchmarking methodology, the AfDB estimates that the continent would need $495.6 billion annually, or about 17 percent of Africa's projected 2024 GDP, until 2030 to accelerate its structural transformation process and put it at par with high-performing developing countries with currently comparable levels of development.[59]

When the deadline for Agenda 2063 is used as a reference, the annual financing needs fall to $86.7 billion, or about 3 percent of Africa's projected 2024 GDP. The bulk of these resources are in road infrastructure (64.8 percent of the total), highlighting the dearth of current investment in the sector, followed by education (17.4 percent), energy (11 percent), and productivity-enhancing research and development (6.8 percent) (figure 2.19a).

Given the current country performance levels on these critical sectors (annex figure 2.A.2) and their projected values, which are assumed to change in line with GDP per capita, the annual financing gap to fast-track structural transformation is estimated at $402.2 billion (or about 13.7 percent of Africa's 2024 GDP) under the SDG framework and $70.4 billion (2.4 percent of GDP)

FIGURE 2.19 Estimated annual financing needs and gap to fast-track structural transformation in Africa by 2030 and 2063



Source: Staff calculations based on the methodology described in annex 2.2 and database from Sachs et al. (2023), UNESCO, CIA, EIA, NASA, IMF, and World Bank.

under the Agenda 2063 deadline, with a longer time horizon and spread of investment across each SDG target. Road infrastructure remains the main contributor to Africa's financing gap (72.9 percent), followed by education (10.4 percent), energy (9.9 percent), and productivity (6.8 percent) (figure 2.19b).

These huge financing needs and associated financing gap reflect mainly Africa's underperformance in key SDGs directly linked to structural transformation (and other development indicators). On road infrastructure, the largest financing needs and financing gap reflect the continent's shortfall explained by decades of underfinancing to upgrade existing road infrastructure or open new roadways, to match the growing population and economic dynamism across the continent. Africa's median road density is about 12 km per 100 km^2, compared with 42.5 km in high-performing developing countries and 136 km in high-income countries. Weak legal, regulatory, and institutional frameworks also discourage private capital investment,[60] especially in road infrastructure, where the return on private investment may not be as obvious. In addition, the transport sector is characterized by mismanagement and poor planning, project preparation, and weak maintenance, all of which compound the problem and risk of private investment in Africa's road infrastructure. Even where public–private partnership models have been deployed, investments have tended to be smaller and adopted largely for urban roads, where tolls are generally easier to collect.

On education, fast-tracking structural transformation will require not only that African countries ensure full enrollment of their school-age population[61] and sustain these rates, but also greatly increase spending per student to upgrade education equipment and facilities (such as buildings, transport vehicles, and virtual learning equipment), to increase salaries of education professionals (in particular in public education systems), and to enhance access to technical and vocational education and training. Improving the quality of curricula will further help mitigate the widespread skills mismatch across the continent and will thus equip graduates with the required skills when they enter the labor market.[62]

On energy, accelerating structural transformation will demand not only that governments ensure universal access to electricity for Africans by 2030 or 2063—in line with the SDG 7 target, the AfDB's New Deal on Energy for Africa, or Agenda

2063—but also increase per capita consumption to align it with that in high-performing developing countries.

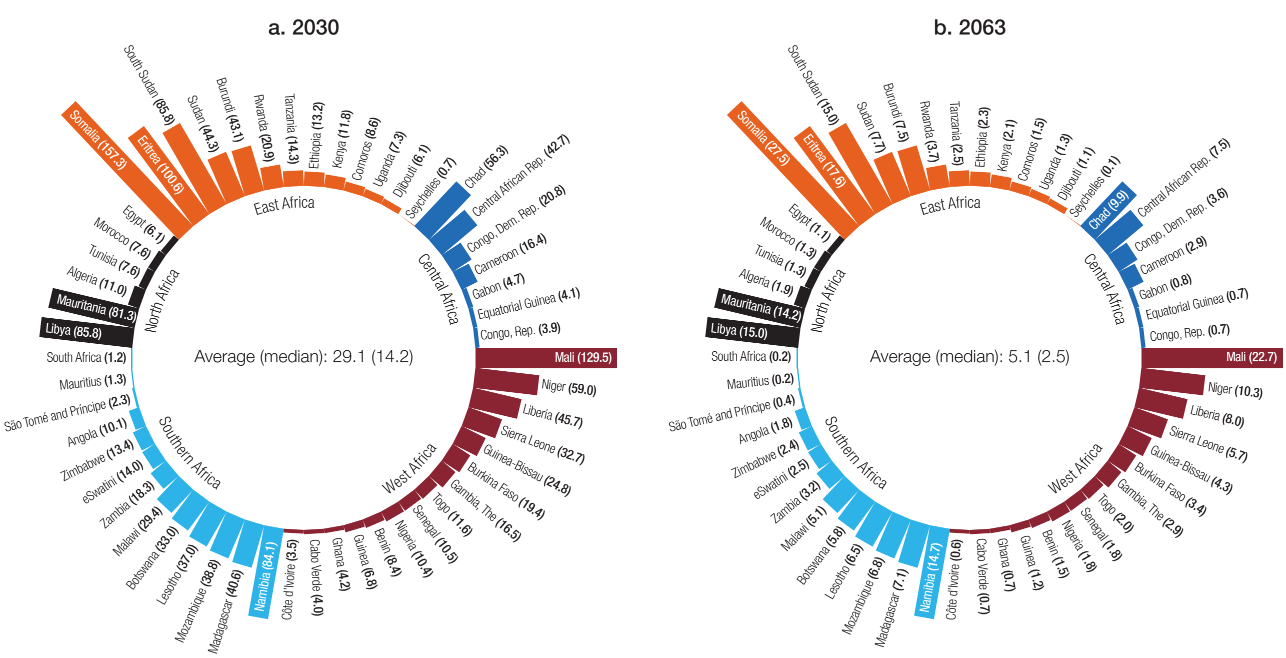
Finally, developing a robust national research and development agenda (or revitalizing it in countries where it already exists) and providing means of implementation (human, financial, and technical capital) will be vital to support technology upgrading and innovation to speed up structural transformation. In addition, investment in ICT, considered one of the means of implementation of all the SDGs,[63] will also be critical to accelerate progress on structural transformation. The AfDB estimates that $7 billion–$10 billion of investment in ICT is needed annually in Africa between 2023 and 2030 to ensure mobile coverage of at least 80 percent of the population.

The enormity of all these figures casts doubt on the ability of some African countries to mobilize the funding, particularly within the timeframe of the SDGs, whose deadline is just six years away. This is a legitimate reservation, especially given the continent's current funding and fiscal squeeze brought about by high debt service costs, the effects of the COVID-19 pandemic and climate change, and exacerbated by rising costs of fuel and food as stoked by Russia's invasion of Ukraine and likely to be amplified by disrupted trade routes due to spillover effects of the conflict in Gaza.

The annual financing gap for structural transformation using the SDGs' 2030 deadline is estimated to account on average for 29.1 percent of African countries' GDP (with a median value of 14.2 percent). It represents at least 10 percent of 2024's projected GDP in 36 African countries (two-thirds of countries), in nine of which it accounts for at least 50 percent of GDP (figure 2.20a). Closing the financing gap by 2030 is, therefore, realistically impossible for most African countries.

For those countries, spread across all five regions, a more reasonable target and combination of financing options would be to allow for a gradual but steady structural transformation over a longer period to ensure mobilization of domestic and external resources, without jeopardizing the conditions preserving debt sustainability. When the target is

FIGURE 2.20 Estimated annual financing gap (percent of GDP) by African countries for structural transformation by 2030 and 2063



Note: Annual financing gap is expressed in terms of 2024's projected GDP for each country.

Source: Staff calculations based on methodology described in annex 2.2 and database from African Development Bank statistics, Sachs et al. (2023), UNESCO, CIA, NASA, IMF, and World Bank.

extended to the Agenda 2063 deadline, the annual financing gap declines to an average (median) value of 5.1 percent (2.5 percent) and in 10 and 35 African countries, and it could stay below 1 percent and 5 percent of GDP, respectively, exceeding 10 percent in only 8 countries (figure 2.20b).

The cross-country heterogeneities in the size of financing needs and gap reflect mainly differences in demographics (current and projected population size and composition, land size, and the like) and socioeconomic characteristics (current and projected GDP per capita, and spending on education, infrastructure, and so on). Mobilizing financing resources is also affected by domestic and external disruptions, including pockets of political instability, weak export demand, and tighter global financial conditions.

Government tax revenues have not increased much in most African countries to reach the 15 percent of GDP that developing countries need to adequately finance progress toward the Sustainable Development Goals

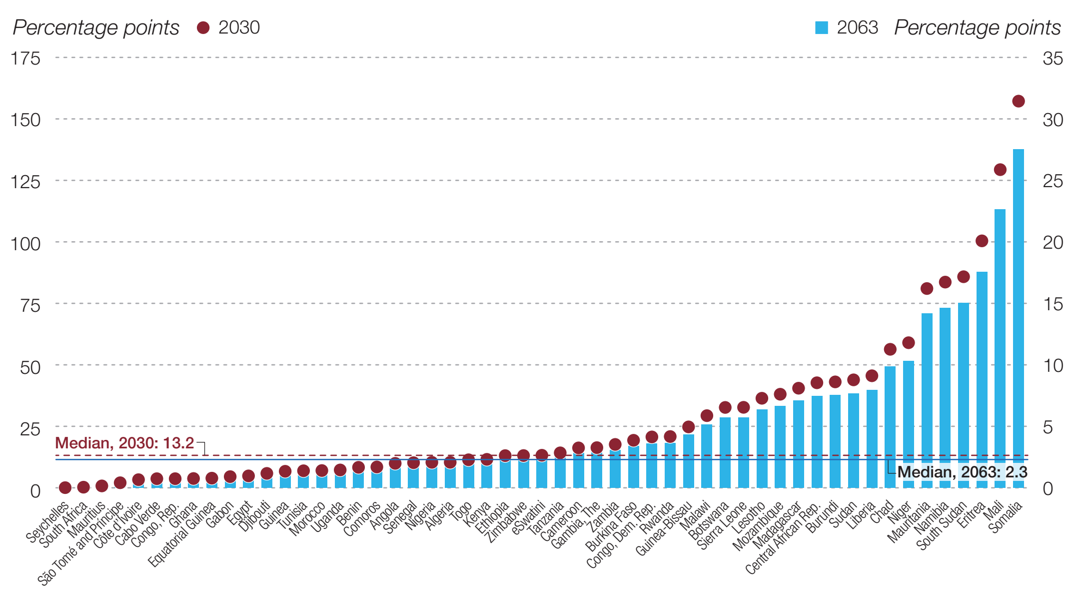
Domestic resource mobilization

Although some African countries may be able to close the estimated financing gaps through improved mobilization of government revenues, many of them cannot

Needless to say, African countries bear the primary responsibility for financing their structural transformation. Closing the estimated financing gap will thus require them, among other things, to boost government tax revenues, enhance public spending efficiency, and show strong political will. Government tax revenues have not increased much in most African countries to reach the 15 percent of GDP that developing countries need to adequately finance progress toward the SDGs (chapter 1). Additional efforts will be required to improve domestic resource mobilization.

Figure 2.21 displays the required increase in countries' current tax-to-GDP ratios to close their financing gap by 2030 or 2063. African countries will need to increase this ratio by a median of about 13.2 percentage points—bringing the current median ratio to 27.2 percent of GDP—to be able to close their financing gap by 2030, assuming that all the mobilized additional tax revenues are efficiently deployed and allocated to that objective. A median increase of 2.3 percentage points will be required to close the financing gap by 2063. In 17 African countries, the required increase in tax effort for structural transformation is estimated at less than 5 percentage points for the SDG deadline of 2030—or 38 countries for the Agenda 2063 deadline.

FIGURE 2.21 Required increase in tax-to-GDP ratio to close the estimated annual financing gap in Africa



Source: Staff calculations based on methodology described in annex 2.2 and database from African Development Bank statistics, Sachs et al. (2023), UNESCO, CIA, NASA, IMF, and World Bank.

To assess whether such tax efforts could be reasonably made by African countries, figure 2.22 compares each country's estimated tax-to-GDP ratio compatible with the need to fast-track structural transformation, notably the tax-to-GDP ratio that allows for closing the financing gap, with each country's tax capacity,[64] defined as the predicted value of the potential tax-to-GDP ratio. Tax capacity provides a benchmark for the maximum amount of tax revenue that could be collected given a country's socioeconomic and institutional factors. Negative values in figure 2.22 mean that a country's estimated tax-to-GDP ratio deemed necessary to close its financing gap surpasses its maximum achievable level given its macroeconomic, demographic, and institutional characteristics. Out of the 39 African countries with data on tax capacity, 18 (46.2 percent) display unattainable tax-to-GDP ratios required for structural transformation if 2030 is the target year—or three countries when 2063 is considered.

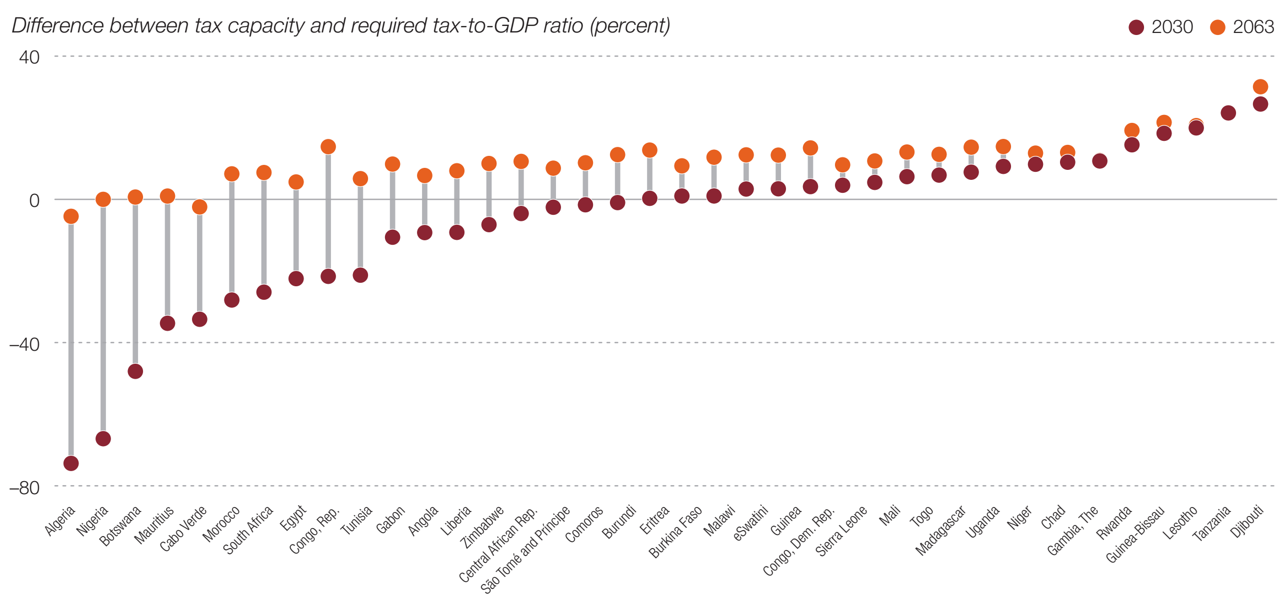
This finding suggests that, regardless of the deadline, domestically mobilized resources might not be sufficient in some African countries to close the existing financing gap for structural transformation. The international financial architecture, with contributions from the private sector, should therefore be an integral part of the financing strategy, not only to complement domestic resources but also to facilitate access to more affordable external resources (chapter 3).

Enhancing efficiency in public spending and tax collection is as important as mobilizing more resources

A large portion of public investment in Africa is lost to inefficiency. Evidence suggests that Africa has a public investment efficiency gap of 39 percent, higher than Europe (17 percent) and Asia (29 percent).[65] In addition, before the COVID-19 pandemic, Africa recorded the world's highest average tax cost—calculated as the ratio of the cost of administering the tax system to total revenues collected by the tax administration. For example, the average cost of tax collection in Latin America and the Caribbean (1.05) was less than half that of Africa (2.31): for every $100 collected, Africa's tax administration cost $231 on average against $105 in Latin America and the Caribbean. All other regions—East Asia and Pacific (1.23), Europe and Central Asia (0.68), North America (0.72), and South Asia (1.56)—had lower cost of tax collection than Africa.

A large portion of public investment in Africa is lost to inefficiency

FIGURE 2.22 Required tax-to-GDP ratio for structural transformation and its predicted potential value



Source: Staff calculations based on methodology described in annex 2.2 and database from African Development Bank statistics, Sachs et al. (2023), UNESCO, USAID, CIA, NASA, IMF, and World Bank.

Further, due to widespread practices of zero-ratings and tax exemptions, as well as inefficiencies in enforcement and frequent noncompliance, Africa lags other regions in efficiency of value-added tax (VAT) collection, measured as the ratio of VAT revenue (as a percentage of GDP) to the VAT rate. At the median, African countries collected annually in 2000–21 only 24 percent of the VAT revenues that they could otherwise have collected with full compliance and without tax exemptions (figure 2.23).

Enhancing the efficiency of public spending and tax collection is thus crucial to closing the huge financing gap for structural transformation. We estimate that, by just increasing the VAT efficiency ratio to the level currently achieved by high-performing developing countries in other regions—those with a VAT efficiency rate of at least 70 percent[66]—African countries can raise their current median VAT revenues (as a share of GDP) by as much as 7.9 percentage points (figure 2.24). Improving the efficiency rate in the collection of other types of tax revenues, such as corporate income, personal income, excise, and property taxes, could also help the continent to self-finance a significant share of its financing gap for structural transformation.

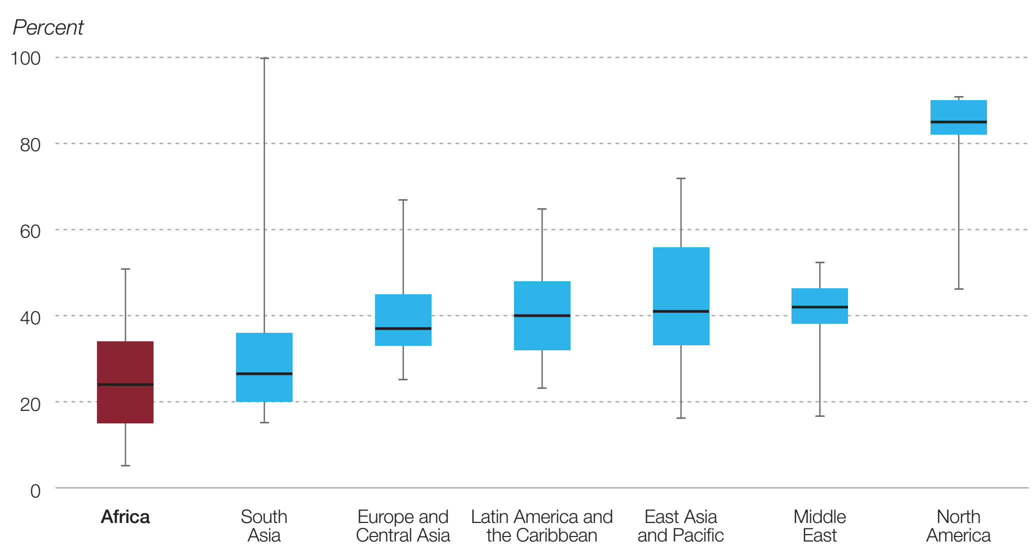
At the median, African countries collected annually in 2000–21 only 24 percent of the value-added tax revenues that they could otherwise have collected with full compliance and without tax exemptions

Resource mobilization from critical and rare earth minerals

Critical and rare earth minerals present Africa an opportunity to mobilize resources for complementing its tax revenues

Africa is rich in natural capital. For instance, the continent is home to the Congo Basin Rain Forest, the world's second-largest rainforest after the Amazon, accounting for 25 percent of global biodiversity. Africa contributes hugely to global production of key minerals: 80 percent of platinum, 77 percent of cobalt, 51 percent of manganese, 46 percent of diamonds, 39 percent of chromium, and 22 percent of gold.[67] These natural resources are fundamental to many African economies, often constituting a major source of export earnings and government revenues. In 2021, African economies earned about $277 billion in resource rents, accounting for an average of 11.4 percent of GDP of beneficiary countries (figure 2.25a). These rents concern mainly forest products, oil, and minerals and, to a smaller extent, coal and natural gas (figure 2.25b). If valued, managed, and harnessed well, revenues from these natural resources could generate resources to complement existing domestic resources for financing structural transformation.

FIGURE 2.23 **VAT efficiency ratio in Africa vs other regions, average 2000–21**

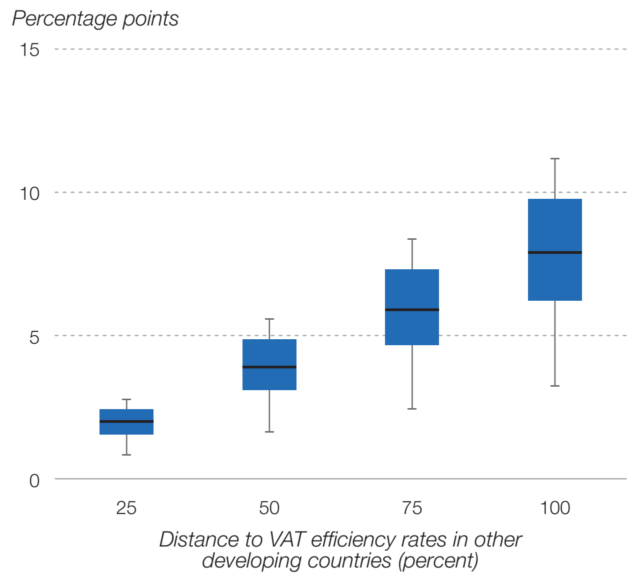


Source: Staff calculations based on USAID Collecting Taxes Database.

Of particular interest are critical and rare earth minerals. Indeed, Africa is at the center of the global supply chain of such minerals, given its substantial endowments in lithium, cobalt, nickel, manganese, graphite, iron, and phosphate, and the critical minerals needed for clean energy technologies such as solar photovoltaic and lithium-ion batteries used in electric vehicles and electricity storage. The increase in clean energy deployment in recent years has led to a huge rise in demand for critical minerals. From 2017 to 2022, demand for lithium tripled while that of nickel and cobalt increased by 40 percent and 70 percent, respectively.[68]

Coupled with higher prices, the global market size of key critical and rare earth minerals—copper, lithium, nickel, cobalt, and graphite—doubled, reaching $320 billion in 2022. Investment in critical minerals development recorded another sharp uptick worldwide of 30 percent in 2022, after a 20 percent increase in 2021, while critical minerals startups raised a record $1.6 billion in 2022. Global exploration spending for critical minerals increased by 20 percent in 2022, driven by record growth in lithium exploration (90 percent growth in 2022, after 25 percent expansion in 2021). Exploration interests, as

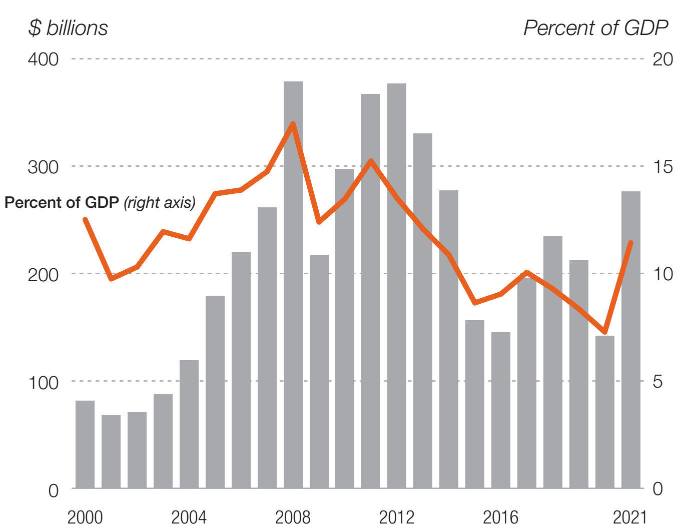
FIGURE 2.24 Potential increase of VAT revenue (percent of GDP) from improved VAT efficiency rates in Africa



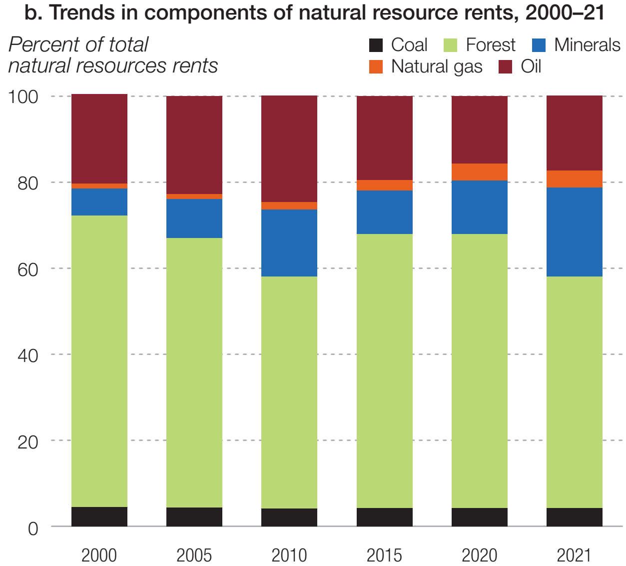
Note: The figure gives the (median) percentage point increase of VAT revenues (as a percent of GDP) when African countries close by various percentages (horizontal axis) the current VAT efficiency gap with high-performing developing countries.
Source: Staff calculations based on USAID Collecting Taxes Database.

FIGURE 2.25 Total natural resource rents in dollars and as a percent of GDP, 2021

a. Trends in Africa's total natural resource rents, 2000–21



b. Trends in components of natural resource rents, 2000–21



Source: Staff calculations using World Bank's World Development Indicators.

well as extraction and processing activities, are expanding in Africa, too.

Demand for critical minerals for clean energy technologies is projected to continue surging in all scenarios. Projections by the International Energy Agency (IEA) indicate that, under the 2050 net-zero emissions scenario, demand for critical minerals will grow by three-and-a-half times to 2030 from 2021 levels, reaching more than 30 million tons (figure 2.26). Electric vehicles and battery storage will be the main drivers of demand growth, in addition to major contributions from low-emission power generation and electricity networks.

Under the 2050 net-zero emissions scenario, global revenues from the production of just four key minerals—copper, nickel, cobalt, and lithium—are estimated to amount $16 trillion over the next 25 years (in 2023 US dollar terms), with Africa expected to reap more than 10 percent of these cumulative revenues. For African countries rich in these critical minerals,[69] this boom provides an opportunity to complement their domestic revenues for structural transformation by moving from merely extracting and exporting these raw minerals to processing them, thereby increasing value added, creating higher-skilled jobs, and increasing foreign reserves.

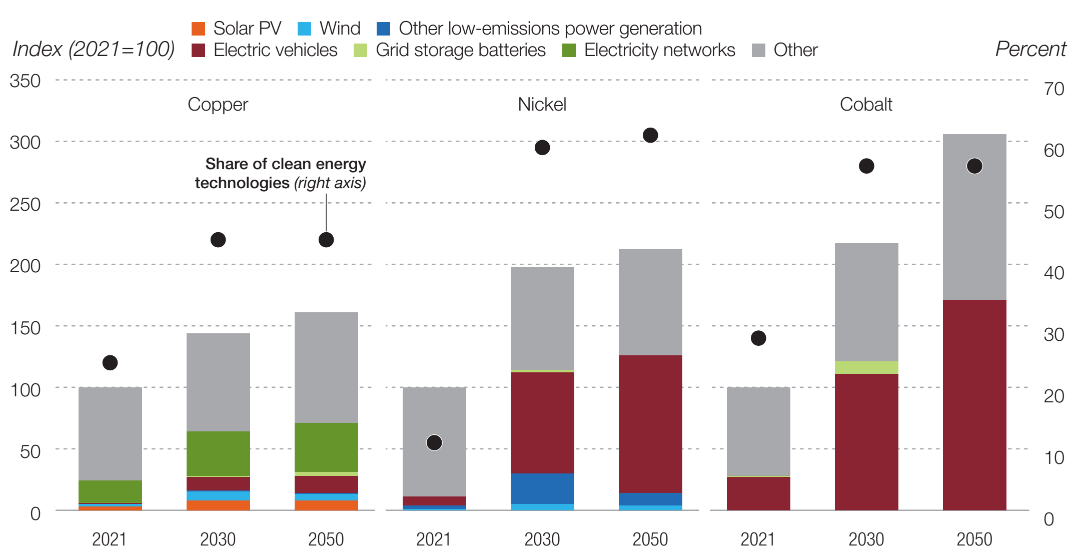
Under the 2050 net-zero emissions scenario, demand for critical minerals will grow by three-and-a-half times to 2030 from 2021 levels, reaching more than 30 million tons

POLICY RECOMMENDATIONS

The above analyses strongly suggest that accelerating Africa's structural transformation will require a multipronged approach, consisting of the following elements, spearheaded by African countries:

1. **Establish and institutionalize endogenous development plans and policies tailored to areas of comparative advantage as priorities and implement them consistently, while avoiding policy reversals that tend to disrupt progress.** To address their development challenges, African countries need not outsource their development plans. Instead, they should take full ownership by harnessing local knowledge of their economies and sociocultural conditions and other unique areas of comparative advantage, within the national, regional, and global contexts. The rate and pace of structural transformation of African countries will largely depend on the quality, relevance, and effectiveness of policies and on the continued and institutionalized implementation of development plans and strategies. Therefore, there should be unreserved political commitment to rally citizens toward a nationally agreed development plan and vision,

FIGURE 2.26 **Trends in global demand for selected minerals by end use in the net-zero scenario, 2021–50**



Source: Staff calculations based using the database from the IEA Critical Minerals Data Exporter.

avoiding electoral-cycle-induced recurrent and policy reversals that characterize most African countries. Continuous and systematic implementation of public policies, in particular linking fiscal policies to structural transformation objectives, will create certainty and stability to attract domestic and foreign capital into areas supportive of the country's structural transformation agenda. Countries operate in a regional and global village, so national development plan needs to domesticate regional and global development goals, such as the SDGs, Paris Climate Agreement, and Agenda 2063, with a focus on practical actions that improve the quality of lives of their citizens. The national development agenda needs, however, to be driven by citizens to secure their buy-in and improve the quality of their lives.

2. **Scale up investments to build requisite human capital suited to local realities, circumstances, and development priorities.** Countries need to scale up investments in education at all levels to build and improve the quality and relevance of technical and soft skills to drive their development agenda tailored to local contexts and circumstances. This will require prioritizing systems of learning and curriculum that enhance productivity growth in sectors of comparative and competitive advantages. For example, countries need to prioritize scaling-up skills in science, technology, engineering, and mathematics (STEM). And those rich in natural resource endowments—minerals and vast arable land—will need to train enough geologists, agronomists, and other related experts to leverage their resources to drive structural transformation. Furthermore, the domestication of the education and skills learning and training systems, including the language of teaching, will be crucial to improve the quality and relevance of the education curriculum and leverage the ongoing technology and ICT boom. As a matter of policy priority, it is important for African countries to establish innovation centers of excellence, in collaboration with host universities and technical and vocational training centers; develop demand-driven skills training programs to better align education and training systems to labor markets and thus reduce widespread skills mismatches; strengthen public–private partnerships to align skills acquisition of graduates with labor market needs; and franchise their education system in partnership with global universities to build world class education institutions.

   Cognizant of the importance of adapting and upgrading education curriculum in its regional member countries, the African Development Bank has been in the forefront of supporting enabling education infrastructure and skills acquisition. For instance, the Bank supported the Regional Center of Excellence in ICT in Rwanda, in collaboration with the Carnegie Mellon University, to provide world-class master's degree programs in computer sciences and ICTs. The Bank's Coding for Employment program is a leading flagship initiative to equip the continent's youthful workforce with demand-driven skills with the overarching objective of creating a critical mass of digitally enabled and globally competitive youth who harness the transformative power of the fourth industrial revolution.

Countries need to scale up investments in education at all levels to build and improve the quality and relevance of technical and soft skills to drive their development agenda tailored to local contexts and circumstances

3. **Scale up domestic resource mobilization and prioritize prudence in public finance management.** African countries need to own their development agenda and have the primary responsibility for financing their structural transformation. However, in most countries, domestic resource mobilization (DRM) has yet to keep pace with Africa's enormous development financing needs and effectiveness in public financial management remains weak. Countries should consider the following:

   Tax revenue mobilization. The Bank estimates that the median African tax-to-GDP ratio should increase from its current level—about 14 percent—to a minimum of 27.2 percent to be able by 2030 to close the estimated annual financing gap of $402.2 billion for structural transformation. To scale up DRM for structural transformation, countries need to invest in systems that improve efficiency in tax administration and public financial management. This will require, for instance, enhancing the digitalization of tax collection and administration systems. Evidence has shown that digitalization of tax administration would increase information flows and improve the transparency of the tax system, widen the tax base, enhance enforcement, mitigate compliance risks, and ultimately stimulate voluntary compliance.[70] Digital technology allows pre-filling tax declarations using third-party information, thus easing the tax compliance burden because taxpayers can simply check and confirm the pre-filled information. Electronic cash registers also help governments track sales and transactions by transmitting information in real time to a server accessed by tax authorities. In addition, the establishment of a solid, regularly updated database will allow the identification and location of the individuals, firms, or landed properties on which to levy a tax. The Bank estimates that by increasing efficiency of VAT collection to the levels achieved by high-performing developing countries, African countries can raise VAT revenues by up to 7.9 percentage points of GDP.

African countries will need to improve tax compliance by enhancing the social contract with their citizens

Nontax revenue mobilization. Countries could also aim at increasing nontax revenues such as property income, royalties, fines, penalties, forfeits, and business permits,[71] which are often neglected or difficult to administer due to the complexity of processes and widespread informality of economies. Although some progress has been achieved over the years, there is still room for improvement in collecting nontax revenues in most countries. For example, over 2010–22, nontax revenues accounted on average for only 19.1 percent of government revenues in Africa and just 3.7 percent of GDP, while tax revenues brought in 80.9 percent of government revenues (15.6 percent of GDP). PFM systems should incorporate nontax revenue planning into the budgetary process, ensuring that the revenues collected are not only efficiently allocated but also well used. Strong political commitment will be needed to develop expertise in core departments and fiscal units in charge of collecting such revenues. Due diligence, clear guidelines, and built-in regulatory systems will be needed to design an effective structure of nontax revenue. And countries can use innovative instruments to collect more resources—from levies on natural resources extraction to pollution fees or marketing associations—that may be hard to reach through conventional means. Other reforms to strengthen nontax revenue mobilization could include investing in enabling infrastructure, better reporting of nontax revenue collection, and clearer relationships between the central government and subnational authorities.

Tax compliance. African countries will further need to improve tax compliance by enhancing the social contract with their citizens. Countries should seek to promote voluntary tax compliance to increase DRM as enforcement capacities which are often weak in many countries and hard-to-tax sectors, such as informal companies, predominate. More importantly, governments should visibly use tax revenues for public welfare—by providing quality public goods and services—to enhance trust in the utilization of public resources and significantly reduce implicit taxation (where citizens self-provide social amenities because of the failure of the government to fulfill its regalian functions such as the provision of basic social services). In countries that practice federal and devolved systems of government, there is a need to democratize DRM and utilization by bringing tax systems closer to the people.

Informal economy formalization. Enhancing the formalization of the informal economy could also boost DRM. The size of the informal sector in Africa significantly limits the tax base and revenue collection. For instance, informal employment in Africa accounts for 85.8 percent of total employment, the largest percentage in the world[72]. To promote formalization, policymakers could take a broader strategic approach that seeks to register informal firms not only to tax them but also to protect their rights, entitlements, and assets as entrepreneurs. The attractiveness of the formal sector can be enhanced, for example, by providing greater access to resources and information, pension schemes, social insurance, or other incentives—conditioned on registration—through intermediaries such as business associations, nongovernmental organizations, or local community groups. A flat rate presumptive tax levied on turnover can improve revenue collection from informal firms. Despite the difficulties and biases associated with estimates of turnover, especially for small businesses, this approach appears to have been effective in taxing the informal sector in Tanzania.[73]

Public finance management. In addition to improving domestic revenue mobilization, countries need to build capacity in prudential and efficient management of public finance throughout the public financial management cycle – from DRM to strengthening supreme audit and public accountability systems. As Africa's premier financial institution, the Bank is playing a critical role in supporting regional member countries to increase their DRM and improve their PFM systems. For instance, the Bank's Public Finance Management Academy (PFMA) responds to the urgent need for accelerated capacity development (training, technical assistance, and policy dialogue) in African countries. Through the PFMA, the Bank has created a virtual interactive collaborative environment, virtual knowledge repositories; a policy lab unit, and a virtual campus on PFM for real-time support to public officials in African countries. Its first cohort of 51 public officials from 26 countries, graduated in December 2023.

4. **Build and deepen national and regional markets for goods, services, capital, and finance.** Developing domestic and regional financial and capital markets will reduce countries' dependence on external markets and thereby minimize vulnerability to global shocks. Developing robust financial markets will require improving property rights' regimes, diversifying the supply of financial products and services in the banking sector, and regionalizing financial markets through legal harmonization and cross-listing of assets at the regional level. Capital markets development will require creating an enabling policy and regulatory environment to mobilize at scale and channel resources held by pension funds, insurance and collective investment schemes for financing structural transformation. In that regard, the AfCFTA can be a game changer if fully implemented and domesticated by all African countries. It will create a single continental market for goods and services, with free movement of capital and talent and skills. Implementing policies that enable free mobility of labor and services, such as the open visa entry for Africans championed by Kenya and Rwanda, would facilitate the operationalization of the AfCFTA.

Preferred procurement and pan-African payment policies. The launch in 2022 of the Pan-African Payment and Settlement System (PASS) by the African Union and the African Export-Import Bank to complement trading under the AfCFTA is a move in the right direction as it will help address currency risks between trading partners. The PASS simplifies the historical complexities and costs of making payments in local currencies across African borders, providing operational efficiencies that open vast economic opportunities for all stakeholders. The development of preferred procurement solutions will further encourage domestic production and consumption to enhance SME growth by enabling African countries to source raw materials and other inputs from each other and thus benefitting from mutual comparative advantages. It will build a hub of local products and markets, enhance value addition, create jobs, and help transform African economies. The continent has rich endowments in resources across all its five regions, and some countries have already managed to build capabilities in different sectors, including motor vehicle manufacturing in Morocco, Nigeria, South Africa, and Uganda; thriving tech hubs in Kenya and Nigeria; growing financial services in Mauritius; and aircraft parts manufacturing in Morocco. Such intra-African "friend-shoring" will help protect the continent from global shocks and strengthen regional value chains while deepening domestic markets. African countries could also facilitate, without nepotism, the emergence of

Developing domestic and regional financial and capital markets will reduce countries' dependence on external markets and thereby minimize vulnerability to global shocks

national champions tasked with leading the economic diversification process and fostering the creation of backward and forward linkages with smaller firms, which will result in deepening domestic markets.

Franchising and local content policies. Countries should further proactively pursue and promote a policy of franchising and leveraging technological know-how of foreign firms can also promote cross-border investment among African countries to complement local content policies and requirements, especially where capacity—technical and financial—is lacking. Africa's integration in global value chains and fast-paced structural transformation are conditional on technological adoption and innovation as well as skills acquisition. In the short term, many African countries will lack sufficient technical capacities and technology to benefit from the projected rise in the demand of critical and rare earth minerals. Through franchising, they could, however, close that gap by importing critical technologies, leveraging global innovations, and allowing foreign manufacturing firms and other producers to set up enterprises on the continent. Foreign firms should be required to facilitate the acquisition and adoption of frontier technologies by local workers through tailored skill-training modules. But to maximize the benefits of franchising, countries must identify domestic capacity gaps and select franchising models that suit their contexts and serve best their interests.

The use of innovative financing instruments such as blended finance could increase private participation in infrastructure for green growth by derisking the sector

5. **Create targeted and streamlined incentives to catalyze private capital flows to support countries' endogenous development plans in key sectors for structural transformation.** By making the conditions right for the private sector and by creating a conducive business environment and providing carefully crafted and targeted fiscal incentives, African countries could stimulate the private sector—domestic and external—to invest more in critical sectors. The use of innovative financing instruments such as blended finance could increase private participation in infrastructure for green growth by derisking the sector. The development of sustainable finance instruments (including green bonds and loans, and sustainability bonds and loans) as well as carbon markets could boost private investment in green sectors. Indeed, the potential of the private sector to contribute to Africa transformation is huge: global assets under management amounted to $98 trillion at end-2022[74] and are expected to reach $145.4 trillion by 2025.[75] In addition, remittances—the largest and most stable source of external funding in Africa—are an important source of external financing. Their function in promoting investment for Africa's transformation can be enhanced through, for instance, diaspora bonds and diaspora "remittance securitization." Countries could also hive off their subsidies to state-owned enterprises to allow them to operate efficiently and competitively and contribute to the state budget. Containing tax avoidance and illicit financial flows would also curtail the drain of public resources.

6. **Invest in natural capital accounting beneficiation and conservation and include them in the system of national accounts to expand the size of the economy.** Much of Africa's natural capital resources remains largely unexploited, and the values or services they provide are typically poorly measured and sometimes completely unmeasured as part of African countries' wealth. As a result, the value of African economies continues to be underestimated amid the abundance of green wealth. Investing in, measuring, and valuing natural capital and integrating it in the systems of national account will help estimate the true value of Africa's green wealth, expand its GDP, and improve conservation. The Bank, in collaboration with many African countries, has been advocating proper valuation of the continent's green wealth and its services in GDP. Indeed, Africa's natural resources provide essential environmental services such as carbon sequestration, pollution control, and retention of soil fertility, which sustain human existence. The inclusion of such critical environmental services in the valuation of country GDP—the green GDP—could encourage countries' green transitions.

7. **Invest in youth entrepreneurship development programs to harness Africa's demographic dividend.** The youth are Africa's greatest asset, which, if well harnessed, could speed structural transformation. By 2030, one in four youth in the world will be African, and, if well nurtured, this youthful population can drive the continent's future economic growth and structural transformation. However, reaping the benefits of the demographic dividend from the African youth will depend on investing in human capital development and creating economic and job opportunities for the youth. Of youth aged between 15 and 35 years not in school, one-third are unemployed and discouraged, another third is vulnerably employed, and only one in six is in wage employment. The Bank estimates that 17 million jobs need to be created every month between now and 2063 to keep constant the participation and unemployment rates of African youth. Supporting youth to create their own businesses holds promise in leveraging the continent's democratic dividend and addressing the widespread youth unemployment and underemployment. That is why, under its Jobs for Youth in Africa Strategy and its Youth Entrepreneurship and Innovation Multi-Donor Trust Fund, the Bank is supporting countries in establishing Youth Entrepreneurship Investment Banks as a model to address market failures and fragmentation in the provision of tailored financing and nonfinancing services to youth entrepreneurs.[76]

8. **Launch ambitious national infrastructure programs for broad-based policy implementation to accelerate structural transformation.** While in the long term, all type of infrastructure is important, in the short term, countries need to prioritize which infrastructure to build depending on their geographic situation and level of development and concentrate limited resources on creating "islands of excellence" with dense and sector-specific infrastructure to boost productive capacities and competitiveness. Priority could be given to the energy sector, which is most likely to achieve a high social rate of return, and to the transport sector, which is especially important for landlocked countries in creating linkages to coastal countries with seaports. Given the significant transformational impact of digitalization, investing in the ICT sector will close the existing digital divide between African countries and the rest of the world. An ambitious national digitalization program in Africa will increase economy-wide competitiveness, enhance efficiency and transparency of policy implementation, improve DRM, and curb illicit capital flows as well as address widespread market efficiencies, facilitate proper measurement and valuation of natural capital, and support the competitiveness of youth-led businesses. Digital masterplans should clearly identify key pillars—in digital infrastructure, digital services, data management, digital skills, and digital innovation for entrepreneurship—with clearly set milestones. In Kenya, for instance, the combination of the money-transfer system M-Pesa with an online application for taxes (the iTax System) has helped increase tax filling, compliance, and revenues. The Government of Kenya has also launched a 10-year Information Communication Technology Digital Masterplan 2022–32 to align with global technological advances and enhance the rise of Kenya's digital economy. This will further position Kenya as a technology hub in Africa.

   The Bank has been investing in core digital infrastructure and skills and in enabling infrastructure such as connectivity and energy in African countries. For example, it invested more than $1.5 billion over the past 10 years in ICT infrastructure development projects across the continent.

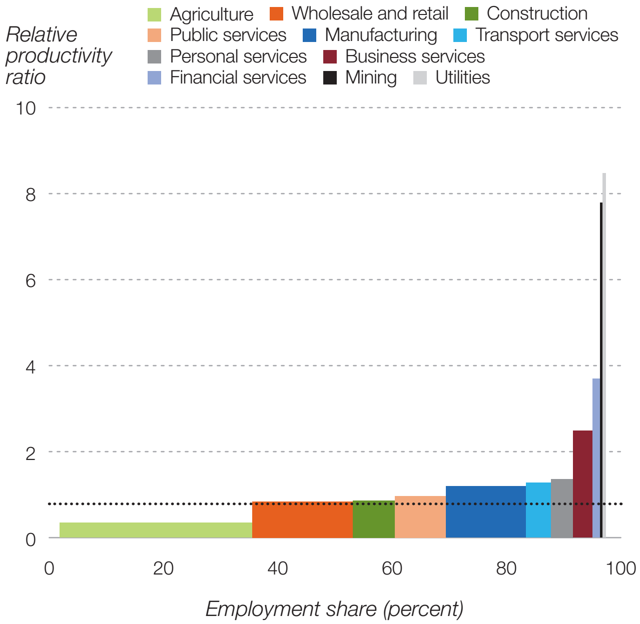
Reaping the benefits of the demographic dividend from the African youth will depend on investing in human capital development and creating economic and job opportunities for the youth

9. **Take proactive actions to harness governance of macroeconomic policies and business environment to improve risk profiling and perceptions and attract innovative global capital and financial instruments to build capacity in project preparation.** The lack of investment-ready project pipelines is often cited among the most important impediments not only to unlocking private finance but also leveraging existing innovative finance instruments. Large infrastructure projects have extensive development and gestation periods

and often entail multifaceted feasibility studies and expert transaction advice. Many African governments and local private players lack the capabilities, as well as the resources, to design and implement infrastructure projects with commercial potential. In addition, short political cycles may constrain private sector financing commitments to long-term infrastructure projects. Many investors therefore lack bankable project pipelines as only a few projects meet financiers' risk–return expectations, and so fail to reach financial closure. Building capacity in project preparation and implementation is therefore crucial. Building such capacity would require, for instance, that private financiers not only provide resources but also participate in building bankable projects. The participation of financiers across the entire project cycle from concept to bankability—from development of strong feasibility studies to analysis of market prospects and establishment of viable business plans—and financing will ensure that they have a stake in and ownership of proposed projects. That will increase the probability of the project receiving finance and succeeding when it becomes operational. Moreover, enhancing governance of the macroeconomic and investment climate will improve risk profiling of African countries and change external perceptions about African markets. The Bank's Strategy for Economic Governance in Africa aims to promote transparency and accountability in public service delivery, stimulate government effectiveness, building enabling environments for business, fighting corruption, and enhancing the institutional frameworks to efficiently manage the economy.

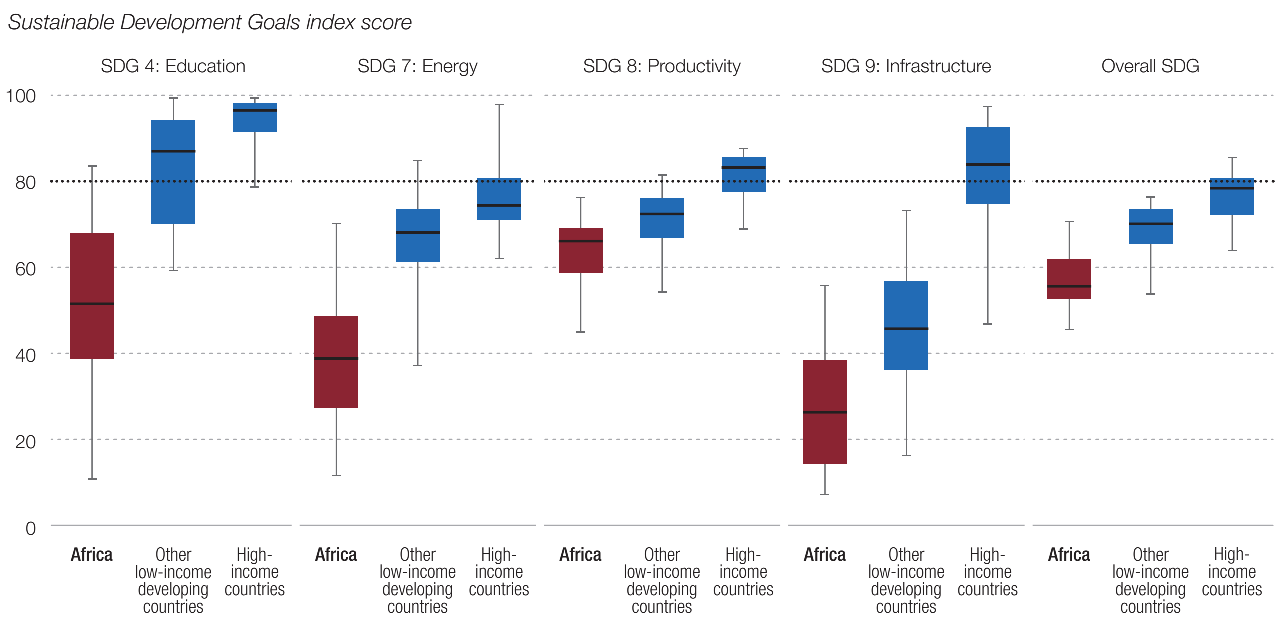
ANNEX 2.1 ANNEX FIGURES

ANNEX FIGURE 2.1.1 Relative sectoral productivity and employment shares in developing Asia, 2018



Note: The figure shows the average of 14 developing Asian countries: Bangladesh, Cambodia, China, India, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Nepal, Pakistan, Philippines, Sri Lanka, Thailand, and Viet Nam.
Source: Staff calculations using Economic Transformation Database (Kruse et al. 2023).

ANNEX FIGURE 2.1.2 Africa's performance on structural transformation–related SDG targets benchmarked with other regions, 2022



Note: High-income countries are countries with GNI per capita greater than or equal to $13,846 in 2022.

Source: Staff calculations based on database from Sachs et al. (2023).

ANNEX 2.2 METHODOLOGY TO ESTIMATE FINANCING NEEDS AND FINANCING GAP TO FAST-TRACK STRUCTURAL TRANSFORMATION IN AFRICA

Estimates of the financing needs and financing gap to fast-track structural transformation in Africa are computed building on the benchmarking methodology linked to the Sustainable Development Goals (SDGs) developed by Gaspar et al. (2019) and applied, among others, by Prady and Sy (2023). For this chapter, the methodology quantifies the annual cost of achieving high SDG performance in four areas most directly relevant to structural transformation (see below).

For each African country, the estimated financing gap corresponds to the additional total expenditure required, compared with what the country spent in 2023 (or latest available year), to reach the spending level currently attained by high-performing countries, defined here as developing countries in other regions of the world with an SDG index score above 80 (out of a maximum of 100). These non-African developing countries had a gross national income (GNI) per capita below \$13,846 in 2022. Since these high-performing countries are used as benchmarks for each African country, costing estimates assume high spending efficiency. Two deadlines are used as target years: 2030 for the SDGs and 2063 for the African Union's Agenda 2063.

SDG 4: Quality education

Education, considered as "soft" infrastructure, is a key component to equip the current and future workforce with the required skills set for structural transformation. This chapter uses government expenditures per student by main education level (primary, secondary, and tertiary) as a proxy for government efforts to improve the quality of education. For each education level, the methodology sets values of education spending at the median levels observed today in other developing countries with high education outcomes (SDG 4 index score above 80). Next, for each African country, the education financing needs are estimated using the corresponding benchmarked key input variable costs and the country's school-age population for each education level with the targets of 100 percent enrollment rates in primary and secondary education and 50 percent in tertiary education, in line with the SDG 4 target. The education financing gap is then defined as the difference between the financing needs per student and the current government education spending per student, multiplied by the school-age population of each education level to obtain the total financing gap by education level for the country.

SDG 7: Energy

Lack of access to affordable, reliable, sustainable, and modern energy for all is also holding the continent back from leveraging its full development potential and accelerating its structural transformation. For each country, therefore, this chapter estimates the additional cost needed to provide universal access to electricity of the projected population by each deadline, while assuming that per capita electric consumption will increase in line with the rise in real GDP per capita. The projected median per capita electricity consumption (in kWh) in other developing countries with an SDG 7 index score above 80 percent is then applied as the benchmarked input variable that African countries should aim for. The cost associated with the financing needs and financing gap in the energy sector is then obtained by multiplying the corresponding total kWh with the global weighted average of the levelized cost of electricity (LCOE) per kWh observed in 2010–21 for renewables, which was \$0.126.[77] The LCOE refers to the cost of producing one kWh of electricity from a particular technology (in the present case, bioenergy, geothermal, hydropower, solar photovoltaic, onshore and offshore wind, and concentrated solar power), including capital costs, fixed and variable operation and maintenance (O&M) costs, and fuel costs. Although the LCOE does not necessarily reflect the true cost of putting up energy infrastructure and distributing electricity, it provides investors and governments with an idea of what it will cost to recoup their investments, once established.

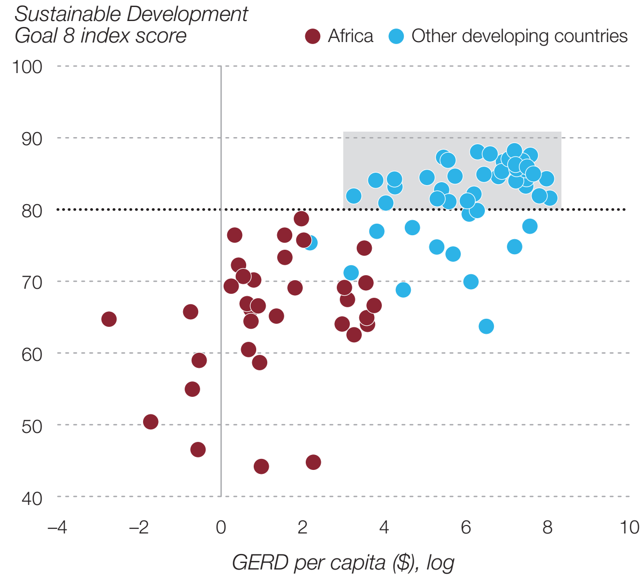
SDG 8: Productivity

Closing Africa's productivity gap—one of the main proxies to measure progress on structural transformation—requires technological upgrading and innovation, as highlighted in the SDG 8.2 target. To measure countries' technological upgrading efforts and innovation capacity necessary to improve productivity, this chapter uses gross domestic expenditure on research and development (GERD) per capita. The benchmarking exercise is similar to the one applied for education: median values of GERD per capita observed today in non-African developing countries are computed. Next, for each African country, financing needs to accelerate technological upgrading and innovation are obtained as the level of GERD per capita using the corresponding benchmarked median cost and the country's population. The financing gap is then measured as the difference between the financing needs and the current level of GERD. It is assumed that GERD per capita of each country will grow according to the rate of per capita GDP growth provided in the *World Economic Outlook* of the International Monetary Fund (IMF). Given that current IMF projections for GDP per capita (and therefore the growth rate) are up to 2029, GDP per capita was assumed to grow at the average rate of the last three years in each country for the years beyond 2029. This assumption allows for the tractability of the approach and can be relaxed as new growth projections become available. Annex figure 2.2.1 illustrates the benchmarking exercise for SDG 8.

SDG 9: Infrastructure

Hard infrastructure such as transport infrastructure is critical to structural transformation by facilitating, at lower cost, free movement of labor between regions with a surplus or shortage of skills and/or economic opportunities, as well as by enabling firms to thrive in economic sectors with strong comparative advantage (AfDB 2018). Road transport, in particular, is the most frequently used means of transporting goods and people across the continent, carrying at least 80 percent of goods and 90 percent of passengers.[78] This makes Africa's road transport infrastructure one of the key enablers of structural transformation.

ANNEX FIGURE 2.2.1 Derivation of benchmarked values for spending on R&D per capita



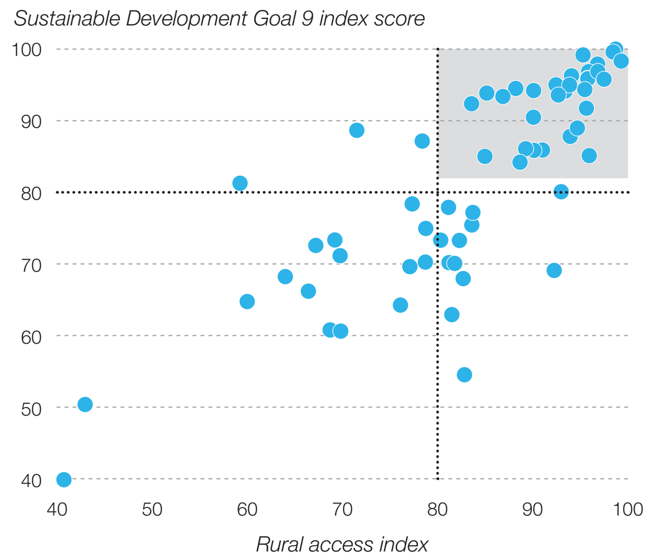
Note: Countries in the box with a SDG 8 index score above 80 are used to benchmark the level of per capita gross domestic expenditure on research and development (GERD) of African countries consistent with high SDG 8 outcomes.

Source: Staff calculations based on database from Sachs et al. (2023), UNESCO and World Bank.

In this chapter, only power (see previous point) and transport (road) infrastructure are considered. These two elements are among the most critical to Africa's structural transformation, in addition to ICT infrastructure as a means of implementation (SDG 17). For road infrastructure, road density (the ratio of the length of the country's total road network, in km, to the country's land area, in km^2) and the Rural Access Index—the proportion of the rural population living within 2 km of an all-season road—are used as input variables to capture a country's current state of road infrastructure. Benchmarked values of these input variables were computed for the subset of non-African developing countries with high performance: SDG 9 index score and rural access index above 80 (annex figure 2.2.2).

Using the benchmarked values, we estimate, for each country, the necessary kilometers of roads needed to catch up by 2030 or 2063 to the

ANNEX FIGURE 2.2.2 Derivation of benchmarked values for road density



Note: The countries in the box are non-African developing countries with high performance on SDG 9, proxied with the SDG 9 index score and rural access index above 80, used to measure the level of road density of African countries consistent with high SDG 9 performance.
Source: Staff calculations based on Gaspar et al. (2019), Mikou et al. (2019) and database from World Bank, CIA, NASA, and Sachs et al. (2023).

road density in high-performing peer countries, accounting for the country's land area. We then estimate the total cost of road network needs by multiplying the estimated necessary kilometers by the unit cost of constructing/upgrading one kilometer, which is set at a minimum of $500,000, following Iimi et al. (2016). To account for depreciation, we increase the unit total cost per kilometer by 5 percent, following Gaspar et al. (2019) and Prady and Sy (2023). The additional road network (road infrastructure deficit) for each African country, compatible with high performance on SDG 9 and the Rural Access Index, was then computed as the difference between the median road density in peer countries and the current road density, multiplied by the country's land area (net of terrestrial protected areas).[79] The corresponding financing gap was then obtained by multiplying the total additional road network by the unit cost of constructing/upgrading one kilometer.

NOTES

1. https://www.bcg.com/publications/2023/the-tide-has-changed-for-asset-managers
2. https://www.pwc.com/ng/en/press-room/global-assets-under-management-set-to-rise.html
3. As used in this context, *green wealth* is a term denoting "the unmeasured value of Africa's natural capital," as espoused by Dr. Adesina, President of the African Development Bank Group. See https://www.afdb.org/en/news-and-events/speeches/keynote-speech-dr-akinwumi-adesina-president-african-development-bank-group-40th-anniversary-guardian-newspapers-lagos-nigeria-28-november-2023-66327.
4. Countries that have successfully transitioned from low-income to high-income status generally undergo a structural transformation, which involves four main features: a falling share of agriculture in economic output and employment; a rising share of urban economic activity in industry and modern-services; migration of rural subsistence workers to urban settings; and a demographic transition in birth and death rates that always leads to a spurt in population growth before a new equilibrium is reached.
5. This is a narrow sense of structural transformation because the concept is often defined to include the urbanization and demographic transition that typically accompany economic growth (Timmer 2012).
6. Fosu 1999; Smith 2021.
7. Iyoha 2000.
8. Adjei et al. 2014.
9. Smith 2021.
10. McMillan and Harttgen 2014.
11. Structural change is the reallocation of economic activity across agriculture, industry, and services. It is sometimes used interchangeably with "structural transformation", which extends to include social changes such as demographic shifts, institutional adjustments, and changes in social structure (see Gollin and Kaboski 2024 for new forms of structural transformation).
12. Mensah et al. 2023; McMillan et al. 2014.
13. McMillan et al. 2014.
14. Diao et al. 2021; Kruse et al. 2023.
15. Kaldor 1968; Haraguchi et al. 2017.
16. Hirschman 1958.
17. Rodrik 2016; 2022.
18. Rodrik 2013.
19. Diao et al. 2021; Baldwin and Forslid 2023.
20. GCA 2021.
21. Mbow et al. 2019.
22. Sen 2019.
23. Lopez et al. 2023.
24. Caldera Sánchez and Röhn 2016.
25. McMillan et al. 2014.
26. Diao et al. 2019.
27. See McMillan and Rodrik (2011).
28. Kruse et al. 2023.
29. Diao et al. 2021; Kruse et al. 2023.
30. Cust and Zeufack 2023.
31. Kruse et al. 2023.
32. Diao et al. 2021.
33. See Fan et al. (2023).
34. AfDB 2024.
35. All the data used to compute this variable are from Penn World Tables 10.1.
36. The Balassa-Samuelson effect suggests that an increase in wages in the tradable goods sector of an emerging economy will also lead to higher wages in the nontradable (services) sector of that economy.
37. McMillan et al. 2014; Mensah et al. 2023.
38. For instance, Deininger et al. (2014).
39. Rodrik 2022.
40. McMillan and Zeufack 2022.
41. See Weiss (2005) and Tasneem and Biswas (2016).
42. Shivakumar et al. 2022.
43. Diao et al. 2024.
44. Timmer 2012.
45. AfDB 2021a.
46. OECD 2020.
47. Gollin et al. 2016.
48. See, for example, Nayyar et al. (2021).
49. Herrendorf et al. 2022.
50. EIB 2021.
51. Nayyar et al. 2021.
52. See, for instance, Bento and Restuccia (2021).
53. UNCTAD 2022.
54. Fan et al. 2023.
55. US Bureau of Labor Statistics 2014 and Miglani 2023.
56. For a discussion of these amenity differences, see Gollin et al. (2021).
57. For example, Gollin and Kaboski (2024).
58. Barrett et al. 2022.
59. The World Bank's current country classification by income level is used: developing countries are

defined as those with a gross national income (GNI) per capita below $13,846, and high-income countries as those with a GNI per capita of $13,846 or more.

60. AfDB 2018.
61. It was assumed that African countries target 100 percent enrollment rates for primary and secondary education (with six years of education each) and a 50 percent enrollment rate for tertiary education (Gaspar et al. 2019).
62. AfDB 2020.
63. UNCTAD 2019.
64. See USAID (2023) for more details on the computation of tax capacity.
65. AfDB 2021b.
66. This value represents the 95th percentile of the VAT efficiency ratio in other developing countries.
67. https://am.afdb.org/en/programme/thematic-knowledge-event-2-harnessing-natural-capital-finance-climate-and-green-growth.
68. IEA 2023.
69. The Democratic Republic of the Congo dominates the global cobalt market with more than 70 percent of global output and about 50 percent of the world's proven reserves. Other producers of critical minerals include South Africa, Gabon, and Ghana, together accounting for more than 60 percent of global manganese production. Guinea (bauxite), Mali (lithium), Mozambique (graphite), Zambia (copper), and Zimbabwe (nickel and platinum) are poised to benefit from this mining boom (IMF 2024).
70. UNCTAD (2018).
71. The main categories of nontax revenues include: (i) grants from foreign governments or international organizations (budget aid, food aid, capital transfers, current transfers, project grants, program grants, international debt relief, etc.); (ii) rents and royalties (such as oil or mining royalties); (iii) other property income (interest, dividends and other returns on government investment); (iv) sales of goods and services (which include some administrative fees); (v) fines and penalties (including fines and penalties due to tax violations), and (vi) miscellaneous and unidentified revenues (non-tax revenues that cannot be classified according to the other categories).
72. Kiaga and Leung (2020)
73. Monye and Abang (2021)
74. https://www.bcg.com/publications/2023/the-tide-has-changed-for-asset-managers
75. https://www.pwc.com/ng/en/press-room/global-assets-under-management-set-to-rise.html
76. For further details on job-rich reforms needed to stem the high rate of unemployment (especially among young people) in Africa, see Monga et al. (2019).
77. IRENA 2023.
78. AfDB 2014.
79. Terrestrial protected areas are totally or partly protected areas of at least 1,000 hectares designated by national authorities as scientific reserves with limited public access, national parks, natural monuments, nature reserves or wildlife sanctuaries, protected landscapes, and areas managed mainly for sustainable use.

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FINANCING STRUCTURAL TRANSFORMATION IN AFRICA: THE NEED FOR REFORMS OF THE GLOBAL FINANCIAL ARCHITECTURE

3

KEY MESSAGES

- **Since the 1970s, multilateral financial institutions, such as the international Bretton Woods Institutions—the World Bank, International Monetary Fund (IMF), and other global institutions—have collectively and individually been vital for financing development.** They have supported countries during major global economic challenges, such as the Latin American Debt Crisis of the early 1980s, the African Debt Crisis of the 1980s and 1990s, the Asian Financial Crisis of the late 1990s, the Global Financial Crisis of 2007–09, and the recent COVID-19 pandemic in 2020–21, to name a few. They have also supported economic recovery efforts in Africa and other developing regions by spearheading global response actions in times of crisis. Recent examples include the Debt Service Suspension Initiative, the G20's Common Framework for debt resolution, and the IMF's general allocation of $650 billion-equivalent in Special Drawing Rights (SDRs) to ease the fiscal and balance-of-payment challenges that several developing countries faced during the pandemic.

- **While multilateralism and international development finance institutions have served the world well, weaknesses remain.** The persistent weak global growth and recurring economic and financial crises. The growing global inequality and continuing human deprivation due to poverty, hunger, conflict, and fragility. The rising challenges to an open global trading regime. And the pervasive risks of pandemics, natural disasters, climate change, and geopolitical tensions. All suggest that more can be done to achieve the ideals for which these institutions were established. The respite they offer during a crisis is often short-lived, and the downside trends in economic fundamentals and risks often return in the medium term. Typical examples are Mexico's Tequila Crisis in 1994, and asset selloffs in 2013 after the United States Federal Reserve tightened monetary policy in the aftermath of the Global Financial Crisis. The same scenario is playing out in the post–COVID-19 period.

- **Today, the scale and nature of challenges have morphed into regional, national, and community crises, at levels where global institutions are ill-equipped to address them promptly.** How can the collective capacity and effectiveness of multilateralism and the global financial institutions to sustainably address contemporary global shocks be improved? By examining the changing nature of "global commons" challenges that the world faces today in health pandemics and climate change. By examining the changing nature of conflicts and geopolitical tensions. And by examining the interconnectedness of global value chains and economies to the extent that economic policy management now extends beyond national boundaries. National tools for policy management, such as domestic monetary policy to tackle inflation, are increasingly weakened by external shocks.

- **In addition, the current global financial architecture (GFA) and system of multilateralism is not delivering enough resources in a timely manner and scale to meet national and global development goals in Africa, including the Sustainable Development Goals (SDGs) and the African Union's Agenda 2063.** Neither the public nor private sector as currently constituted has been able to channel enough resources to address the development financing needs of Africa. The current system also makes access to development finance very expensive and cumbersome for African countries. The high cost of sovereign borrowing by these countries relative to their peers in other regions of the world often leads to debt vulnerabilities. The structure and scale of the current global climate finance architecture mirror the current GFA, making it difficult for the most vulnerable African countries to harness climate resilience opportunities. This climate finance architecture is complicated and loosely defined, misaligned with climate vulnerabilities and climate risks, and has been unable to channel enough resources to implement African countries' Nationally Determined Contributions.

The current global financial architecture makes access to development finance very expensive and cumbersome for African countries

- **Africa's sovereigns face higher costs of financing in international capital markets than advanced and emerging economies, given perceptions of risk and resultant mispricing of their sovereign debt by international investors originating from unfavorable credit ratings.** In 2021, African sovereign eurobonds were issued with yields above 5 percent and, in 40 percent of the cases, yields exceeded 8 percent. In contrast, the average sovereign bond yield for advanced economies was 1.1 percent and for emerging market economies, 4.9 percent. It has been estimated that African countries are paying 500 percent more in interest costs when borrowing in international capital markets than when borrowing from the World Bank or other multilateral development banks such as the African Development Bank.

- **To better respond to countries' development aspirations, institutional governance reforms in the multilateral institutions are urgently needed, to make the instruments of global financial governance more nimble, inclusive, and responsive.** To meet the scale and scope of global challenges, global financial institutions need to scale up development financing from billions to trillions of dollars. Achieving the required scale of financing will entail close collaboration between the public and private sectors across all levels—global, regional, and national—as well as development of innovative financing mechanisms to leverage resources from all sources. The World Bank, IMF, and regional development banks need to work more collaboratively and to deploy their risk capital more innovatively to leverage private capital at scale. There is also an urgent need to reform the GFA to make it nimbler and fit for orderly debt restructuring.

This need for reform is most evident in Africa, where the population still living in extreme poverty is estimated at about 34 percent, debt vulnerabilities are increasing, the benefits of international trade remain below expectations, and the impacts of climate change, to which the continent has not contributed, are costing it 5–15 percent of GDP per capita growth annually. Further, debt resolution in Africa, especially outside Paris Club processes, has been disorderly and protracted, with costly economic consequences.

According to the United Nations, the GFA is plagued with gaps, inequities, and inefficiencies, including disproportionate allocation of emergency funds to developing countries, even where these may already exist, as was evidenced during the COVID-19 pandemic and in food price hikes. This, on top of higher borrowing costs for developing countries even after adjusting for risk; underinvestment in global public goods, particularly climate action and pandemic preparedness; volatile capital markets with recurring global financial crises; and a less transparent international tax architecture that enables global tax evasion and avoidance. The G20 has also observed the need for reforms of the GFA. The 2018 Report by the Eminent Persons Group on Global Financial Governance, commissioned by the G20, recommended reforms of the GFA and governance of international financial institutions (IFIs) to promote economic stability and sustainable growth.[1] The report underlined the importance of ensuring that the IFIs contribute to growth and development in Africa. It stated that "to bend the arc of history we must succeed in Africa, where the poverty, demographic and environmental challenges are the largest—and so too are the opportunities to contribute to world growth and the global commons."[2]

- **Given their membership structures, the multilateral development banks and financial institutions—World Bank, IMF, AfDB, and other regional development banks—are best placed to lead global and regional efforts to mobilize and allocate resources at scale toward achievement of the SDGs in developing countries and to addressing global commons challenges.** But their governance structures (shareholding models and weighted voting systems) and scale of resources available to them often affect the speed and scale of financial flows to countries that need funding the most, as was evident during COVID-19 responses. Access to emergency financing was largely skewed toward developed economies that needed it least. For example, of the $650 billion in Special Drawing Rights (SDRs) issued by the IMF in 2021 to help countries navigate the adverse effects of the pandemic, Africa received $33 billion, or 4.5 percent, of the total available envelope. In addition, of the $17 trillion (or 19 percent of global GDP) rolled out as fiscal measures to fight the pandemic in 2020–21, Africa's share was only $89.5 billion (0.5 percent). And the same trends are observed in the scale and flows of the global climate finance architecture, which is misaligned with, for example, climate vulnerability and voluntary carbon market development.

- **Measures are needed to strengthen global, regional, and national institutions, as are subsidiarity agreements between the global and regional institutions, to increase responsiveness to increasingly complex development challenges in Africa and elsewhere in the developing world.** Multilateralism, including its development finance institutions, has over the decades transformed into multilayered forms of governance. Profound changes are symbolized by the growing role of regional development banks such as the AfDB, Asian Development Bank, Islamic Development Bank, Latin America Development Bank, and the Inter-American Development Bank. Most countries are members of these regional organizations, with some overlapping memberships. These banks can enhance multilateral efficiency by sharing burdens, exchanging information and best practice, building capacity, and increasing legitimacy through positive policy outcomes.

- **Specific recommendations for multilateral financial institutions to mobilize resources for Africa's structural transformation at scale include recycling SDRs through MDBs, implementing the MDB capital adequacy reforms, and reforming credit rating methods.** If implemented, the proposed reforms could greatly increase financing for Africa's structural transformation and move the continent to a higher level of economic development. Rechanneling SDRs through the MDBs could increase financing for Africa by about $46.2 billion a year over the next 10 years if the recommendations of the Bridgetown Initiative—to rechannel $100 billion to the MDBs—are implemented. Reforms of the MDB Capital Adequacy Framework proposed by the G20 could increase financing for Africa by another $5.2 billion a year. In addition, Africa could save up to $44 billion in

Given their membership structures, the multilateral development banks and financial institutions are best placed to lead global and regional efforts to mobilize and allocate resources at scale toward achievement of the Sustainable Development Goals in developing countries and to addressing global commons challenges

accumulated debt arrears if the IMF's lending into arrears policy is fully implemented. Africa could also save up to $74 billion a year in interest payments if the global credit ratings system were fairer and based on fundamentals. Collectively, these initiatives could secure $169.4 billion a year in development financing, or about 42 percent of the estimated annual financing gap of $402.2 billion to fast-track Africa's structural transformation.

Key recommendations for what countries need to do to address climate change and leverage the private sector for green transitions have already been highlighted in the AfDB's *African Economic Outlook 2022* and *2023*.[3] Key policies that can drive structural transformation in African countries, even with a changing GFA, are in chapter 2 of this report.

Simplifying procedures of the climate finance architecture will make it more accessible to climate-vulnerable countries that also have limited capacity to fulfill complicated and expensive project preparation procedures

- **However, implementing the following GFA reforms could unlock substantial capital for structural transformation in Africa, but they should not be considered a panacea.** The continent needs to also capitalize on domestic opportunities and positive elements already in the current GFA.

1. **Accelerate and scale up low-cost concessional financing for Africa's development,** through (i) rechanneling SDRs; (ii) making healthy replenishments of the concessional windows of the AfDB (the African Development Fund) and the World Bank (the International Development Association); (iii) reforming global tax governance to make it more transparent and inclusive; (iv) maximizing MDB funding capacity by implementing the G20's Capital Adequacy Framework and Triple Agenda; and (v) improving the scale of financing and transparency of bilateral creditors.

2. **Reform the global debt architecture to make it more transparent, nimble, accessible, and affordable to developing countries** through (i) devising market-based solutions to unsustainable eurobonds; (ii) providing debt relief to free resources for climate actions; (iii) considering proposals to create a sovereign debt authority and a sovereign insolvency system; (iv) having the G20 countries consider legislation that encourages private lenders to participate in debt workouts; (v) creating opportunities for MDBs to lend to countries during protracted debt negotiations by implementing the IMF policy of lending in arrears; (vi) providing further support to African capacity development in debt productivity and public financial management; (vii) improving the IMF–World Bank Debt Sustainability Framework (DSF) to make it adaptable to new economic realities; and (viii) reforming credit rating methods used by private agencies to improve credit ratings. State-contingent debt instruments can also help reshape Africa's public debt risks in a world beset by heightened macroeconomic uncertainty.

3. **Strengthen climate finance accessibility for vulnerable countries that need it most.** Simplifying procedures of the climate finance architecture will make it more accessible to climate-vulnerable countries that also have limited capacity to fulfill complicated and expensive project preparation procedures. Also needed is discouraging the use of debt as a climate finance instrument and the existing bias toward adaptation projects, which often increases the debt vulnerability of climate-vulnerable countries and deepens their economic vulnerability due to limited access to finance for climate adaptation. In addition, there is a need to scale up the resourcing of the Loss and Damage Fund, which was announced at COP27 in Egypt and has attracted about $661 million, to match the fiscal impacts of physical climate effects in countries.

4. **Adopt reforms to improve Africa's access to emergency financing facilities.** Lacking fiscal capacity, most African countries address temporary shocks by

borrowing to smooth their consumption and investment paths and avoid sharp economic fluctuations. With increased frequency of recurrent and sometimes overlapping endogenous and exogenous shocks, reforms of the GFA need to include actions to enhance Africa's access to financial safety nets—delinking access to IMF financing from quotas, introducing state contingent clauses in the loan agreements with the IFIs, and creating an African emergency finance facility/financial stability mechanism or institution. African countries should also implement reforms to strengthen and deepen their financial sectors so that eventually they become their own real cushion against shocks.

5. **Make the governance of the GFA—more inclusive to enhance Africa's participation and strengthen its voice.** GFA governance provides little voice to countries of the Global South[4], and particularly to Africa. Increasing Africa's participation and voice in the GFIs will increase the continent's ownership of decisions taken in these organizations, in line with its growing importance on the global stage. The realignment of the IMF quota-based allocation will make it fit-for-purpose and the IMF has already taken steps in this direction. Admitting more African countries as sovereign members of the G20 would enhance Africa's participation in global policy discourse and decisionmaking. For the longer term, African countries need to pursue growth-enhancing policies, which will increase the size of their economies and amplify their voice in the GFIs.

6. **Implement a mandatory requirement for countries to adopt policies for greening their GDP.** While natural assets deliver crucial global public goods —such as carbon sequestration, biodiversity conservation, and other ecosystem services—the value of these positive externalities is not fully factored in the measurement of countries' GDP. A mandatory requirement to reinforce methods of natural capital accounting will thus ensure proper valuation of natural capital and accounting for it in systems of national accounts. In this way, Africa and other natural resource–endowed regions can leverage their green wealth to improve their credit ratings and unlock resources for structural transformation.

7. **Leverage private sector financing for transformation.** The scale of public resources that can be mobilized through a scaling up of domestic revenue mobilization and concessional financing from official multilateral and bilateral creditors to support Africa's structural transformation to meet the SDGs and Agenda 2063 in the near term will be very modest relative to the scale of resources required, even in the best-case scenarios. The private sector offers significant opportunities to fill the resource gap. Measures to incentivize private finance in Africa are therefore critical for structural transformation in Africa. Reforms of the GFA could support asset recycling by transferring existing assets of debt distressed countries to the private sector to generate funding for infrastructure and other catalytic projects to accelerate structural transformation. Reforms could also embed mechanisms for a portfolio-based approach toward private sector investment rather than a project-by-project approach to leverage economies of scale and existing synergies of projects within the same portfolio than projects managed in silos can achieve.

A mandatory requirement to reinforce methods of natural capital accounting will ensure proper valuation of natural capital and accounting for it in systems of national accounts

INTRODUCTION

The current global financial architecture (GFA) embedded within the principles of multilateralism is a product of the idea for wider international cooperation, facilitated through the establishment

The increased leaning toward trade protectionism, friend-shoring, and regionalization of supply chains means that fragmentation of the global financial architecture is more likely than ever. This could forestall Africa from increasing its share of global trade

of institutions after the Second World War. Multilateral institutions and the wider GFA have undoubtedly contributed greatly to global development and to mitigating the impacts of adverse global economic events. Since the 1970s, institutions such as the World Bank, International Monetary Fund (IMF), and other development finance institutions have helped finance development in the developing world. They have supported countries during major global economic challenges, such as the Latin American Debt Crisis of the early 1980s, the African Debt Crisis of the 1980s and 1990s, the Asian Financial Crisis of the late 1990s, the Global Financial Crisis of 2007–09, and the recent COVID-19 pandemic in 2020–21, to name but a few.

Since the mid-1970s, there have been more than 2,200 episodes of economic and financial crisis, and global development finance institutions were critical in providing the much-needed countercyclical response to support economic recovery efforts in Africa and other developing regions by spearheading global response actions in times of crises. Recent examples include the Debt Service Suspension Initiative, the G20's Common Framework, and the IMF's general allocation of $650 billion-equivalent in Special Drawing Rights (SDRs) that helped ease the fiscal challenges countries faced in the pandemic.

However, such respites have often been episodic and therefore short-lived, and downside trends in economic fundamentals and risks often return in the medium term. Typical examples are Mexico's Tequila Crisis in 1994 and asset selloffs in 2013 after the Federal Reserve tightened monetary policy. The same scenario is playing out in the post-COVID-19 period. Thus, the recurrent cycles of booms and busts throughout history and the international Bretton Woods Institutions' responsiveness and effectiveness in addressing persistent "global commons" challenges such as climate change, conflict, and health pandemics beg fundamental questions. The current tightening of US monetary policy conditions and the appreciation of the dollar have only amplified the already dire consequences for emerging markets and developing economies. They are eroding access to international capital markets, increasing the cost of servicing maturing debt, heightening the risk of debt defaults, destabilizing currencies, depleting foreign exchange reserves as countries intervene to limit the rate of depreciation and volatility, and pushing price stability beyond the targets of central banks.

Further, the scale and scope of challenges today have morphed into regional, country, and community crises to levels at which these global institutions are ill equipped to address them promptly. Perhaps the collective capacity and effectiveness of multilateralism and the global financial institutions (GFIs) to sustainably address contemporary global shocks is best examined through the prism of (i) the changing nature of the global commons challenges the world faces—climate change, health pandemics; (ii) the changing nature of conflicts and geopolitical tensions, for example, the Russia-Ukraine conflict; and (iii) the interconnectedness of global value chains and economies in that economic policy management is externalized beyond national boundaries. National tools for policy management, such as domestic monetary policy to tackle inflation, are increasingly weakened by external shocks.

All these factors have huge implications for development in Africa and the rest of the developing world. Recent heightened global risks have deterred investment flows in, and trade with, emerging markets and developing economies. The increased leaning toward trade protectionism, friend-shoring, and regionalization of supply chains means that fragmentation of the GFA, as we now know it, is more likely than ever. This could forestall Africa from increasing its share of global trade from below the current 3 percent to that comparable with other regions. Equally, unless trade patterns recalibrate, intra-Africa trade —estimated at about 14 percent of total trade—could remain stifled. As in other regions, Africa established a regional trading bloc to scale up intraregional trade and has now ratified the African Continental Free Trade Agreement, which is set to foster deeper financial integration and trade, presenting a unique opportunity for regional production and financial value chains.

Yet multilateralism and the associated development finance institutions have also created inequalities. The market conditions, global challenges, and constraining factors for global economic growth, peace, and security today are not the same as they were post–World War II when the rules-based world order was created. All of the following have exposed limitations in the GFA's capacity which is now undergoing a stress test of historic proportions: persistent weak global growth and recurring economic and financial crises; growing global inequality (despite significant improvements in living conditions worldwide in recent decades); persistent human deprivation due to poverty, entrenched gender bias, hunger, conflict, and fragility; rising challenges to an open global trading regime; highly integrated and inadequately regulated financial markets which increase vulnerabilities to cross-border capital flows, and pervasive risks of pandemics, natural disasters, technological change such as artificial intelligence, climate change, and geopolitical tensions. All have resulted in slowly waning trust in multilateralism and the GFA. There is a growing consensus that more could be done to change course and achieve the ideals for which the GFIs were established about eight decades ago. Some even argue that we are on the cusp of an emerging GFA multipolarization which could translate into lasting divergence and fragmentation between advanced countries and developing economies.

The need for reforms is even more evident in Africa where an estimated 34 percent of the population still lives in extreme poverty, debt vulnerabilities are increasing,[5] the benefits of international trade remain below expectations, and the impacts of climate change, which the continent has not contributed to, are costing the continent 5–15 percent of GDP per capita growth annually. Climate change impacts are decimating lives and livelihoods across the continent while the promise of scaled-up climate finance remains a mirage. Further, around 85 percent of the continent's 1.4 billion people either live in or share land borders with a conflict-affected country, and key drivers of fragility—abject poverty, youth unemployment, and adverse climate change effects—are increasing across the continent.

Since the 1980s, emerging and developing countries, including those in Africa, have become more integrated into global financial markets and have reduced their almost exclusive reliance on multilateral banks, official bilateral creditors, and a handful of commercial banks for development financing. Against a backdrop of recurrent global and regional shocks, Africa's journey toward structural transformation demands heavy and well-thought-out investment in infrastructure, human capital, climate action, and productivity-enhancing technology to put the continent back on the path of higher and sustained growth.

Yet, the current GFA and system of multilateralism are not delivering adequate resources in a timely manner and at the scale needed to meet national and global development goals in Africa, including the Sustainable Development Goals (SDGs) and the African Union's Agenda 2063. Neither the public nor the private sector as constituted has been able to channel enough resources to address Africa's finance needs for accelerating structural transformation. The current system makes access to development finance expensive and very cumbersome for African and other developing economies. The high cost of sovereign borrowing by African countries relative to their peers in other regions has exacerbated debt vulnerabilities in countries already facing heightened risk of debt distress. Empirical evidence shows that in 2021, even after discounting for the risk related to COVID-19, African sovereign eurobonds were issued with yields above 5 percent and, in five countries, yields exceeded 8 percent. In contrast, the average sovereign bond yield for advanced economies was 1.1 percent and for emerging market economies, 4.9 percent.

The current global financial architecture and system of multilateralism are not delivering adequate resources in a timely manner and at the scale needed to meet national and global development goals in Africa, including the Sustainable Development Goals and the African Union's Agenda 2063

Multilateral and development finance institutions have over the decades transformed into a multilayered form of governance, with national, regional, interregional, and global levels of authority. Profound changes are symbolized by the growing role of regional development banks such as the African Development Bank (AfDB), Asian Development Bank, Islamic Development Bank, Inter-American Development Bank, and Latin America Development Bank. Most countries are members of these regional organizations, with some overlapping memberships. These regional organizations may enhance multilateral efficiency by sharing burdens, exchanging information and best practice, building capacity, and increasing legitimacy through positive policy outcomes. Still, measures are needed to strengthen these regional and national institutions, and to craft subsidiarity agreements between the global and regional institutions for responsiveness to increasingly complex challenges in Africa and the developing world relating to sustainable development and the global commons.

The rules and operational processes of international development finance institutions need to be redefined, to make them more nimble, effective, and efficient in responding to current global commons challenges. They need to be more inclusive of the diverse states and institutions that have emerged since their creation. Reform of the GFA is urgently needed to manage many imbalances and inequities in the world today, from trade imbalances to unequal access to capital; climate and energy injustice; and the growing bifurcation in the global financial systems. Also needed are a more effective and nimble debt resolution mechanism; prudent and transparent assessment of sovereign risk, based on a more inclusive methodology that can deliver low-cost, long-term, concessional development financing; and a system that fosters greater participation of countries in decision-making in global development finance institutions.

The rules and operational processes of international development finance institutions need to be redefined, to make them more nimble, effective, and efficient in responding to current global commons challenges

LIMITED ACCESS TO AFFORDABLE FINANCING CONSTITUTES A CONSTRAINT TO FAST-TRACKING AFRICA'S STRUCTURAL TRANSFORMATION

Africa emerged from the COVID-19 pandemic relatively strong, but halfway through to the end date of the United Nations Agenda 2030 on Sustainable Development Goals (SDGs), and mid-way through the implementation of Agenda 2063 of the African Union, reaching these targets appears extremely unlikely. The quantum and scale of resources are low, undermining efforts to end poverty and make the necessary investments to achieve structural transformation. The United Nations and the AfDB estimate that approximately $1.3 trillion will be required annually to meet Africa's sustainable development needs by 2030; and $234.5 billion–$250 billion to finance climate actions.[6]

While much of the investment will have to be financed by Africans themselves, there is also a pressing need for increased external financing, from public and private sources. For instance, in 2022, external financial flows—including foreign direct investment, official development assistance (ODA), remittances, and net portfolio investments—to Africa were only $174.9 billion, a 19.4 percent decline from the $217.1 billion in 2021. Further, due to misalignment and donor-centered climate finance architecture, Africa's share of global climate finance remains marginal, despite being a continent extremely vulnerable to the effects of climate change. Out of the $652.6 billion of global climate finance mobilized in 2019/20, Africa received only $29.5 billion (4.5 percent), 86 percent from public sources and 14 percent from private sources. In comparison, East Asia and the Pacific mobilized $293 billion, about 10 times as much as Africa, Western Europe some 3.5 times as much ($105 billion), and North America close to 3 times as much ($85 billion).[7]

Access to emergency financing is also largely skewed toward developed economies that need it the least. Of the $650 billion in SDRs issued by the IMF in 2021, Africa received just $33 billion (4.5 percent), an allocation inconsistent with the continent's development priorities and its underlying existing and new challenges. And of the $17 trillion (or 19 percent of global GDP) as total fiscal measures to fight the COVID-19 pandemic in 2020–21, Africa accounted for just $89.5 billion (0.5 percent) of the global figure. The response by developed countries to the plight of Ukraine also highlights the asymmetrical treatment of risks and development needs. As of February 29, 2024, the Kiel Institute for the World Economy reported total bilateral commitments and European Union (EU) assistance of about $362.8 billion—of which $181.8 billion were already allocated—for Ukraine from more than 41 countries, mostly advanced economies.[8]

The scale of resources to support Africa's structural transformation implies a radically reformed and strengthened GFA that is nimble and fit for purpose to mobilize resources at scale and on affordable terms. International calls for reforms present an opportunity for Africa to ensure that the reformed GFA is responsive to its needs. The continent has been engaging with international financial institutions (IFIs) and bilateral partners for decades and, despite the shifting composition of public debt toward private creditors, multilateral borrowing has remained relatively stable since 2000, accounting for 34 percent of total external debt in 2022 (figure 3.1).

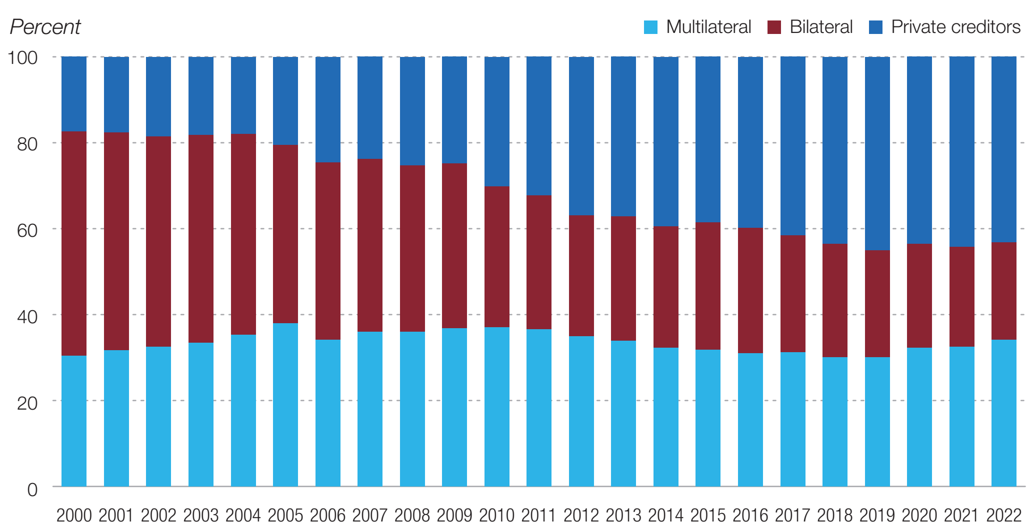
Among multilateral creditors, the World Bank—the International Development Association (IDA) and International Bank for Reconstruction and Development (IBRD)—was the top creditor. Africa's debt to the World Bank's IDA and IBRD combined was about 55 percent in 2022, down from 62 percent in 2000. The share of debt held by the AfDB in total multilateral debt remained relatively stable from 2000, from 22.5 percent to 19 percent at the end of 2022, and averaging 22.9 percent over the last 10 years. This share is expected to rise based on innovative instruments to raise capital to support the AfDB's operations as outlined in its Ten-Year Strategy 2024–2033. The European Investment Bank, Islamic Development Bank, and Arab Fund for Economic and Social development contributed 5 percent, 4 percent, and 3 percent of total multilateral debt to Africa in 2022, respectively. Other multilateral creditors accounted for 11 percent in 2022, up from 4 percent in 2000 (figure 3.2a).[9]

Among bilateral creditors, there has been a growing shift toward China in the last two decades. When broken down by bilateral creditors, which accounted for 23 percent of Africa's total outstanding external debt stock in 2022, the top creditors were China (42 percent), France (10 percent), Saudi Arabia (7.9 percent), Kuwait (6.4 percent), Germany (6.4 percent), and Japan (5.7 percent), with other creditors at 21 percent (figure 3.2b). From a historical perspective, there has been a growing shift from traditional Paris-club lenders to non-Paris club lenders, notably China. The scale of non-Paris club lending has increased for this group of countries, but with opacity and a lack of transparency, the precise sizes and terms of loans are unclear.

The existing incentives for MDBs and other public financial institutions often lead to suboptimal coordination between public and private sector resources in financing development projects in developing countries, especially in Africa. There is broad consensus that the bulk of financing for the SDGs, climate action, and delivery of other global and regional public goods must come from the private sector. The private sector is awash with capital—the private credit market topped $2.1 trillion globally in 2023 in assets and committed capital looking for productive and profitable investments).[10] Yet African countries face an uphill task in mobilizing these resources to finance their development agendas, or to deliver on their commitments to address the global commons

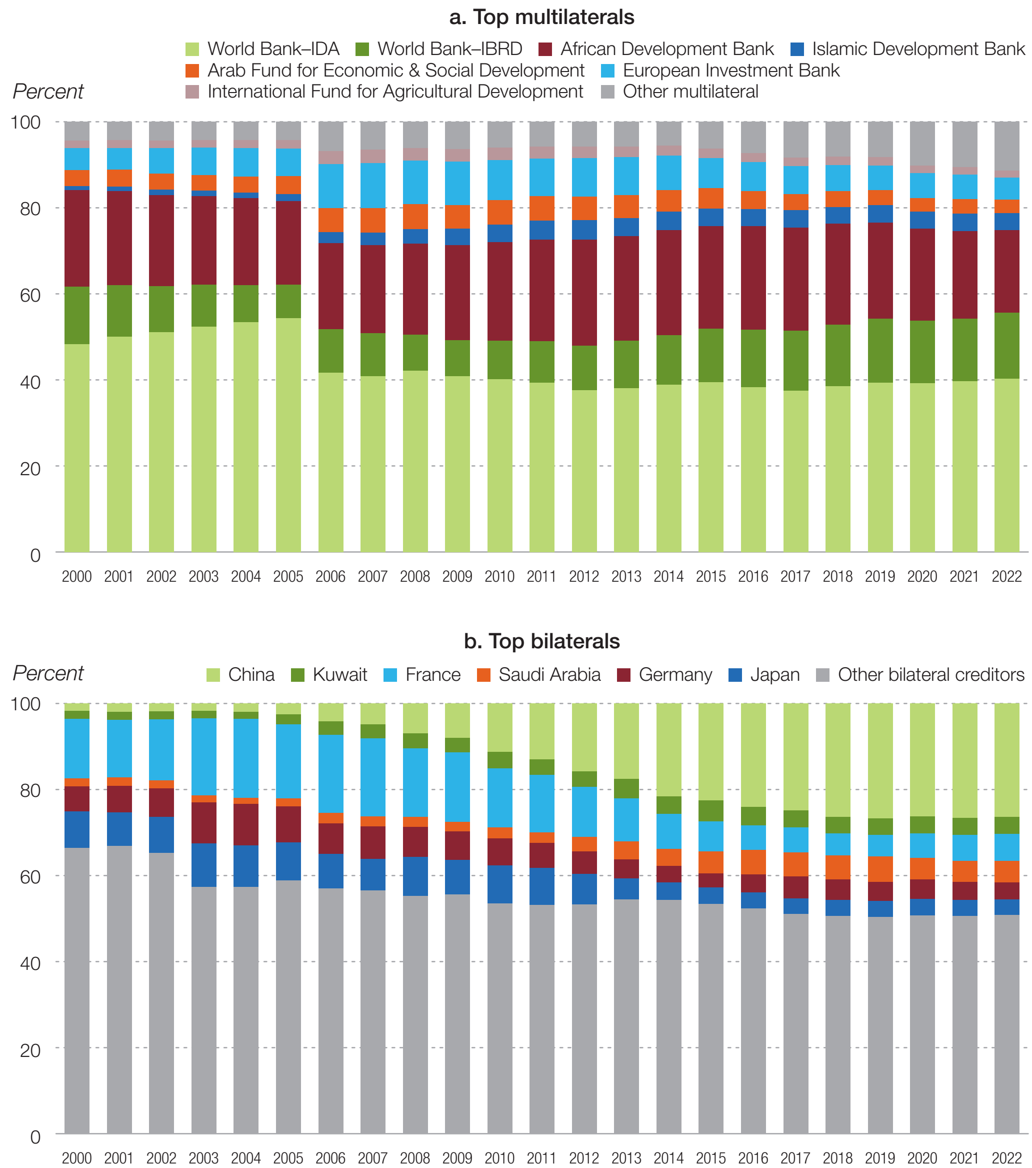
The continent has been engaging with international financial institutions and bilateral partners for decades and, despite the shifting composition of public debt toward private creditors, multilateral borrowing has remained relatively stable since 2000

FIGURE 3.1 Disbursed external debt by creditor types, 2000–22



Source: Staff calculations based on World Bank International Debt Statistics.

FIGURE 3.2 Top creditors to African economies, 2000–22



Source: Staff calculations based on World Bank International Debt Statistics.

Africa's debt to the World Bank's International Development Association and International Bank for Reconstruction and Development combined was about 55 percent in 2022, down from 62 percent in 2000

challenges that provide regional and global public goods. For instance, between 2011 and 2020, financing through debt instruments averaged about two-thirds of all climate finance channeled to Africa by developed countries, and about one-third of projects financed through debt have been on non-concessional terms.

So, there is a need therefore for greater alignment between public and private sector financing models, standards, practices, and instruments to achieve greater leverage in driving national and regional development agendas. The *African Economic Outlook 2023* established that the leverage ratio between public and private sector climate finance in African countries was 0.16 on average.[11] The same scenario is observed on a global scale regarding the delivery of global public goods.

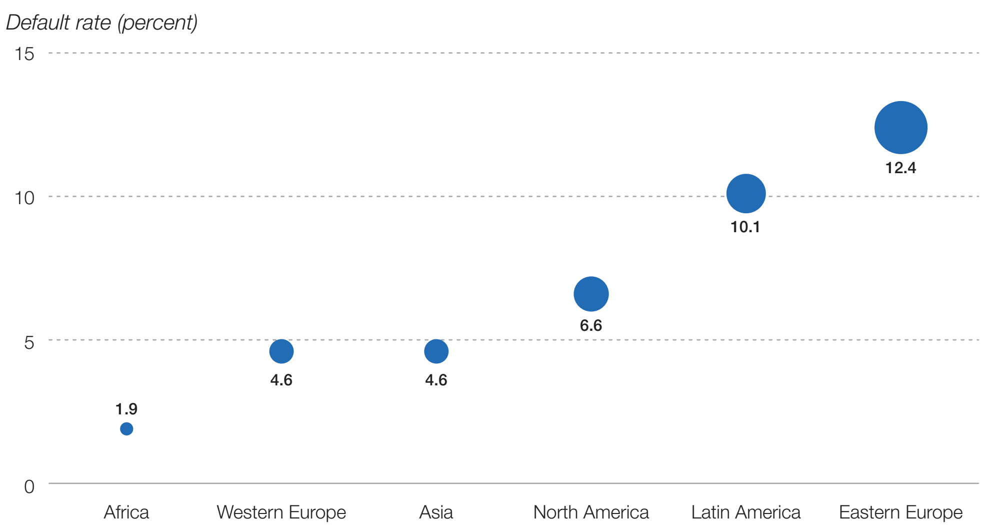
Through the Glasgow Financial Alliance for Net Zero, corporate actors have demonstrated a global commitment to net zero. But to leverage this commitment for climate action, the mandates, governance structures, operating models, and financial firepower of MDBs and other public finance institutions need to be augmented and strengthened to better align with the scale of financing, speed, and modalities of delivery. MDBs need to be more prevalent in risk mitigation projects, and to define the types of risks to be mitigated with public resources, so as to address growing concerns that public resources might be deployed to socialize risks and privatize gains. This risk-based model of deploying climate finance has resulted in low climate-finance inflows and a high cost of capital more generally to Africa, which dwarfs investments in transformational sectors such as renewable energy. In addition, the high-risk premium paid by African countries due to a high-risk perception by global public investors increases the cost of private climate finance to African countries, despite the evidence that investments in Africa are not as risky as often seen.

Most African countries are rated below investment grade by external rating agencies (S&P, Moody's, and Fitch), but these ratings are often based on subjective assessments due, in part, to asymmetric information about African market conditions.[12] Thus, contrary to risk perceptions driven by the sovereign ratings of African countries, estimates show that Africa has the lowest risk of default on infrastructure among its peers —the other main regions—as shown by a 2020 study by Moody's Analytics covering more than 8,000 project loans from consortium members originated in 1983–2018. Africa had the lowest default rate at just 1.9 percent, versus that in Eastern Europe (12.4 percent), Latin America (10.1 percent), North America (6.6 percent), Asia (4.6 percent), and Western Europe (4.6 percent) (figure 3.3).[13]

Reforms of the GFA should therefore not only target the MDBs but also extend to bilateral and private sector creditors. Some of the commercial lenders are aligned with bilateral creditors, but with the terms that have entangled borrowing African countries into unsustainable debt. The reforms would therefore be more beneficial to Africa if they help to (i) mobilize more low-cost financial resources for structural transformation, through a reallocation of SDRs and reforms of the MDBs that allow for increased access to concessional financing; (ii) create a platform for information sharing on the terms of loans, through a mutually agreed mechanism/platform that encourages voluntary disclosure to foster transparency and accountability among creditors; (iii) provide quick and less onerous resolutions for unsustainable debt and avoid more future debt problems; (iv) reconfigure the global climate finance architecture to ensure the mobilization of adequate and affordable financing for climate action, including honoring commitment by advanced economies to disburse $100 billion to developing countries, the significant

Contrary to risk perceptions driven by the sovereign ratings of African countries, estimates show that Africa has the lowest risk of default on infrastructure among its peers

FIGURE 3.3 **Default rates on infrastructure and other projects lowest in Africa**



Source: Staff calculations based on Moody's Analytics, 2020.

share of which should accrue to Africa; (v) improve access to emergency financing to deal with exogenous shocks; and (vi) democratize the governance of IFIs for more inclusive decisionmaking on how resources are allocated and ensure that terms for Africa, as their major client, are aligned with the continent's needs for structural transformation and broader development agenda.

GROWING CONSENSUS ON THE NEED TO REFORM THE GFA

Huge changes in the GFA…

The world has changed in three important ways that have challenged the ability of the GFA to handle emerging global and regional dynamics. First, the share of the Global South in the world's GDP has more than doubled over the last three decades, rising from 16 percent in 1991 to 37 percent in 2021, and its share of the world's population concurrently rose by 5 percentage points. For Africa in particular, the share of its GDP in the world economy increased from 1.9 percent in 2002 to 2.9 percent in 2022, and its population from 12 percent of the world total in 1990 to 18 percent in 2022. Africa's participation in decisionmaking and in GFA governance needs to reflect these dynamics for a fairer distribution of power and influence.

Against a backdrop of change, one constant is that Africa's sovereigns face high costs of financing in the international capital market relative to advanced countries and emerging economies, due to mispricing of their sovereign debt by international investors presumably originating from unfavorable credit ratings by global rating agencies

Second, new non-state actors—including regional organizations, civil society groups, the private sector and philanthropic bodies—are increasingly important in the world economy and in the provision of important global public goods and services and financing for development, including in Africa. Two-thirds of private philanthropic resources for sustainable development globally in 2018–20 targeted African countries,[14] averaging $2.9 billion a year during the period, followed by developing countries in Asia ($1.4 billion), and Latin America and the Caribbean ($0.4 billion). These resources are targeted mainly at critical areas of Africa's development, including health and climate actions, the green transition, and gender and youth empowerment.

Third, the investment needed to deliver on global public goods—especially climate and pandemic preparedness—as well as on the SDGs is huge, and the current system has been unable to mobilize stable and long-term financing at scale for the continent and for other developing regions. The world therefore needs a GFA that can support development of innovative financing mechanisms and can mobilize resources at scale and affordable cost.

… with some constants

Against this backdrop of change, one constant is that Africa's sovereigns face high costs of financing in the international capital market relative to advanced countries and emerging economies, due to mispricing of their sovereign debt by international investors presumably originating from unfavorable credit ratings by global rating agencies. As shown in Chapter 1, African sovereign eurobonds in 2021 were issued at yields significantly higher than those on comparable instruments in advanced and emerging economies in other regions of the world. As a result, many governments dedicate a high share of revenue to debt service payment while being unable to sufficiently invest in the delivery of fundamental rights in health, education and social protection.

Moreover, debt restructuring mechanisms, including that under the G20's Common Framework, are facing lengthy delays, thereby putting pressure on public finances and creating liquidity challenges for countries in debt distress. While progress has been made recently with the faster debt treatment for Ghana under the Common Framework than with Zambia previously and other earlier applicants to the Common Framework, more needs to be done to ensure its future credibility. Thus, the GFA needs to be reformed to empower Africa with stronger voice and to allow equitable access to emergency financing, debt resolution mechanisms, and sustainable development financing, including for climate action, while ensuring Africa's meaningful participation in resource allocation decisions.

Sources of the calls for change

Repeated calls for reforming the GFA have come from the UN, the Bridgetown Initiative, and the G20, as well as from many experts and academic writers. On the UN's 75th anniversary in 2020, the General Assembly adopted a resolution stating that global challenges can only be addressed by global responses, through reinvigorated multilateralism.[15] In 2021, the UN Secretary-General presented *Our Common Agenda,* which outlines the global response to global problems.[16] It stresses the need to re-embrace global solidarity and strengthen the multilateral system, including the GFA, to make it more inclusive and reflective of the world of the 21st century. It was followed by a series of high-level evidence-based policy engagements in preparation for the Summit of the Future.[17]

The UN argues that the existing GFA financial architecture has failed to mobilize the stable and long-term financing needed to combat the climate crisis and achieve the SDGs. According to the UN, this architecture is plagued with inequities, gaps, and inefficiencies, including disproportionate allocation of emergency funds to developing countries, even where these may already exist, as was evidenced during COVID-19 pandemic and food price hikes; higher borrowing costs for developing countries even after adjusting for risk; underinvestment in global public goods, particularly climate action and pandemic preparedness; volatile capital markets with repeated global financial crises; and an international tax architecture that leads to global tax evasion and avoidance. In response, the UN recommends reforms in six areas: global economic governance; debt relief and the cost of foreign borrowing; international public finance; global financial safety nets; policy and regulatory frameworks for capital markets; and the global tax architecture.[18]

The G20 has been a strong advocate for reforming the GFA. A 2018 report by an Eminent Persons Group on Global Financial Governance, commissioned by the G20, recommended reforms of the GFA and governance of IFIs to promote economic stability and sustainable growth.[19] The report underlined the importance of ensuring that the IFIs contribute to growth and development in Africa. It stated that: "to bend the arc of history we must succeed in Africa, where the poverty, demographic and environmental challenges are the largest—and so too are the opportunities to contribute to world growth and the global commons." This declaration is a stark recognition of the inadequacy of the global financial system to adequately address challenges facing Africa but it also reflects a strong realization of the immense opportunities that the continent presents to the world, and that progress in Africa will directly translate into success for the world.

The report was followed by the Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks.[20] It argued that the world is facing turbulent times with a challenging combination of short-term crises and longer-term development requirements, straining the international community's capacity. It underlined the need to maximize MDB funding capacity through optimizing their balance sheet use and recommended strategic shifts in five areas: definition of risk tolerance; use of callable capital; expanded use of financial innovations; improved credit rating agency assessment of MDB financial strength; and increased access to MDB data and analysis. In July 2023, the G20 issued a Roadmap for the Implementation of the CAF Report, which described progress in implementing the CAF recommendations and suggested some additional actions to achieve the CAF report's objectives.[21]

Repeated calls for reforming the global financial architecture have come from the United Nations, the Bridgetown Initiative, and the Group of 20, as well as from many experts and academic writers

In 2023, the G20 proposed The Triple Agenda, which recommended a three-pronged approach to reform the MDBs: (i) adopting a triple mandate of eliminating extreme poverty, boosting shared prosperity, and contributing to global public goods; (ii) tripling MDBs' sustainable lending levels by 2030; and (iii) creating a third funding mechanism that would permit flexible and innovative arrangements for engaging with private investors interested in supporting parts of the MDB agenda.[22] The report argues that implementing all the proposals in the CAF report "will fall substantially short of what is needed." It therefore recommends a generalized capital increase (GCI) for those institutions facing a binding headroom constraint.

The report also argues that "new equity in MDBs would provide extraordinary value-for-money to shareholders." According to the report, "each dollar of new equity could reasonably be expected to support at least $15 of additional external financing for sustainable investments: $7 in direct MDB lending and $8 in additional direct and indirect mobilization of external private capital."[23] The MDB role to provide financial assistance and reform the architecture was buttressed by a unified proposal in the Heads of MDBs Viewpoint Note during the IMF and World Bank 2024 Spring Meetings, which reaffirmed their collective determination to deliver on commitments and strengthen collaboration to support sustainable development using innovative instruments.

Over the past decade, the AfDB has also undertaken several pioneering initiatives on scaling up its balance sheet to expand lending headroom to its regional member countries (box 3.1).

The call for reforming the multilateral financial system transcends the UN and the G20. African leaders and heads of regional organizations, including the AfDB, have highlighted the inability of the current system to meet the needs of the Global South in general and Africa in particular. The latest call championed by the President of the Republic of Kenya in 2023 at the 28th Conference of Parties (COP28) on reforming the GFA has added impetus to voices of the African Union and other regional leaders.[24] The aim is to make Africa an equal partner in access to international financial resources to support the attainment of the SDGs and to address climate change challenges.

This call was underscored by 19 African leaders during the World Bank's IDA–21 replenishment meeting held on March 29, 2024 where they reinforced the call for $120 billion replenishment and reforms to support Africa's transformation agenda.[25] Outside policy circles, there is also increasing recognition of and evidence on the failure of the GFA and the need for change.[26] Notably, there is near unanimity on the inequities in access to development and emergency financing, as was evident during the COVID-19 pandemic when developing countries had limited access to vaccines.

The Bridgetown Initiative, led by the Prime Minister of Barbados, an advocate of reforms to the GFA, has identified several ways to accelerate progress toward the SDGs and the Paris Agreement.[27] Priority actions under this initiative include

BOX 3.1 Financial innovation initiatives led by the African Development Bank Group

Since 2015, the African Development Bank has developed several pioneering financial innovations to scale and bolster its support to Africa's transformation in the face of evolving global economic and development finance environments. These innovations are in line with the recommendations from the G20 Independent Review of MDBs' Capital Adequacy Frameworks to scale up MDB financing. While the G20 Independent Review recommendations were published in 2022, the African Development Bank had already been at the forefront of balance sheet optimization through the innovative use of risk transfer products.

In 2015, it became the first MDB to launch its own captive risk participation vehicle: the Private Sector Credit Enhancement Window. It was also among the first MDBs to ideate and launch the Exposure Exchange Framework Agreement, under which it has executed over $10 billion in risk transfers. In 2018, it became the first MDB to undertake a synthetic securitization transaction on its private sector portfolio and in 2022, following the debilitating impact of COVID-19 pandemic, it launched another pioneering risk transfer transaction with the support of the United Kingdom, partially transferring the risk on $2 billion in sovereign loan assets to private insurers and the United Kingdom. This risk transfer enabled the AfDB to release an estimated $2 billion from its balance sheet to finance climate investments. In January 2024, it launched a $750 million sustainable hybrid capital transaction, the first of its kind by an MDB. This instrument increases its lending capacity by $2.2 billion to $3 billion and establishes a new asset class for investors as well as a new funding tool that will help strengthen MDBs' lending capacity for the foreseeable future.

In total, the African Development Bank has unlocked more than $13 billion in additional lending capacity to date. Further, having stretched its balance sheet over the past decade, it is exploring means to deploy these innovative techniques on transactions at origination in risk-sharing initiatives under its guarantees business model. The recent environment, social, and governance (ESG)–labeled partial credit guarantees to mobilize private capital to sovereigns such as Benin, Côte d'Ivoire, and Egypt were achieved through risk-sharing partnerships with the insurance market to grow the AfDB's headroom to maximum impact and to help improve the debt situation in borrowing countries. Over the lifetime of its new Ten-Year Strategy, the AfDB will continue to explore opportunities to deploy innovative financial instruments to further optimize its balance sheet and increase lending capacity by collaborating more with peer institutions.

providing immediate liquidity support through the rechanneling of $100 billion of SDRs, suspending IMF surcharges, and restoring enhanced access limits established during pandemics for the Rapid Credit Facility; restoring debt sustainability by redesigning the Common Framework, encouraging the restructuring of private debt, and adopting natural disaster clauses in all lending instruments; mobilizing private sector investment to over $1.5 trillion a year for green and just transformations; increasing official development lending for SDGs to $500 billion a year; ensuring that the multilateral trading system supports green and just transformations; and reforming the governance and operations of IFIs to be more inclusive and equitable.

The remainder of this chapter will not attempt to analyze all the reforms proposed by the UN, G20, Bridgetown Initiative, AfDB, or other players. Instead, it will focus on recommendations most important for Africa's structural transformation and suggest how they could be implemented—actions that increase financing for development and the climate, resolve debt problems, expand the global safety net, and enhance Africa's participation in the governance of and decisionmaking in the GFA. The objective is to inform the debate in Africa and to provide analysis that can be used by African leaders to determine their priorities and inform their future discussions and negotiations with international partners.

MOBILIZING ADDITIONAL RESOURCES FOR AFRICA'S STRUCTURAL TRANSFORMATION

Africa's plans for structural transformation, presented in detail in the African Union's Agenda 2063, entail an increase in total factor productivity through two channels: technological improvements and physical and human capital investments to raise within-sector productivity (that is, to increase agricultural yields); and a shift of productive resources from sectors of low productivity to high productivity.

Chapter 2 provides a granular analysis on the evolution and gaps of structural transformation in Africa. Achieving progress requires policy and regulatory reforms to encourage innovation and entrepreneurship, as well as major investments in soft and hard infrastructure, human capital, and technology. To succeed in its structural transformation, reach the SDGs, and attain the milestones in Agenda 2063, Africa needs investments in the trillions of dollars a year. In addition to the $1.3 trillion in SDG financing, the AfDB estimates that financing the four key pillars in fast-tracking structural transformation alone will require filling a financing gap of $402.2 billion. This investment will have to be financed through domestic and external resources, private and public.

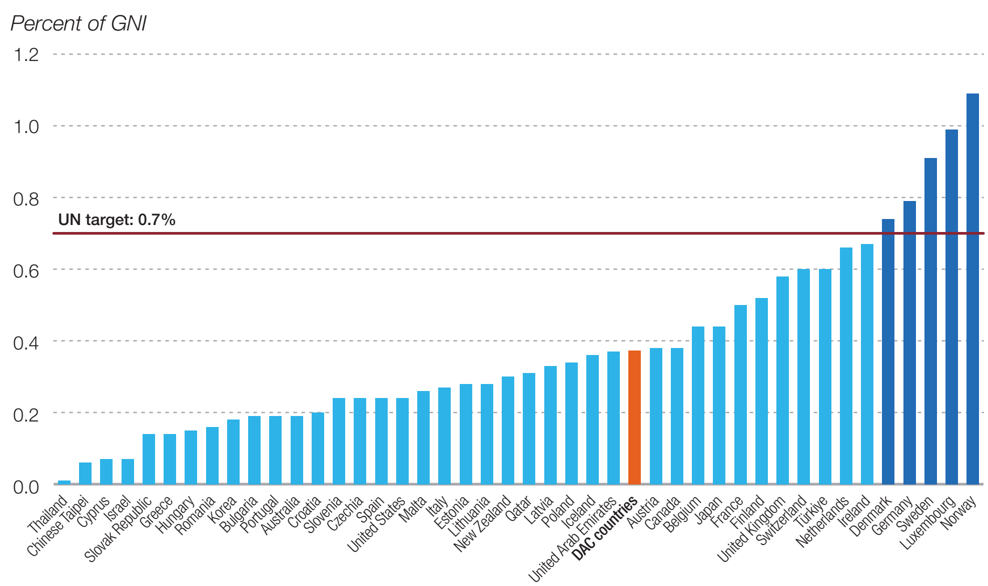
Domestic resources have been and will remain Africa's main source of development financing. However, given the enormity of the financing gap, reforms of the GFA should support increased external flows to finance Africa's economic transformation. Financial flows including ODA, foreign direct investment, portfolio flows, and remittances to Africa have been erratic, and it is unlikely that traditional ODA to Africa will increase in the short term because donor countries are facing many competing priorities (chapter 1). Moreover, as at end-2023, only a few advanced countries met the ODA threshold of 0.7 percent of gross national income (GNI). The average for members of the Development Assistance Committee (DAC) of the Organisation for Economic Co-operation and Development (OECD) was about 0.4 percent, and a majority of countries fell below the mean (figure 3.4). In the short run, the best hope for increasing ODA to Africa is to recycle SDRs and implement CAF reforms by the MDBs, coupled with an MDB GCI.

In the short run, the best hope for increasing official development assistance to Africa is to recycle Special Drawing Rights and implement Capital Adequacy Framework reforms by the multilateral development banks (MDBs), coupled with an MDB generalized capital increase

Recycling SDRs

The G20 has called for recycling $100 billion-equivalent of SDRs to developing countries through the MDBs. This follows the IMF's largest allocation of $650 billion (or SDR 456.5 billion) into the world economy in 2021 to help countries deal with the economic fallout from COVID-19. Countries' SDR allocation was in proportion to their IMF quotas. Thus, according to Georgieva et al. (2023) rich countries, who already had enough reserves, received $350 billion of additional liquidity that they did not need and therefore they sit "dormant."

FIGURE 3.4 **Official development assistance, by members of the Development Assistance Committee, 2023**



Note: Dark blue bars represent providers that met or exceeded the UN target of 0.7 percent ODA/GNI in 2023. ODA is on a grant-equivalent measure by members of the OECD Development Assistance Committee (DAC) as a percent of gross national income (GNI).

Source: OECD International Development Statistics database (2024), flows by donor.

The proposed framework developed by the African Development Bank with the Inter-American Development Bank on rechanneling Special Drawing Rights shows that the reallocation can be leveraged three or four times

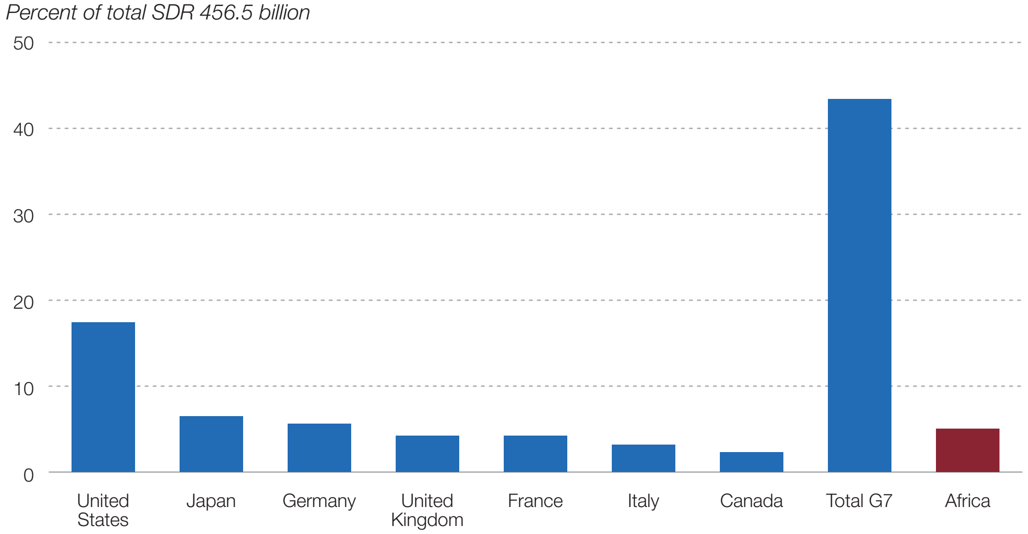
The G7 member countries' allocation of SDRs in August 2021 was 43 percent of the total of 456.5 SDR billion, while the allocation for all of Africa was 5 percent (figure 3.5).[28]

The AfDB has been at the forefront with a proposed framework on how to better optimize the use of the SDR reallocation. The framework that it developed, with the Inter-American Development Bank on rechanneling SDRs, shows that the reallocation can be leveraged three or four times. Thus a $5 billion in SDRs rechanneled through the AfDB could deliver up to $20 billion of new financing for African countries.[29] Most MDB shareholders with strong SDR positions willing to channel their SDRs to MDBs are required by the IMF to maintain the Reserve Asset Status of pledged SDRs, while minimizing their budget cost. This means that countries lending their SDRs should still be able to account for these onlent SDRs as reserves.

An initial recycling of SDRs has occurred through the IMF and was used to finance the Poverty Reduction and Growth Trust (PRGT) and the Resilience and Sustainability Trust (RST). By end-2023, the PRGT received $46 billion from 23 contributing countries and the RST $41 billion from 18 contributing countries. Generally, expanding the recycling window to include the MDBs would serve the interests of shareholders and other stakeholders interested in Africa's development.

The IMF Executive Board authorized on 10 May 2024 the use of SDRs by IMF members for the acquisition of hybrid capital instruments (financial instruments with perpetual maturity that has both equity and debt properties) issued by prescribed holders (official entities approved by the IMF to hold SDRs) subject to a cumulative limit of SDR 15 billion. The expectation is that IMF members channeling the SDRs to prescribed holders under such capital contributions would have Voluntary Trading Arrangements (VTAs) in place to help ensure sufficient liquidity and an equitable distribution of potential SDR exchanges into currencies in the VTA market.[30] This is a positive development. Increasing the cumulative limit to SDR 100 billion as recommended by the Bridgetown Initiative would help the initiative to achieve transformational impact.

FIGURE 3.5 SDR allocation in August 2021



Source: IMF 2021.

The reallocation would present four main benefits. First, the MDBs can leverage their capital so that one dollar of recycled SDRs could generate direct MDB financing of \$4–\$7, something that neither the PRGT nor the RST can do. Second, the MDB finance projects have direct impacts on the SDGs, and so directly improve people's livelihoods, while the PRGT and RST provide general balance-of-payments support within the context of an IMF program with specific conditionality. Third, the MDBs conduct maturity transformation while the IMF typically provides shorter-term lending. Finally, MDBs have a wealth of knowledge and experience in partnering with clients to achieve effective development solutions, and they combine affordable long-term finance, technical support, and policy dialogue and advisory services in a unique way to deliver impactful and sustainable results.

In an increasingly fractured world, MDBs have a history of strong convening power, bringing together diverse nations not just to discuss but to act in support of a shared agenda of transformative growth. They have a strong financial track record, which allows them to borrow on very attractive terms, and so can borrow large medium- and long-term resources from bond investors at affordable financial rates, whose benefits can then be passed on to Africa's low-income countries. And by internalizing the risk that would otherwise be borne by their clients in international financial markets, MDBs facilitate investment in critical areas of infrastructure and investment in human capital and skills development, which would be difficult otherwise given the high cost of capital.

How then would recycling \$100 billion-worth of SDRs as hybrid capital with the MDBs impact Africa? Using the assumption in the Triple Agenda of the G20 with a leveraging ratio of seven for direct lending and eight for indirect private financing, financing for Africa would increase by about \$46 billion a year over the next 10 years (box 3.2). Under the much more conservative assumption of a leveraging ratio of four used by the AfDB, financing to Africa would increase by about \$12 billion a year over the next 10 years. This figure is far higher than the \$8.9 billion pledged for the AfDB's three-year replenishment cycle for ADF-16 (African Development Fund).

To bridge Africa's climate finance gap, the ADF launched a *Climate Action Window* (CAW) during its 16th replenishment cycle, with an initial envelope of \$429 million, 75 percent of which was allocated for adaptation, 15 percent for mitigation, and 10 percent for technical assistance. The CAW enjoys a comparative advantage as an ADF instrument. Among others, the Fund has financed

Using the assumption in the Triple Agenda of the G20 with a leveraging ratio of seven for direct lending and eight for indirect private financing, recycling \$100 billion-worth of Special Drawing Rights as hybrid capital with the multilateral development banks would increase financing for Africa by about \$46 billion a year over the next 10 years

BOX 3.2 Assumptions and potential financial savings from leveraging SDR recycling

Assuming the $100 billion of SDRs would be distributed to the MDBs in proportion to their capital, the AfDB would receive $23 billion of additional hybrid capital which, using the figures from the Triple Agenda report of the G20, would generate seven times as much direct financing, $161 billion, and eight times as much indirect financing through the private sector, $184 billion, for a total of $345 billion. The World Bank would receive $39 billion of additional hybrid capital. Using the same 1:15 ratio used in the G20 report, that would generate $585 billion of additional financing. This leverage ratio is higher than the Bank's proposal of 1:3 at the lower end or the upper bound of 1:4, which makes it highly conservative.

Leveraging the G20 ratio would mainly impact IBRD financing for middle-income countries in Africa. Hence, Africa's share of IBRD lending is around 20 percent, which goes mainly to North Africa and to Southern Africa. This would imply an additional $117 billion of financing going to Africa.

Thus, under the high leverage scenario in the G20 report, a rechanneling of $100 billion worth of SDRs through the MDBs could produce a total additional financing, direct and indirect, of $462 billion from both the AfDB and the IBRD. This figure is the total stock of financing generated by rechanneling the SDRs. It would not usually be lent out in one year. Assuming that it is lent out over 10 years, the annual increase in financing for Africa would be $46.2 billion.

Under a more conservative scenario where one dollar of MDB capital only produces four dollars of additional financing, the total additional financing for Africa would be $123 billion—$92 billion from AfDB and $31 billion from IBRD, or an annual increase of $12.3 billion over 10 years.

Source: Staff calculations based on leverage ratios derived from proposed rechanneling of SDR.

the Lake Victoria Water and Sanitation Initiative in East Africa, enhancing access to clean water and sanitation while promoting long-term sustainability against climate change impacts. Leveraging initial financing of the CAW with additional resources from both public and private sources will bolster the flow of climate finance to address climate vulnerability and risk in Africa.

Implementing CAF reforms and adopting a GCI for MDBs

Additional financing for Africa would also come from implementing the CAF reforms and through a GCI for all MDBs, as well as higher replenishments for the World Bank's IDA and the AfDB's ADF. According to the G20's Roadmap report, CAF reforms under implementation would increase AfDB's lending capacity by $42 billion and IBRD's lending capacity by $51 billion, with 20 percent or about $10 billion going to Africa. That is, total additional lending to Africa would increase by $52 billion or $5.2 billion a year over the next 10 years.

MDBs are committed to implementing the CAF reforms, but that would not be sufficient to guarantee the provision of long-term and affordable development financing, especially with the enormous financing gap that must be closed to fast-track structural transformation in Africa. As stated in the G20's Triple Agenda report, there is a need for a GCI for all MDBs—particularly the AfDB—as well as significant replenishments of their concessional financing arms—IDA and ADF. Bank estimates of financing gap show that ADF countries will need about $245 billion a year for investment in the four key pillars to accelerate structural transformation over the three-year ADF-17 replenishment cycle.[31] Implementing these reforms would be critical for the MDBs and other GFIs to have the financial capacity to address the complex and growing sustainable development and global commons challenges in African and other developing countries.

During the recent IDA Replenishment meeting of the World Bank Group, His excellency Dr. William Ruto, President of the Republic of Kenya, called for the replenishment of the ADF with up to $25 billion during its forthcoming 17th replenishment cycle. Given the huge scale of financing gap estimated by the AfDB for fast-tracking Africa's structural transformation, this would represent about 10 percent of annual estimated resources required by ADF countries during the three-year replenishment cycle. For the entire three years, the proposal represents only about 3 percent of the total estimated financing gap.

For its part, the United Nations Economic Commission for Africa (ECA) continues to advocate for reforms of the global financial architecture (box 3.3).

Reforming the GFA should however not be considered as a panacea for Africa's structural problems in transforming their economies. The continent needs to capitalize on its domestic resources, including leveraging its abundant natural and human capital, improving the collection of tax and nontax revenues, enhancing public spending efficiency, and fighting illicit financial flows (IFFs) and tax evasion and avoidance. For instance, Africa can retain about $90 billion a year that is siphoned off through IFFs by improving domestic surveillance systems and accountable tax mechanisms that prevent leakages of such funds to tax havens and through other illegal means, including illicit harvesting and exploitation of the continent's natural resources.

BOX 3.3 Reform proposals by the High-level Working Group on the Reform of the Global Financial Architecture convened by the ECA

The High-Level Working Group on the reform of the global financial architecture convened by the ECA has made novel reform proposals specific to the IMF and the World Bank. The proposals include:

For the IMF:
- Ensure an ambitious comprehensive review of the IMF's concessional financing and policies to ensure the Fund can meet countries' rising demand for concessional resources. This will ensure the provision of sufficient loan and subsidy resources for the PRGT to guarantee lending capacity of at least SDR 3 billion a year from 2025, utilizing all possible internal resources including selling part of the IMF's gold reserves in the medium term to be used to bolster the PRGT's reserves; permanently terminating the PRGT Administrative Cost reimbursement, which could result in significant long-term savings for the PRGT; permanently increasing overall access limits for PRGT; and maintaining the concessional financing nature of PRGT with zero interest rate for all eligible countries.
- Enable affordable long-term catalytic lending through the IMF's RST by facilitating scale-up of debt swaps for nature, climate, and adaptation; enhance credit for green finance; and support country efforts to design and implement frameworks to attract private finance.
- Suspend IMF surcharges for two to three years while reviewing the institution's surcharge policy, with a view to eventually eliminating these surcharges.

For the World Bank:
- Ensure that the World Bank dedicates adequate attention to Africa's needs and development priorities, such as regional integration, infrastructure development, the just energy transition, and structural transformation.
- Scale up concessional and non-concessional World Bank financing to ensure that it can fulfill its expanded vision and mission, while safeguarding the principle of additionality. This will require making more resources available through donor pledges to the IDA20 Crisis Response Window Plus and providing more financing by implementing balance-sheet optimization measures of the IBRD and seeking its capital increase.
- Leverage more effectively the existing resources and transform the World Bank's approach to delivery, especially for African countries.
- Consider vulnerabilities beyond a country's income status to determine eligibility for World Bank concessional financing.
- Scale up the use of guarantees to reduce borrowing costs for developing countries by developing joint guarantee products by the Multilateral Investment Guarantee Agency, the International Finance Corporation, or the IBRD/IDA, to reduce exposure to sovereign and political risk, abolishing counting guarantees, and improving and streamlining access to guarantees.
- Crowd in private capital through de-risking techniques and blended finance vehicles.

Reforming the global tax architecture

African countries collect on average 15 percent of GDP as taxes, with high- and upper-middle-income countries like Seychelles and South Africa with rates as high as 28–33 percent, and low-income countries like Chad and Ethiopia as low as 7 percent.[32] These shares have remained relatively unchanged over the past three decades, with African countries' tax share of GDP in the range of 12–15 percent in 1990–2020.

Indirect taxes, which include sales tax, value-added tax (VAT) and excise taxes, account for 49 percent of tax revenue, the largest component of all taxes. Payroll taxes represent a very small amount reflecting the low share of the labor force employed in the formal sector. Taxpayers in Africa also deal with higher tax compliance costs than in countries at similar income levels in other regions, with residents in African countries spending 273 hours a year dealing with tax compliance issues compared with an average of 220 hours in other regions of the world.[33]

The gap between the tax capacity of 20 percent and the 15 percent of GDP collected reflects inefficiencies in revenue collection that can be corrected over the short term through domestic governance reforms

Implicit taxation, as opined by President Adesina,[34] is also high in many developing countries in Africa. When taxpayers self-provide basic social and economic services, such as street lighting, construction and repair of roads in their neighborhoods, water and sanitation, and security services, citizens may be paying higher taxes than is normally understood or reflected in countries' fiscal data. This places a heavy burden on citizens and erodes their trust and confidence in government, leading to low tax morale and compliance.

Following Coulibaly and Gandhi (2018) and Coulibaly (2020), it is useful to distinguish between the concept of tax capacity and that of efficiency of revenue collection. At 20 percent of GDP, Africa's tax capacity is low relative to other regions (chapter 1). Low tax capacity reflects structural factors such as the relative size of the informal economy and the sectoral distribution of GDP. It also reflects weakness in tax administration systems. As Africa succeeds in its efforts toward structural transformation (informality decreases and the share of high-productivity sectors in GDP increases), tax capacity will gradually improve.

The gap between the tax capacity of 20 percent and the 15 percent of GDP collected reflects inefficiencies in revenue collection that can be corrected over the short term through domestic governance reforms. The reforms are even more important than raising tax rates, given the structural constraints African governments face in collecting taxes, even at lower tax rates. Thus, reforms to improve governance and tax administration will infuse efficiency and compliance, thereby bolstering revenue intake from existing tax rates. Conversely, raising tax rates without addressing binding structural constraints would escalate already prevalent tax evasion and in turn yield minimal benefits from higher tax rates. Recent evidence has also shown that improvements in information and communications technology (ICT) access have enhanced the possibility of using technology to help raise domestic resource mobilization and tax collection in African countries.[35] Amid environments of low tax morale and low tax compliance, and of perceptions and realities of corruption (where tax collection systems are often manual and require in-person meetings with tax officials), technology may be able to provide a low-cost fix to raise domestic tax collection.[36]

With the success of innovative technologies and the adoption of mobile money services like M-Pesa in Kenya, African residents are becoming increasingly familiar with technology use for financial services. Technology like electronic fiscal devices, which automatically record transactions while they are performed and communicate the information to the tax administration, can raise tax compliance by sharing information about the sales amount made in each period, which can be checked against self-reported sales amounts from both VAT and income tax returns.

Mandatory use of electronic sales register machines has also yielded higher tax benefits in countries where implemented. In Ethiopia, for example, VAT payments increased substantially after such machines were introduced, with firms that were previously likely to evade tax reporting showing the largest increases.[37] This suggests that digitalization and automation could complement reforms to enforce compliance by making it easier for taxpayers to pay their taxes. These efforts must also be paired with data privacy and cybersecurity efforts from implementing governments to protect citizen's rights and information.[38]

Evidence also points to the importance of training of tax officials, especially in more advanced areas such as audit and transfer pricing. Chapter 2 presents details on how improvements in tax effort and efficiency of revenue collections can generate resources to finance Africa's structural transformation.

While countries ultimately need to rely on domestic resources to finance their development goals, global tax evasion and avoidance restrict their ability to do so. Reforms of the global tax architecture would therefore help improve domestic resource mobilization by containing IFFs and tax evasion and avoidance. Estimates in 2021 show that international profit-shifting, one of the most prevalent sources of leakage, costs African countries about 7 percent of their total tax revenues[39]—or 1 percent of Africa's GDP (about $275 billion), which is the same as total net international transfers to Africa in 2022.

The proposed minimum effective corporate global tax rate of 15 percent (box 3.4) is probably too low and will have little or no impact on African countries. Coulibaly and Abedin (2023b) point out that the average corporate tax is 24 percent. The rate should be comparable to those obtaining in all countries so that no company operating across borders should pay lower in Africa than they would pay elsewhere. Thus, reforms to improve governance and transparency of the global tax architecture are needed to curb illegal repatriation of resources to offshore tax havens. Moreover, setting a minimum tax that is so far below the average could lead to countries downward adjusting their tax rates toward the minimum with no change in revenue intake.

In addition to the minimum tax rate, the IMF (2019) argues for reforms of residual profit allocation, broadly allocating a normal return to source countries and sharing the residual based on a formula. It also argues for the allocation of taxing rights to destination countries. In recognition of the importance of tackling tax evasion and avoidance, several Africa-led initiatives have been established to stem IFFs (box 3.4).

Africa's domestic resource mobilization goes beyond tax and combatting illicit flows. Capital markets can also provide a conduit through which long-term local currency financing can be mobilized by leveraging savings and institutional capital in African countries. The AfDB has been supporting this through the African Financial Markets Initiative (AFMI) and the capital markets development workstream of its operations. Strong political commitment at the highest level would bring further impetus to the agenda for broadening the tax base in Africa.

BOX 3.4 Reforming the international tax cooperation architecture to reduce IFFs

International tax norms and tax rules

For decades, decisionmaking on global tax matters has largely been led by the Organisation for Economic Co-operation and Development (OECD) with most multilateral tax agreements reached in fora without universal participation, particularly by developing countries, which bear the highest burden of resource leakages.[1] The result is that developing countries with the greatest financing needs have been excluded from the development of new international tax norms.

This deficiency has limited the potential effectiveness and inclusiveness of the global tax norms and the tax system. Indeed, the OECD's inclusive framework for base erosion and profit shifting (BEPS) has been the main mechanism to date for international tax collaboration, which was launched in 2013 to end tax evasion and avoidance. The BEPS was born out of concern over the increased manipulation of existing gaps and mismatches in tax systems by multinational enterprises to evade taxes, thereby robbing countries of tax revenues. Currently, 143 countries have subscribed to and are implementing the BEPS framework. Although 27 African countries are part of the BEPS inclusive framework, there is concern that the initiative has not helped much to stem IFFs from the continent. Further, there has been very limited and in some cases no participation by African countries in BEPS processes, grounded in an atmosphere of distrust and a belief that mainly developed countries benefit from the BEPS initiatives.[2]

(continued)

BOX 3.4 Reforming the international tax cooperation architecture to reduce IFFs *(continued)*

Call for an inclusive mechanism to establish and oversee international tax norms and rules

The outsize influence of wealthy nations in the global tax cooperation system has led many lower-income countries, including African countries, to advocate for a more representative body to oversee the establishment and management of international tax rules. In November 2023, a proposed resolution for reforming global tax governance from the Africa Group at the UN passed overwhelmingly, marking an initial step toward a UN framework convention on international tax cooperation.[3] This resolution would shift control of international tax norms and rules from the OECD to the UN—an organization of 193 member states—to achieve a more inclusive and effective international tax cooperation.

The success of the resolution, despite strong opposition from the OECD, was historic because the last attempt to bring decisionmaking on tax rules to the UN was in the 1970s, and the failure of that attempt dissuaded any similar efforts for nearly 50 years.[4] The resolution thus demonstrates the overwhelming demand from low-income countries for an inclusive voice on global tax rules, which they have historically been excluded from. Such efforts will be reinforced by the participation of countries and financial centers across the world that are destinations for IFFs and can put all countries on an equal footing to negotiate global tax rules at the UN.

Further, to address tax competition and profit shifting, which has put unprecedented stress on the international corporate tax system, 136 countries, including 20 countries in Sub-Saharan Africa, agreed in 2021 to a minimum effective corporate tax rate of 15 percent, starting in 2023.

The Extractive Industries Transparency Initiative (EITI) was established as a global initiative to enhance transparency and combat IFFs, especially in extractive sectors. With a membership of 52 countries, half of which are from the African continent, EITI has helped limit the severity of IFFs, which are known to be highly prevalent in extractive industries.[5] As a global watch-dog, EITI requires governments to disclose all payments received from companies. Companies are also required to disclose payments made to the government in the form of established taxes and royalties. Amounts provided by both the government and the companies are then reconciled by an independent body.

This reconciliation has helped track underpayments, including some in Africa. For instance, through its 2012 and 2013 reporting, Ghana identified a $55 million discrepancy in reporting from a company to the Ghana Revenue Authority. According to its 2016 EITI report, Nigeria also recovered $2.4 billion in unpaid taxes following reconciliation of its oil and gas payments in 2016.[6] The effectiveness of EITI in stemming resource leakages depends on national and global cooperation, including from powerful global conglomerates, which may use tax havens to hide true representation of their earnings from extractive industries.

Regional initiatives to tackle IFFs and tax evasion and avoidance

In recognition of the severity of IFFs and tax evasion and avoidance in the continent, several Africa-led initiatives have been established, including:

- The Africa Initiative of the Global Forum on Transparency and Exchange of Information for tax purposes. This Africa-focused program was established in October 2014 to end tax evasion and bank secrecy through increased transparency and automatic exchange of information. Its membership consists of 33 African countries.[7] The 2022 Tax Transparency in Africa Report states that between 2014 and 2021, $244 million was identified and mobilized by nine African countries through this initiative.[8]
- The African Tax Administration Forum (ATAF) was formed in 2009, with a membership of African tax/revenue authorities. Its mandate is to strengthen their capacity in revenue mobilization and administration and to ensure that they are accountable to citizens. On IFFs, ATAF's work involves the promotion of transparency and intergovernmental cooperation in information exchange. ATAF also undertakes capacity-building activities through the training of officers from African tax authorities in diverse areas of taxation including transfer pricing, treaty abuse and other harmful tax prices, and customs management. As part of this program, ATAF has supported the establishment of transfer pricing units in several African countries. Increased tax collected due to ATAF since its creation totals $340 million, and an additional $1.20 billion tax has been assessed.[9]

(continued)

BOX 3.4 Reforming the international tax cooperation architecture to reduce IFFs *(continued)*

- The Yaoundé Declaration,[10] signed during the 10th plenary meeting of the Global Forum on Transparency and Exchange of Information for Tax Purposes. It mandated the African Union to initiate high-level engagements on leveraging tax cooperation to stem IFFs for scaling up domestic resource mobilization.

While reforms are underway to address imbalances of inclusivity in the global landscape for fighting tax evasion and avoidance, the effectiveness of these and other initiatives at regional and country level will largely depend on establishing and domesticating appropriate legal and institutional frameworks to use such instruments, enabling countries to benefit from tax cooperation.

Notes

1. GATJ 2022.
2. UN 2022.
3. https://undocs.org/Home/Mobile?FinalSymbol=A%2FC.2%2F78%2FL.18%2FRev.1&Language=E&DeviceType=Desktop&LangRequested=False.
4. Tax Justice Network 2023.
5. Available at https://eiti.org/countries.
6. Available at https://www.u4.no/publications/the-potential-role-of-eiti-in-fighting-corruption-and-iffs.
7. https://www.oecd.org/tax/transparency/what-we-do/technical-assistance/africa-initiative.htm.
8. AU, ATAF, and OECD 2022.
9. https://www.ataftax.org/overview.
10. https://www.oecd.org/tax/transparency/what-we-do/technical-assistance/Yaounde-Declaration-with-Signatories.pdf.

DEALING WITH AFRICA'S DEBT

More than 40 years after the debt crisis of the 1980s and after the implementation of the Heavily Indebted Poor Countries (HIPC) initiative, nearly half of African countries face sovereign debt problems (chapter 1). Although the debt situation in Africa is not systemic, the large number of countries either in debt distress or at high risk of debt distress presents a concern for the future development of the continent. Addressing Africa's debt conundrum requires reforms of the global debt and financial architecture to make it more accessible, nimble, and relevant, by facilitating restructuring of the existing stock of debt and reduction of Africa's debt premium to avoid the further buildup of unsustainable debt, which would drive countries deeper into debt distress (see recommendations at the end of this chapter).

Improving management and transparency of debt

Countries need to enhance their debt management capacity and develop notional, intertemporal fiscal rules to avoid overborrowing and getting into a debt crisis. There is a need to strengthen domestic fiscal councils and debt management offices, and to enhance the transparency of debt transactions, which can be achieved by improving the capacity of fiscal councils and making them independent, with clearly defined mandates to undertake surveillance on fiscal management and offer policy advice to governments. The use of fiscal councils in Africa remains low, with only Kenya, South Africa, and Uganda having them, but in Chile, for example, such use has been important in providing annual policy advice that informs budget planning, building fiscal prudence.[40]

To enhance transparency in debt management, it is important that details on debt agreements be made public for citizens to be aware of the commitments so as to assess the costs and benefits of each transaction. For example, some recent arrangements that included mortgaging public assets or placing future export earnings from natural resources (resource-backed loans) in escrow accounts may not have been politically feasible if they had been subjected to public scrutiny and due diligence. To further deepen fiscal prudence, the current uptake in use of fiscal rules in Africa signals the appetite of policymakers to achieve debt sustainability. For example, in Botswana the implementation of the debt and expenditure rules has been crucial to mitigate a rise in public debt. Yet, while progress on fiscal rules has been impressive, the exposure to shocks, uncertainty, and macroeconomic volatility, make the calibration of appropriate fiscal targets more difficult, calling for the need for larger fiscal buffers. A recent IMF study found that at end-2022, slightly more than half of Sub-Saharan African economies had debt ratio above their recommended country-specific anchor in the region-- median anchor stands at about 55 percent of GDP.[41] The rules lack the provision to sanction countries that fail to comply and have limited "escape clauses" to respond to emerging global challenges, such as COVID-19. This calls for reforms of the rules and a framework built to improve coordination at national and regional levels during implementation.

Africa's natural capital, which provides essential environmental services, should be valued to reflect its role as a capital good that sustains human existence

Regional multilateral development banks such as the AfDB with large footprint and convening power can play an important role in developing capacity for improved debt management and enhancing debt transparency. In Africa, the AfDB has developed strategies and initiatives to build capacity for scaling up domestic resource mobilization and to improve public financial management and debt management. These include the Strategy for Economic Governance in Africa (SEGA) (2021–25), the Multidimensional Action Plan for the Management and Mitigation of Debt Distress Risks in Africa—the "Debt Action Plan" (2021–23), the Capacity Development Strategy (2021–25), the Sustainable Borrowing Policy (2022), and the Public Financial Management (PFM) Academy. Under the PFM Academy, the AfDB has trained and graduated the first cohort of 51 high public officials from 26 countries responsible for public financial debt management. The IMF and World Bank launched in 2018 a Multipronged Approach to Address Debt Vulnerabilities (MPA).[42] In 2021, the OECD launched—at the request of the G20—an initiative to operationalize the Institute of International Finance's voluntary principles of debt transparency.[43] The objective is to enhance the transparency of private sector lending, particularly to low-income countries.[44]

Beyond implementing ongoing initiatives, the MDBs could work on strengthening domestic legal frameworks for public debt; standardizing clauses that promote transparency in public debt contracts; and developing frameworks for voluntary disclosure and reconciliation of loan information by borrowers and creditors.[45]

Enhancing the IMF–World Bank Debt Sustainability Framework

The current World Bank–IMF DSF needs to be updated to reflect the changing structure of economies and the impact of shocks, such as pandemics and climate change, on economies, especially those in Africa. Many low-income countries have natural capital[46] that is not captured as part of their wealth in assessing their headroom for debt accumulation. For instance, the value of Africa's natural capital was estimated at $6.2 billion in 2018.[47] This value includes only marketed assets. Other services, such as carbon sequestration by Africa's rich forests, are not measured and valued.

Africa's natural assets, like the Congo Basin Rainforest, act as critical carbon sinks, contributing substantially to climate change mitigation efforts. The negative externalities from unsustainable practices, including deforestation and pollution, are already undermining long-term economic sustainability and social well-being across the continent. While these natural assets deliver significant global public goods such as carbon sequestration, biodiversity conservation, and other ecosystem services, the value of these positive externalities are not factored in the measurement of the wealth of countries.

Excluding the value of such ecosystem services may result in a downward assessment of the size of GDP and the headroom required in assessing debt sustainability for countries endowed with these services and assets. Africa's natural capital, which provides essential environmental services, should thus be valued to reflect its role as a capital good that sustains human existence. Thus, greening the wealth of African economies by proper valuation and measurement of natural capital and associated ecosystem services could expand Africa's economies and unlock resources for the continent's structural transformation and development.

One issue with the DSF is that it focuses only on the liabilities side of the government balance sheet, that is, what the government owes—and it ignores government assets, that is, what the government owns and from which resources can be generated to liquidate the debt. Moreover, the fact that the methodology used to assess debt sustainability is not publicly available makes it difficult to replicate it independently and validate the findings.

Further, the DSF does not include climate or other sustainability and fragility risks such as the need for increased military spending to curb threats of insurgence, nor does it account for crucial investment needs for climate adaptation, such as the need to repair infrastructure damaged by cyclones or floods or the financing needed to achieve the SDGs. The DSF needs to be based on realistic assumptions and account for climate risks, and its spending needs to scale up investment in climate resilience, the transition to a green economy, and the 2030 Agenda for Sustainable Development. Facing growing concerns on the weaknesses of the DSF, the World Bank and IMF have recently agreed to incorporate climate considerations in their ongoing work on debt sustainability, including through the revised joint Low Income Country Debt Sustainability Framework.[48]

Improving and launching credit rating agencies

Credit rating agencies are very useful in informing the public about the creditworthiness of countries and in enabling emerging and developing economies to secure sufficient funding to achieve their development goals. Credit rating helps bridge the informational asymmetries inherent in the complexity of international markets, by providing information to investors about risks and opportunities associated with a sovereign borrower.

Improved policy space and attendant sound macroeconomic conditions in the wake of the debt relief through HIPC and the 2005 Multilateral Debt Relief Initiative provided collateral for African countries to engage with international capital markets. Many of these countries sought a credit rating to provide comfort to creditors of their creditworthiness. Borrowing from international financial markets by several African countries has grown exponentially over the past two decades, since Seychelles issued its first eurobond in 2006. Yet despite the high appetite for Africa's bonds from global investors, regional policymakers often flag a mispricing of their sovereign debt, presumably originating from a perception of risk by international investors that lead to "unjustifiably" high borrowing costs.

According to a UNDP estimate, this subjectivity, and lack of transparency in ratings, cost African countries over $24 billion in excess interest and over $46 billion in forgone lending over the life of multiple bonds in domestic and foreign currencies.[49] Moreover, Africa will have to pay $74 billion in debt service in 2024, in part due to high global interest rates and a stronger US dollar. Reforms to the GFA can spearhead conversations on this to make sovereign credit ratings more objective and transparent for African countries. As a first step, there is a need to push the agencies toward greater transparency, asking them to distinguish between the model-based and discretionary components of their sovereign ratings. In the same vein, the AfDB is also well positioned to lead the valuation of natural capital for Africa's transformation, and has already begun work on valuing African natural capital to compute "green GDP" and to inform green transition policies. This initiative has strong political support and ownership at the highest level across the continent, and results will inform policymaking to embed "natural capital accounting" in the System of National Accounts for reevaluating countries' GDP.

> The African Development Bank is well positioned to lead the valuation of natural capital for Africa's transformation, and has already begun work on valuing African natural capital to compute "green GDP" and to inform green transition policies

While credit ratings are influenced by many factors,[50] the rating of African countries by global credit rating agencies tends to ignore the value of natural capital and associated ecosystem services in assessing a country's headroom and debt risk profile. To reduce perceived risks of private investment in countries, MDBs like the AfDB can work with African countries to provide more up-to-date data and information on the state of their economies, and with international credit agencies to strengthen methodologies for assessing sovereign risk and help reduce the information gap in assessing credit ratings of Africa's sovereigns.

Through the African Union, African countries are working to develop and operationalize the African Credit Rating Agency (ACRA).[51] African Ministers of Finance have decided that ACRA will be private sector–driven, self-funding, and self-sustaining. The African Union has already developed the legal, financial, and structural aspects of the agency that support its sustainability, credibility, and independence. The creation of ACRA, as a pan-African initiative, would be another step toward African economic and financial integration and could enhance African countries' access to financing and integrate the continent with global financial markets. Moreover, its creation as a complement to global rating agencies could encourage these agencies to benchmark their services with a regional comparator rating agency, no doubt further improving their approach to assessing and rating Africa's risk.

Restructuring sovereign debt

The legacy problem of existing debt must be resolved. Seven African countries are in debt distress and 13 others are at high risk of debt distress, per the February 2024 update of the IMF–World Bank debt sustainability analysis. For the seven countries in debt distress, debt restructuring will be needed to avoid explicit default, which is more likely given the bunching of debt service payments in 2024 and 2025. Already three countries, including Benin, Côte d'Ivoire, and Kenya have issued eurobonds during the first quarter of 2024 to refinance maturing debt, although at higher yields than on the refinanced debt. Moreover, not all issuance of eurobonds is for the financing of developmental needs as "new debt" as a proportion of the proceeds from bond sales are being used increasingly to refinance past debts, and this could exacerbate debt vulnerabilities in these countries in the future. Progress is being made with the G20's Common Framework, as seen in the recent experience of Ghana, whose debt restructuring has been faster than that of Zambia and other earlier applicants to the Common Framework.

A debt relief for climate initiative is needed, tailored toward supporting African countries, and may include reductions of both bilateral and multilateral debt to finance climate mitigation and adaptation

Still, the Common Framework's shortcomings, such as eligibility, timeliness, and the comparability of treatment systematically, must be tackled. These stem mainly from coordination failures of bringing together different classes of creditors, given the changing structure of Africa's public external debt, where more than half of it is now held by non-Paris Club members and by private creditors and bondholders who are not members of the London Club.

Given the multiplicity of lenders, debt restructuring is now complex and protracted. Restructuring requires an agreement with many disparate bondholders with widely different interests and constraints. Their incentives are very different from those of London Club members. It also requires an agreement with other key lenders including China, in addition to Paris Club members. China's geopolitical interests, and its domestic financial and institutional constraints, are very different from those of Paris Club members and, unless China joins the Paris Club or subscribes to its tenets, the G20 will need to pay special attention to the country's needs to get its support for debt restructuring agreements under the Common Framework.

A possible approach to dealing with outstanding debt would be a market-based solution—like the Brady Plan of the 1980s, with some adjustments to reflect today's realities.[52] It could involve the creation of a special-purpose fund to be capitalized by IFIs and official bilateral development partners. This fund would then be used to secure collateral against new tradable bonds, to be issued by debtor countries. The collateral, which implies a credit enhancement, would allow the new bonds to be issued at better terms—longer maturities and lower coupon rates, with the proceeds used to reduce the outstanding balance on existing debt. These better terms—plus a possible haircut—could lead to sizable reductions in debt burdens to sustainable levels.

A debt relief for climate initiative is also needed, tailored toward supporting African countries, and may include reductions of both bilateral and multilateral debt to finance climate mitigation and adaptation.[53] Eligible countries would be granted partial debt relief in exchange for their commitment to investing the savings from debt service in climate-related projects such as renewable energy or forest protection on the mitigation side; or irrigation and food security on the adaptation side. To reap the benefits of debt service savings, improved fiscal efficacy is required, through spending these funds to scale up investment in productive infrastructure to support economic and structural transformation. A list of eligible projects would be agreed upon during negotiations, and IFIs could monitor implementation. The interest of this proposal is that it requires sacrifices from all classes of creditors—even those with "preferred creditor" status.

The shift from syndicated bank loans to traded securities as the principal instrument for sovereign financing, combined with the greater diversity of claims and interests, has made it difficult to secure collective action from creditors when a sovereign's debt is unsustainable. That is why several voices have recommended the creation of a sovereign debt authority and a sovereign insolvency system to facilitate orderly and rapid restructuring of unsustainable debt, so as to support the debtor country while also protecting the rights of creditors.[54] Although the proposal for a centrally managed sovereign debt authority has been around for more than two decades, it has not been accepted by the international community. A more politically feasible second-best solution may thus be explored to help improve the debt situation for African countries, including reforms that could be implemented immediately, while discussions on the costs and benefits of a centrally managed sovereign debt authority continue.

G20 countries could consider enacting legislation to encourage private creditor participation in debt workouts. Most sovereign debt is governed by laws of a few jurisdictions, such as New York State or England. Those key financial centers could be encouraged to enact statutory reforms that would codify a duty on creditors to cooperate in the context of sovereign debt restructuring; limit the amount that a creditor can receive in a legal proceeding if an agreement is reached with a majority of creditors; immunize sovereign debtors' assets from seizure where the debtor has initiated an orderly debt restructuring process; and retrofit collective action mechanisms into existing instruments.[55] Efforts are underway in New York and London to deal with this issue through new legislation.[56] The G20 should encourage all its member countries to adopt similar laws.

Updating the IMF lending in arrears policy

Implementation of changes in the IMF's lending in arrears policy, as approved by the IMF Board of Directors on April 9, 2024, would encourage official bilateral creditors to move faster on debt restructuring.[57] Because MDB provision of quick-disbursing budget support is almost always linked to the presence of an IMF program, this would also imply that MDBs would be more flexible and be able, in certain conditions, to support countries before final agreement is reached on restructuring official debt. Changes in the lending in arrears policy could save Africa up to $44 billion in outstanding arrears (chapter 1).

The IMF mandates that all the programs it supports be fully funded, and this mandatory requirement is endorsed by all MDBs, which benchmark their support to a debtor on the presence of an IMF program. This means that when a country's debt is considered unsustainable, MDBs and IFIs cannot provide that country with financing unless it takes steps to restore debt sustainability. In practice, a program and financing cannot take effect unless the country and its creditors have an agreement on debt restructuring. If the country is already in arrears to its creditors, an agreement with creditors on arrears clearance is needed prior to getting IMF balance-of-payments support, and thus MDB budget financing. The IMF distinguishes between arrears to private creditors and those to official bilateral creditors.

With private creditors, the IMF can proceed with a program, despite the arrears, if it considers the country to have made an adequate debt restructuring effort or if it is assured in writing that a debt restructuring deal will be forthcoming.

IMF policy on arrears to official bilateral creditors has traditionally been more stringent. Until April 9, 2024, the IMF could only lend to a country in arrears to official creditors under one of three "strands." The first strand is that there is a debt restructuring agreement between the country and a representative majority of its official bilateral creditors, which usually meant an adequately representative Paris Club agreement or an agreement under the Common Framework. The second strand is that the creditors provide consent for the IMF to lend despite their arrears.

The third strand requires that the following three criteria are met: prompt financial support is essential and the country is pursuing adequate policies; the debtor is making good faith efforts to reach agreement with the creditor on a contribution consistent with the parameters of the IMF-supported program; and the decision to lend into arrears would not have an undue negative effect on the IMF's ability to mobilize official financing packages

Group of 20 countries could consider enacting legislation to encourage private creditor participation in debt workouts in future cases. The third criterion effectively excludes IMF lending if there is no agreement or consent from a major creditor. That is, the design of the policy means that in restructuring contexts where multiple creditors are involved, the IMF can only use the first and second strands, with co-use of the third strand, but that would rarely involve a majority creditor or group of creditors.[58]

Where a representative committee of creditors has been involved, as with the Common Framework, the IMF has simply waited for it to deliver the required financing assurances. This approach worked well when all the major official creditors were members of the Paris Club, but this process faces long delays in the new creditor landscape. Disagreements among creditors over processes, parameters, and comparability of treatment hold up progress. With Chad, the delay was about 11 months, and with Zambia it took 9 months.[59] The system seems to be working a little better as the delay with Ghana fell to five months, but that is still quite long, and long delays are costly. The debtor countries' macroeconomic situations and their debt sustainability continue to worsen as MDB financing is being held hostage to an agreement with creditors. In these conditions, the debtor is in a much weaker negotiating position against the creditor.

A new policy would provide the international financial institutions (IFIs) with greater flexibility to lend to African countries before an agreement on official arrears clearance, and should reduce delays in concluding IFI-supported programs and in obtaining financing

Aware of these issues, the IMF has updated its lending in arrears policy by introducing a fourth strand. This additional strand could be used when the existing strands cannot provide a pathway—that is, if an adequately representative agreement has not been reached through a representative creditor forum, consent is not forthcoming within four weeks of being requested, and the three criteria under the third strand cannot be satisfied. The new policy distinguishes IMF-supported programs with *normal* access and those with *exceptional* access. For a program with normal access, IFIs would follow a "standard safeguards approach," and can go ahead with a program before official arrears clearance, provided that the program includes conditionality to support the debt restructuring process, as well as a commitment from the debtor country to good faith efforts to establish safeguards for lending by IFIs (that is, pursue an agreement with its creditors). For a program with exceptional access, IFIs would follow an "enhanced safeguards approach," which in addition to the program conditionality and debtor commitment under the "standard safeguards approach" will require a direct commitment to the IFIs by a sufficient set of creditors about their restructuring intentions.

This new policy would provide the IFIs with greater flexibility to lend to African countries before an agreement on official arrears clearance, and should reduce delays in concluding IFI-supported programs and in obtaining financing. It would also encourage creditors to move faster to reach agreement and reduce the pressure on debtor countries.

Resolving debt issues through international and African actions

International actions to resolve debt issues would affect Africa's structural transformation through two channels. First, supplementing the Common Framework by a Brady-bond type initiative and by a debt reduction for climate mechanism like the HIPC initiative (but that would be applied to middle-income and low-income countries) would reduce debt service costs and thus release more resources for investment. Second, the debt restructuring, with reforms of the DSF and credit rating agencies, would enhance Africa's creditworthiness and reduce the risk premia attached to African debt, improving the availability of new financing and reducing its cost. For instance, as seen, Africa will have to pay $74 billion in debt service payment due in 2024 in part due to the high-risk premium on its sovereign borrowing. Reforms to credit rating agencies could reduce debt service costs and release additional financing. Africa could also save up to $74 billion a year in interest payments if the global credit ratings system were fairer and based on fundamentals. The UNDP calculates that gains from lower interest could be $24 billion and additional new lending could be as high as $46 billion. Further, Africa could save up to $44 billion in accumulated arrears if these arrears are forgiven. Resources freed from these reforms could secure about $169.4 billion a year in development financing, or equivalent to about 42 percent of the estimated annual financing gap of $402.2 billion needed to fast-track Africa's structural transformation.

African countries also need to tap into domestic opportunities to improve their debt position. Reforms geared toward improving public expenditure management will be crucial, as many African countries are experiencing a rise in recurrent expenditures, as seen in large public wage bills. These weigh heavily on public spending, causing elevated fiscal deficits and leaving fewer resources available to invest in critical sectors to accelerate structural transformation. For example in 2022, the wage bill in Africa (excluding North Africa) stood at 51.3 percent of tax revenue, with wide variation among countries.

Countries with fiscal rules in place need revisions of these rules to improve transparency and flexibility, and to make them predictable. These rules should be complemented with independent fiscal councils capacitated to offer unbiased fiscal projections on revenue and to evaluate rules compliance.

Finally, the current momentum by African countries to improve the business climate should be improved and sustained as it can boost private sector development and attract investment. A coordinated regional approach for investment facilitation platforms would therefore enable countries to mitigate investment obstacles, enhance transparency, and improve accountability to ease business operations. The African Investment Forum, launched by the AfDB and its partners in 2018, is a step in this direction.

FINANCING CLIMATE ACTION

Climate change threatens Africa's progress on structural transformation. The negative effects of rising temperatures are numerous and recurring, and include increased mortality and morbidity, loss of GDP per capita, labor productivity declines, lower trade, conflicts and civil wars, and worsening social inequality, including widening gender gaps in human capital outcomes from education to employment and income.[60] Evidence in the African Economic Outlook 2022 shows that climate change has caused annual losses of 10–15 percent of GDP per capita growth in African countries during 1986–2018. The reduction in GDP per capita growth in the high warming scenario is projected at 16–64 percent by 2030 in Africa, with countries in West and East Africa projected to bear the brunt of the impacts.[61]

As seen, mobilizing the financing needed for climate action is an important driver for reforming the GFA. To meet the goals of the Paris Agreement, the Global South (excluding China) needs financing of about $2.4 trillion a year. There is general agreement in the international community that the current system, which has failed to enforce the honoring of climate financing of a $100 billion a year commitment by advanced countries, cannot deliver these trillions and must therefore be reformed, especially as the structure, flow, and scale of current global climate finance are complicated and misaligned with Nationally Determined Contributions and with SDG financing requirements in Africa (box 3.5).

Africa has to ensure that the needed climate investments receive due financing, because the continent is vulnerable to risks of climate change and has historically received too few resources to finance its climate actions. Moreover, Africa must receive climate financing in addition to financing for the SDGs and structural transformation, and there should be no "resource substitutability"—that is, resources needed for development should be additional to those for financing climate and other global public goods actions.

Africa has to ensure that the needed climate investments receive due financing, because the continent is vulnerable to risks of climate change and has historically received too few resources to finance its climate actions

While African populations have contributed just 4 percent to cumulative greenhouse gas emissions, African countries will disproportionately bear the brunt of the damage from climate change.[62] Indeed, the share of climate-related natural disasters in African countries has been increasing since 2000, making up 52 percent of all disasters in African countries between 2000 and 2023. The affected populations from these disasters totaled over 529 million people in this period.[63]

Investing in climate mitigation and adaptation

Tackling the climate crisis will require unheard-of investment in climate infrastructure in multiple sectors including energy, agriculture, water, and health, for infrastructure disaster prevention and preparedness.[64] With droughts and floods threatening food security for millions of Africans,

BOX 3.5 **Instruments for climate risk mitigation, adaptation, and resilience**

The *African Economic Outlook 2022* showed that the current global climate finance architecture is misaligned with countries' Nationally Determined Contributions and their SDG financing requirements. Due to the prioritization of risk-return considerations over development imperatives and climate resilience and vulnerabilities, climate finance tends to be primarily mobilized for more resilient and less vulnerable countries, instead of flowing to climate-vulnerable countries or to those less resilient to climate change. In addition, the high fragmentation of the global climate finance landscape and its donor-centered architecture impedes climate finance inflows to the continent. Equally, maintaining the status quo will be detrimental to Africa and its net-zero ambitions.

There is an urgent need to review and restructure the current global climate finance architecture to align it with countries' Nationally Determined Contributions and their SDG financing requirements, and to ensure that the most vulnerable countries harness climate resilience opportunities. Between 2010 and 2019, debt instruments, mostly loans, accounted for about two-thirds of all climate finance channeled to the continent. Out of these loans, two-fifths were on commercial terms, which may perpetuate the continent's existing debt sustainability problems—hence the need for more concessional financing to address Africa's climate challenges. With Africa's negligible contribution to global carbon emissions and the disproportionate impacts of climate change on its economy, such financing is needed to ensure climate justice. Based on the AfDB's estimates of carbon debt and carbon credits, total climate finance due to Africa to compensate for its historical and future emissions is estimated at between $4.76 trillion and $4.84 trillion for 2022–50, which translates into an annual figure of between $163.4 billion and $173 billion.

Although a $700 million Loss and Damage Fund, which was announced at COP27 in Egypt, was finally agreed on at COP28 in Dubai to provide financial assistance to climate-vulnerable developing countries, this pledge covers less than 0.2 percent of the irreversible economic and non-economic losses from which developing countries suffer each year because of global warming. Resources are available at the global level for climate finance but strong political will is needed to move beyond mere commitment. To put this into perspective, during the COVID-19 pandemic, about $17 trillion was swiftly mobilized worldwide in just two years, 2020 and 2021, to support the global economy. Almost 90 percent of this amount was provided by G20 advanced economies whose commitment to mobilize $100 billion of climate finance for developing countries is yet to materialize.

The AfDB has fully aligned its work with the Paris Agreement, devoting 41 percent of its total investment portfolio to climate finance in 2021 and 67 percent of its climate finance to climate adaptation, the highest of all global and bilateral development finance institutions. It aims to double its climate finance commitments for 2020–25 and commit at least $25 billion toward climate finance by 2025 to address climate vulnerability and risk in Africa.

During COP27, the AfDB and its partners launched the Alliance for Green Infrastructure in Africa to speed up the development of green infrastructure in Africa, which is rare in the continent, and this can be seen in Africa's share of global green bonds that support green infrastructure. Of the total of $522 billion issued globally in 2007–18, Africa accounted for only $2 billion, the lowest share of all regions in the world. Africa also accounted for just 1.9 percent of all green loans in 2021, and 1 percent of global issuances of sustainability bonds and sustainability-linked loans and bonds. By focusing on the development of green infrastructure, Africa can increase its share of green bonds to 2.5 percent globally, and leverage about $14 billion in green financing to boost its green infrastructure assets.

Source: Staff elaboration based on African Economic Outlook 2022 and various other sources.

a growing population and labor force expected to double by 2050—and quadruple by 2100 (at which point the continent will account for 40 percent of the world's labor force)—the need for climate financing is self-evident.[65] Energy access for this growing population remains a perennial problem, with only low levels of electricity generation powered (by fossil fuels). In 2020, an estimated 40 percent of the CO2 emitted in Africa was sourced from fossil fuel–based electricity and heat generation, with 25 percent from transport alone. Closing the energy access gap in Africa will need an estimated investment of more than $25 billion a year through 2030, and a commitment to the green transition, which reduces dependence on fossil fuels while leveraging the continent's vast renewable energy potential for electricity generation.[66]

With 30 percent of the world's mineral resources, Africa has a wealth of natural capital, alongside its human capital—a growing, increasingly educated young labor force. Both are required for the green transition. The continent's enormous renewable energy potential, including wind, solar, hydropower, and geothermal, makes it extremely attractive for private investment. Investing an estimated $1.8 trillion between 2020 and 2030 in energy-efficient buildings, low-carbon transport, and renewable energy in Africa could generate $7.1 trillion in net benefits globally for private investors.[67]

Growing access to ICT, with the expansion of mobile phone use and internet access, also provides opportunities for big gains for private investors. Africa's ICT market is expected to have expanded from $95.4 billion in 2020 to $104.2 billion by 2023. In addition, green technologies, from smart technology in agriculture to enhance renewable energy–powered irrigation to leveraged ICT and online hiring platforms to reduce costs of matching employers and job applicants, have the potential to provide large gains for private investors.[68]

MDBs and bilateral partners can be more purposeful in climate financing by allocating funds for climate adaptation projects that are directly linked to development and economic transformation. But given the concern that such involvement may mean diverting funds from development objectives like better education, health, and food security, it is important to distinguish projects for climate adaptation from those for mitigation. Adaptation is a national public good, mitigation a global public good.

Development financing and climate adaptation financing are not mutually exclusive, however. Additional financing must be dedicated to development financing, in a way that focuses on climate adaptation efforts. For example, a large share of the climate-related natural disasters in Africa came from epidemics (14 percent), which accounted for the second-largest category of disasters after floods (25 percent) between 2000 and 2023. Epidemics of infectious diseases can decrease economic outcomes, with meningitis epidemics in Africa liable to reduce GDP growth by an estimated 2–4.3 percent, absent health aid interventions like cash grants to households and vaccine financing from MDBs such as the World Bank and AfDB.[69]

Health expenditures of African governments are among the lowest in the world. As a result, out-of-pocket spending on health as a share of health expenditure is high in Africa at around 37 percent, double the 18 percent in the rest of the world. A key feature of health spending in African countries is the high share of health spending from external, development partner sources like MDBs. External spending on health accounts for 20 percent of health spending in African countries, far higher than the global average of 0.2 percent. MDBs are therefore vital for Africa in shoring up primary health care and for infectious disease management linked to climate change, and to adapt to the negative effects of climate-induced epidemics through the provision of health aid during epidemics.

Development financing and climate adaptation financing are not mutually exclusive. Additional financing must be dedicated to development financing, in a way that focuses on climate adaptation efforts

Building an African green bank

One way of protecting funding for development is to create specialized institution that would finance only climate mitigation—an African green bank—leaving MDBs to finance development and adaptation. The AfDB has already launched the African Green Bank Initiative (AGBI) to create an ecosystem of green banks throughout Africa, with the aim of mobilizing additional climate finance geared toward green and sustainable growth. AGBI provides a model of leveraging private and public sector investments that support African countries' climate ambitions, in line with their Nationally Determined Contributions.[70]

The AGBI is working to create a $1.5 billion ecosystem of green investment facilities by 2030. As a catalytic initiative relying on a blended finance approach, the AGBI comprises two financing windows: technical assistance (TA) and green finance facility (GFF) funding (figure 3.6).

The proposed African green banks would be able to use financial instruments like green bonds and debt-for-climate swaps to finance climate mitigation in Africa. Private sustainable financial flows to developing economies were around $250 billion in 2021, with 59 percent of that in green bonds. Green loans, sustainability bonds, sustainability-linked loans, sustainability-linked bonds, and social bonds made up the rest.[71] Africa accounted for only 0.1 percent of total global green bond issuance in 2022, much less than its economic size (2.8 percent of global GDP) and population (17 percent). Only three countries—Benin, Egypt, and South Africa—constituted more than 90 percent of Africa's green bonds in 2022. Energy has remained the dominant sector for green bond investments.[72] The proposed African green banks could centralize this process to increase investment from MDBs and corporate lenders, along with managing debt-for-nature and debt-for-climate swaps, and spearheading a more centrally regulated carbon market as well.

Launching the African Carbon Markets Initiative

Carbon markets offer potential for expansion, to finance climate mitigation and adaptation, and to spur economic development in Africa. A major development in the last couple of years has been the launch of the African Carbon Markets Initiative (ACMI) at COP27 in 2022. It aims to set up carbon credits as one of Africa's top export commodities by focusing on nature- and technology-based removal credits. The ACMI was launched by the Global Energy Alliance for People and Planet, Sustainable Energy for All, and the United Nations Economic Commission for Africa (UNECA) with support from the UN Climate Change High Level Champions, and is led by a 13-person steering committee of African leaders and carbon market experts.[73]

Carbon credits—or carbon offsets as they are sometimes called—are certificates that can

FIGURE 3.6 African Green Bank Initiative—two financing windows

	1 Technical Assistance	2 Green Finance Facility Funding
Contributors	*Donor countries, MDBs and DFIs, climate and environment funds, philanthropic or impact investors*	*Private sector, MDBs and DFIs, climate and environment funds*
Description	○ Design and set up green finance facilities ○ Operationalize entities ○ Build bankable pipelines of green projects ○ Set up monitoring, evaluation and reporting processes	○ Assess initial capital requirements and build resource mobilization strategy ○ On a case-by-case basis, capitalize green finance facilities through equity or subordinated debt ○ Support operationalized green finance facilities through debt funding
Financial instruments	○ Grants	○ Equity and subordinated debt ○ Debt funding
Beneficiaries	Governments; Private banks	Public banks; Microfinance institutions

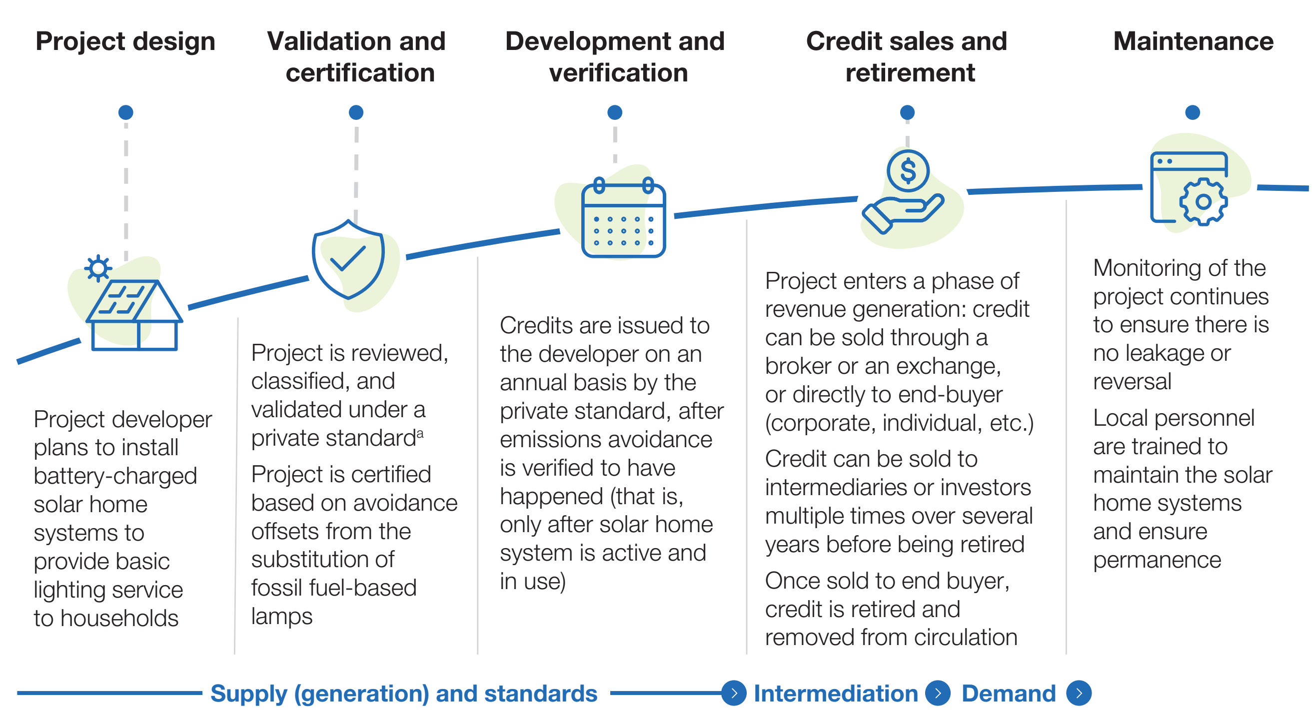
Source: AfDB 2023.

be traded and sold to individuals or corporations who would like to make up for their emissions by using carbon credits to make claims toward their carbon targets. Carbon markets can be compliance markets, like cap-and-trade systems, where regulators set a fixed maximum limit or cap on total emissions and allow producers to trade allowances after an initial auction or distribution period. Or they can be voluntary markets, where a project developer sets up a project to avoid certain emissions (as in gas flaring) or removes CO2 equivalent from the atmosphere (as by growing more trees). Projects need to be verified by an independent body to meet the requirements of the standard-setting entity and, once certified, credits are issued to the project. The developer then sells the credits to firms, governments, or individuals, and these credits can be bought or sold via markets (figure 3.7).

A major goal of the ACMI is to increase the size of Africa's voluntary market. Already there has been some progress, but there is a long way to go. In September 2023, at the Africa Climate Summit in Nairobi, the United Arab Emirates pledged to buy $450 million-worth of credits. The Johannesburg Stock Exchange recently launched its own voluntary marketplace.[74] Article 6 of the Paris Agreement allows countries to partially meet their Nationally Determined Contributions by buying credits or internationally transferred mitigation outcomes (ITMOs) issued by other countries, which would allow the market to find the most efficient way to reduce emissions while raising capital for projects to spur development in poorer countries. African countries could become major exporters of these credits, with capital raised from the credits used to invest in renewable or clean technologies.

Already, several countries are taking advantage of carbon credit market opportunities (figure 3.8). Kenya has amended its climate change law to ensure that its projects are in line with the Paris Agreement article. Ghana and Senegal have sold cookstove-based credits to Switzerland in a bilateral deal. Selecting eligible sectors for these credits or ITMOs is also, increasingly, an essential part of economic policymaking in African countries where governments want to issue ITMOs

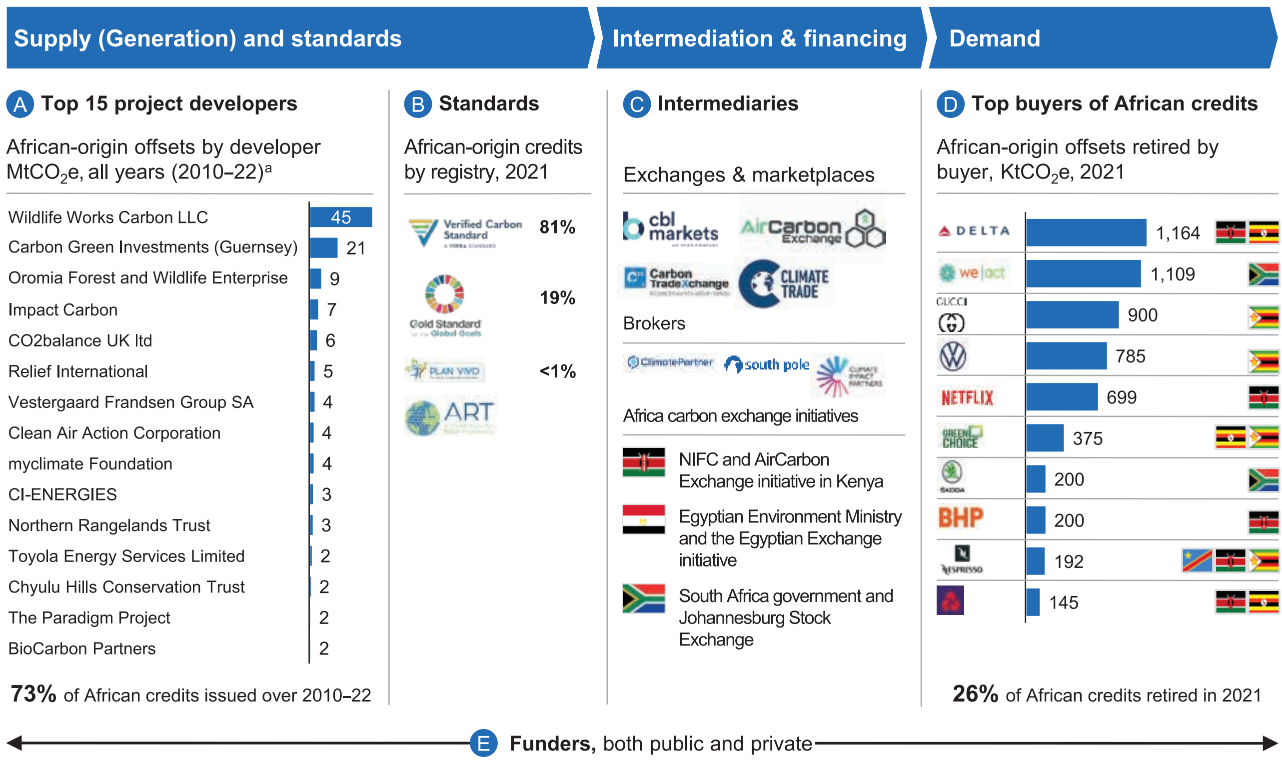
FIGURE 3.7 Example of the lifecycle of a carbon credit project



a. For renewable energy projects, often only countries on the UN's list for least developed countries can qualify for carbon credit generation.

Source: ACMI 2023.

FIGURE 3.8 A snapshot of major players along the carbon credit value chain in Africa



Source: ACMI 2023.

that raise a lot of money for projects in areas that can be very lucrative, like renewable energy and cooking fuel. There is enormous potential for the use of these carbon markets to boost economic outcomes for Africans, including in areas like forestry and lands, where credits could increase community protection of natural resources by providing direct payments for this through the credit scheme. Africa's pastoralists, covering over 40 percent of the continent's land area, could benefit from direct payments for their role in managing carbon sinks.[75]

The ACMI has enormous potential to reduce poverty and reduce carbon emissions. It has, among its objectives, the expansion of voluntary carbon markets to unlock $6 billion in income, while boosting energy access, biodiversity, and health, and creating employment and sustainable livelihoods for Africa's population.[76] Burundi, Gabon, Kenya, Malawi, Mozambique, Nigeria, and Togo are among the growing list of African countries that have already developed plans to sell carbon credits. As one example, the Kasigau Corridor REDD+ (Reducing Emissions from Deforestation and Forest Degradation) project in Kenya has sold carbon credits totaling more than $1.2 million since June 2011.

To fully unlock the climate mitigation and economic development potential of the ACMI will require determination of the appropriate price of carbon in the global carbon markets that set the standard for carbon trading globally. It also requires local research capacity, where African research institutions, universities, and think tanks study the most impactful sectors for these carbon credit markets. The creation of a central database, in partnership with local universities and research institutions in Africa, which tracks the number of projects, funding, and impact details in the newly created ACMI, will strengthen the market's credibility and allow it to reach the potential that the ACMI has for delivering a double dividend of increased economic development and reduced emissions in African countries.

A collaborative report from the African Climate Foundation and the London School of Economics

Firoz Lalji Institute for Africa warns, however, of potential negative impacts on African economies from the European Union (EU)'s Carbon Border Adjustment Mechanism.[77] Projections indicate steep reductions in key exports to the EU, such as aluminum, iron and steel, fertilizer, and cement, potentially leading to annual GDP declines. Additionally, the EU's Regulation on deforestation-free products poses challenges for African exporters dealing in commodities like coffee, cocoa, cattle, and leather, with small-scale farmers particularly affected. Early signs suggest a shift from African coffee among EU buyers. These consequences underscore the need for better coordination, global solidarity, and careful consideration in revising policies to mitigate adverse impacts on low-income countries.

IMPROVING AFRICA'S ACCESS TO EMERGENCY FINANCING

Africa continues to face a confluence of shocks, most recently the economic slowdown caused by the COVID-19 pandemic, the spike in food prices caused by geopolitical tensions, the rise in interest rates as the world's central banks tighten monetary policies, and extreme weather events whose frequency is rising with climate change. The way to deal with a temporary shock is usually for a country to borrow to smooth its consumption and investment and to avoid sharp economic fluctuations. In the case of the pandemic or the spike in food prices, access to financing becomes a necessity to save lives through imports of vaccines and food.

The frequency of shocks will likely remain high or even increase in the future, as evident in the recurrence of climate-related shocks as global warming increases. The current geopolitical situation—with an increase in armed conflict; superpower rivalries; and the move toward deglobalization and restrictive practices, inward-looking trade restrictions, and friend-shoring—is inimical to the functioning of the GFA and to commodity price stability.

Ensuring access to a financial safety net…

Given these challenges, Africa needs greater access to global financial safety nets—better, its own safety net—access to which can help improve its productive capacity, diversify its production base, and build resilience to shocks. Capital markets in Africa are underdeveloped due to low domestic savings and weak institutional and regulatory environments. Most African countries face credit constraints and high interest rates and cannot depend on financial markets to mitigate the impact of exogenous shocks. This is in stark contrast to the advanced economies, where a "flight to safety" causes yields on their bonds to drop and supports their fiscal stimulus.

This is a key paradox that highlights the inequity of the current GFA. Only 11 African countries have access to emergency regional financial support: 10 through the Arab Monetary Fund and South Africa through the BRICS Contingent Reserve Arrangement. The remaining 43 must rely solely on the IMF, and even then, they are constrained because IMF support to any country depends on that country's quota, which is limited for small African countries.

… along three avenues

Reforms to the GFA need to increase Africa's access to global financial safety nets, along three main avenues: delinking access to IMF financing from quotas; introducing state-contingent clauses in loan agreements with IFIs; and creating an African emergency finance facility or institution.

First, in addition to determining country contributions and voting rights, IMF quotas provide a nominal ceiling on a country's access to resources beyond which it must pay higher charges, and its program becomes subject to more oversight. This system made sense at the time the IMF was created because its main mission was to support the gold standard and the fixed exchange rate system by providing balance-of-payments financing to countries to protect their exchange rate. Under a fixed exchange rate system, larger economies would need more support than smaller economies, which made it reasonable to link access to IMF support to a country's quota, which is determined by the size of its economy.

But countries came off the gold standard in the early 1970s and major currency exchange rates are now flexible. It is the smaller and mid-size economies—many of whom are in Africa—that

Reforms to the global financial architecture need to increase Africa's access to global financial safety nets, along three main avenues: delinking access to International Monetary Fund financing from quotas; introducing state-contingent clauses in loan agreements with international financial institutions; and creating an African emergency finance facility or institution require more support from the international financial community. That is why access to lending by the IMF should reflect a country's development needs and creditworthiness, not its quota, and is why the policy of surcharges that penalize African countries that need more support should be revisited.

Second, state-contingent debt instruments (SCDIs) can help reshape Africa's public debt risks in a world of heightened macroeconomic uncertainty. SCDIs link a sovereign's debt repayments to its capacity to service them, while keeping the present value of the stream of debt service constant. This means that during an unexpected shock, there is a built-in reduction in the sovereign's debt service burden, which is compensated for by higher repayments later.

> With Africa's population expected to rise further as a share of the global population, the share of International Monetary Fund voting rights allocated to the continent should reflect these demographic dynamics, not only the size of economies

SCDIs allow for the preservation of policy space by avoiding costly debt restructuring, facilitating a range of countercyclical and stabilization policies. SCDIs can serve as a useful complement to the traditional government policy toolkit. Where the debt burden reduction is large relative to capacity to pay, SCDIs can build economic resilience in the face of shocks. SCDIs' systematic incorporation across multiple debt instruments, including commercial, bondholder, bilateral, and multilateral debt, could foster a less crisis-prone GFA. Careful instrument design and complementarity with institutions, contracts, and regulations can help overcome moral hazard. The instruments' effectiveness is also enhanced with investments in risk reduction and preparedness, and other prearranged finance such as contingency funds, catastrophe bonds, and insurance.[78] Together, these could increase the uptake by reducing higher liquidity premium sometimes associated with the mechanism.

IFIs should be the first to introduce and use SCDIs, and incentivize widespread adoption of sovereign SCDIs to support better public debt management, climate-proofing of public finances, and faster response with a built-in debt deferral mechanism for preagreed shocks—all to help avoid further human suffering and economic loss.[79] The uptake of SCDIs would move governments toward faster, more reliable, post-disaster finance.

Third, the creation of an African emergency finance facility/financial stability mechanism or institution, with the sole mandate of debt refinancing, should complement the work of IFIs and ensure that African countries always have access to adequate and affordable financing, particularly during times of crisis. It would be a facility that can alleviate countries' short-term liquidity constraints by enhancing credit and augmenting liquidity in domestic and international debt markets. The decision of the Assembly of Heads of State and Government of the African Union in February 2022, which called for the establishment of an AFSM and directed the African Union Commission and the AfDB to "work with all relevant stakeholders to accelerate operationalization of the mechanism and its growth," is a move in the right direction.

Beyond these three avenues, African countries should, crucially, implement reforms to strengthen and deepen their financial sectors so that eventually they themselves become their own cushions against shocks.

ENHANCING AFRICA'S PARTICIPATION AND VOICE IN THE GLOBAL FINANCIAL ARCHITECTURE

The current configuration of the GFA governance system provides limited participation and in tandem, little voice to countries of the Global South, particularly to Africa. Voting rights are based on several dimensions, including economic and population sizes. Crucially, the voting rights of the 54 African countries at the IMF—with their combined population of over 1.4 billion people—are only 6.47 percent of the total, about the same as Japan with a population of 123 million people,[80] one-twelfth that of Africa. Switzerland's share of voting rights (1.17 percent) is 13 times that of Ethiopia (0.09 percent), while Ethiopia's population of 130 million is nearly 15 times that of Switzerland (8.8 million). Further, Africa's population has increased from 12 percent of the world's population in the 1990s to 18 percent in 2022. With Africa's population expected to rise further as a share of the global population, the share of voting rights allocated to the continent should reflect these demographic dynamics, not only the size of economies.

Making the GFA more inclusive will increase Africa's participation and amplify its voice and ownership of decisions taken in IFIs, in line with its growing importance on the global stage. It will also enhance the legitimacy and credibility of the IFIs. Coulibaly and Prasad (2023) argue that the IMF has an archaic governance structure because the distribution of quotas among its member countries does not reflect today's economic realities. The IMF has indeed started a process of reforms: the Board of Governors of the IMF completed the 16th General Review of Quotas on December 15, 2023, which would provide for a 50 percent quota increase.[81] Further proposals include possible approaches for quota realignment, including a change in the formula used to determine quotas, which has been deferred to the 17th General Review of Quotas scheduled for June 2025.

Building consensus on a change accommodating additional voices and ownership of processes in international fora, especially during this period of mounting geopolitical competition, is likely to be challenging and take a long time to conclude, as will reaching agreement on proposals to change quota allocations and/or shareholding and associated voting rights in MDBs. Most of the alternative formulas recommended for calculating quotas and voting rights point to a sharp increase in China's voice, mostly by diluting those of some leading economies.

The likely protracted process in completing IMF quota realignment should however not stall implementation of other equally important reforms. One such reform suggested by Coulibaly et al. (2024) is adopting a double majority rule in voting (a majority of voting rights and member countries). The other is to further expand the G20 by adding more African countries, to make Africa's participation more reflective of its population.

It should be possible to immediately agree on a double majority rule for some IFI decisions. Such a reform would not change the various countries' shares and voting rights. It would still mean that countries holding majority shares in an IFI could veto a decision, even if most member states supported it. The concept of double majority is already applied for some decisions at the IMF: a super double majority is required to change its articles of agreement, for example.

Implementing a double majority rule could also raise Africa's voice. While it could slow the voting process, it would increase an IFI's credibility, as it gives more weight to smaller and weaker members.[82] To minimize delays in decisionmaking, the rule could be a simple majority of shares and a simple majority of member states.

Another proposal, by the recent Bretton Woods Committee report, relates to forming ministerial-level councils in both the IMF and World Bank, with decisionmaking powers over issues pertaining to the global commons that will require international public sector action.[83] This could be quickly achieved by strengthening the powers of two institutional ministerial-level bodies that already exist—the joint Development Committee (DC) and the IMF's International Monetary and Financial Committee (IMFC), which are advisory and do not possess structured, binding decision-making authority. These two councils could meet annually to foster institutional and international collaboration.[84] The IMFC agreed in October 2023 to the creation of a 25th chair on the IMF Executive Board for Sub-Saharan Africa.[85] It is however important that African countries ensure that their representatives to IFI boards have the seniority, political weight, technical experience, and knowledge to command the respect of their peers, while working to strengthen the IFIs and enhance their own credibility.

The G20 is similar in a way to an "economic security council." It includes all members of the G7 and all original members of the BRICS, as well as Argentina, Indonesia, South Korea, Mexico, Saudi Arabia, and Turkey. The addition of the African Union as a full member is therefore a welcome initiative, but the African continent remains under-represented with South Africa as the only sovereign member of the group. Admitting more African countries as sovereign members would further enhance Africa's participation in global policy discourse and decisionmaking.

In the longer term, African countries also need to put in place growth-enhancing policies that will increase the size of their economies relatively on the world scene. If Africa were to represent around 6–10 percent of world GDP in 2033 (the end of the second, 10-year implementation plan of Agenda 2063), up from 2.9 percent in 2022, the continent's influence and participation globally would be further enhanced.

Implementing a double majority rule in international financial institutions (IFIs) could raise Africa's voice. While it could slow the voting process, it would increase an IFI's credibility, as it gives more weight to smaller and weaker members

The importance of regional organizations has increased over the last several decades. Coulibaly and Sidiropoulos (2022) show how they can be more effective than global institutions in dealing with certain issues that require a deeper knowledge of a region. Actions to strengthen these regional and national institutions could therefore be needed, as well as clear subsidiarity agreements between global and regional institutions, to ensure adequate responsiveness to regional and global challenges.

Resources mobilized through the reform of the GFA could be channeled through regional MDBs, which focus their financing on scaling up investments in core areas such as the AfDB's High 5 priorities needed to foster structural transformation and to achieve the SDGs and Agenda 2063. Indeed, according to the United Nations Development Programme, effective implementation of the High 5 priorities could result in achieving both Agenda 2063 and the SDGs to a level of about 90 percent.[86]

Resources mobilized through the reform of the global financial architecture could be channeled through regional multilateral development banks, which focus their financing on scaling up investments in core areas such as the African Development Bank's High 5 priorities

Finally, African countries should consider earmarking a sizable share of the increased funding to be mobilized from the reforms of the GFA for investment in soft and hard infrastructure, human capital, and technology, in line with endogenous national development plans and aspirations of Agenda 2063. This alignment between GFA reforms and structural transformation would make the reconfigured system more relevant to Africa.

THE WAY FORWARD—A CAVEAT AND SEVEN KEY RECOMMENDATIONS TO ACCELERATE STRUCTURAL TRANSFORMATION IN A CHANGING GLOBAL ENVIRONMENT

A caveat

Key recommendations on what countries need to do to address climate change and leverage the private sector for green transitions have already been highlighted in the AfDB's 2022 and 2023 editions of the *African Economic Outlook* report.[87] Key policies that can drive structural transformation in African countries even with a changing GFA are articulated in chapter 2 of this report.

Implementing the following GFA reforms could however unlock substantial capital for development in Africa, but they should not be considered a panacea. The continent also needs to capitalize on domestic opportunities and positive elements already in the current GFA.

Seven key recommendations

1. **Accelerate and scale up the mobilization of long-term and affordable concessional finance for Africa's structural transformation.** Structural transformation is a long-term process, and the dividends also take time to come through. In the short run, five reform proposals that can help mobilize concessional resources at scale for transformation stand out:
   - *Rechannel the IMF SDRs to MDBs to leverage more resources for structural transformation in Africa.* Rechanneling and leveraging $100 billion-worth of SDRs could increase low-cost financing for Africa by anywhere between about $12 billion and $46 billion a year over the next 10 years.
   - *Make healthy replenishments of the concessional windows of the AfDB (the African Development Fund, ADF) and the World Bank (the International Development Association).* ADF countries will need about $245 billion a year for investment across the four key sectors to accelerate structural transformation over the three-year ADF-17 replenishment cycle. This would facilitate access to low-cost concessional resources to enable low-income countries in Africa catch up with their relatively high performing peers in other developing regions.
   - *Reform global tax governance to make it more transparent and accountable.* Reforms would help contain illicit financial flows and tax evasion and avoidance, as well as profit-shifting, which costs African countries about 1 percent of their GDP—the same as total net international inward transfers in 2022. Similarly, measures to enforce greater extractives transparency are crucial, including the Extractive Industries Transparency Initiative, which requires compulsory disclosure of all transactions by global

corporations and governments in Africa and other developing regions.

- *Maximize MDB funding capacity by implementing the G20's Capital Adequacy Framework (CAF) and the Triple Agenda.* The CAF identifies ways to maximize MDB funding capacity by, for example, optimizing their balance sheets and making the five strategic shifts highlighted in this chapter. The Triple Agenda recommends a three-pronged approach to reforming the MDBs. The G20 also recommends a generalized capital increase for institutions facing a binding headroom constraint.
- *Improve the scale of financing and transparency of bilateral creditors.* Accounting for 20 percent of Africa's external debt in 2022, resources from bilateral lenders and transparency on their loans should be increased, with voluntary disclosure of information on lending terms, to avoid exacerbating debt vulnerability.

2. **Reform the global debt architecture to make it more transparent, nimble, accessible, and affordable to developing countries.**
   - *To facilitate debt restructuring there is a need to:* (i) develop market-based solutions for unsustainable eurobonds; (ii) implement debt relief to free resources for climate actions; (iii) create a sovereign debt authority and a sovereign insolvency system; (iv) G20 countries could consider legislation that encourages private lenders to participate in debt workouts; (v) create opportunities for MDBs to lend to countries during protracted debt negotiations by implementing the policy of lending in arrears; (vi) further support African capacity development in debt productivity and public financial management; (vii) improve the IMF–World Bank Debt Sustainability Framework (DSF) to make it adaptable to new economic realities; and (viii) improve the credit ratings by private agencies.
   - *The IMF and World Bank should work with other MDBs, including the AfDB, to improve their debt sustainability analyses.* This should include updating the current DSF to reflect the changing structure of economies, and the impact of shocks on economies, especially those in Africa.
   - *The IMF–World Bank DSF methodology for assessing debt sustainability should be made publicly available to make it easy to replicate and independently validate the findings.* The DSF also needs to consider climate risks, loss, and damage, as well as the resources needed to scale up investment in climate resilience, the transition to a green economy, increased defense spending to curb threats of insurgence, and delivery of regional and global public goods.
   - *MDBs like the AfDB could work with international credit rating agencies to strengthen methodologies for assessing sovereign risk and help reduce the amount of subjectivity in Africa's credit ratings.* This will reduce the perceived risk of private investment in African countries. Similarly, African countries should engage with these agencies to provide timely data and clarify the risk perceptions assigned to them, so as to mitigate the apparent subjectivity. State-contingent debt instruments can also help reshape Africa's public debt risks in a world characterized by rising macroeconomic uncertainty.

3. **Strengthen climate finance accessibility for vulnerable countries that need it most.** The misalignment of climate finance architecture with climate vulnerability, cumbersome procedures, and low institutional capacity in most African countries limit the flow of global climate finance to Africa. There is need to simplify the climate finance procedures to make it more accessible to the climate-vulnerable countries that also have limited capacity to fulfill complicated and expensive project preparation procedures. The launch of the Loss and Damage Fund announced at COP27 in Egypt has attracted about $661 million in pledges as of March 2024. While positive, its future scale should match the immense losses from climate-induced events in countries: a recent UN-commissioned report suggests that $150 billion–$300 billion may be needed

Multilateral development banks could work with international credit rating agencies to strengthen methodologies for assessing sovereign risk and help reduce the amount of subjectivity in Africa's credit ratings annually by 2030.[88] Leveraging initial financing of the AfDB's Climate Action Window, launched during ADF-16, with additional resources from both public and private sources will bolster the flow of climate finance to address climate vulnerability and risk in Africa.

4. **Adopt reforms to improve Africa's access to emergency financing facilities.** Lacking fiscal capacity, most African countries address temporary shocks by borrowing to smooth consumption and investment and to avoid sharp economic fluctuations. Reforms of the GFA need to increase Africa's access to financial safety nets, and: (i) delink access to IMF financing from quotas; (ii) introduce state contingent clauses in the loan agreements with the IFIs; and (iii) create an African emergency finance facility/financial stability mechanism or institution. African countries should also implement reforms to strengthen and deepen domestic financial systems so that eventually these can become their own real cushion against shocks.

Measures to incentivize private finance for climate and green growth in Africa are critical for structural transformation in Africa

5. **Make the governance of the GFA more inclusive to enhance Africa's participation and voice.** The IMF has started a process of reforms aimed at increasing Africa's participation. For example, its Board of Governors completed the 16th General Review of Quotas on 15 December, 2023, which provided for a 50 percent quota increase.[89] Further reforms include proposals to explore approaches for quota realignment. In addition, using a double majority rule could improve the participation of member countries in decisionmaking. Another proposal, by the recent Bretton Woods Committee report, relates to forming ministerial-level councils in both the IMF and World Bank with decisionmaking powers over issues pertaining to the global commons that will require international public sector action.[90] This could be quickly achieved by strengthening the powers of two institutional ministerial-level bodies that already exist—the joint Development Committee and the IMF's International Monetary and Financial Committee, which are advisory and do not have structured, binding decisionmaking authority. These two councils could meet annually.[91] The addition of the African Union as a full member in the G20 is a welcome initiative, but the African continent remains underrepresented with South Africa as the only sovereign member of the group. Admitting more African countries as sovereign members is recommended. For the longer term, African countries need to implement growth-enhancing policies (chapters 1 and 2) that will increase the size of their economies and amplify the continent's voice in the GFA.

6. **Implement a mandatory requirement for countries to adopt policies for greening their GDP.** Africa's abundant natural resources present an opportunity for economic transformation toward greener growth. Yet, the current economic valuation framework often fails to capture the full extent of the continent's wealth. Africa's reliance on natural capital, such as oil, minerals, and forests, has fueled economic growth but also led to unsustainable extraction and environmental degradation. A mandatory update of methodologies for measuring the wealth of countries to include their green wealth—the economic value of natural capital and associated ecosystem services they provide—should be introduced and enforced. This approach will ensure that Africa leverages its natural capital to expand the size of its economy, increase risk profile to mobilize resources in international capital markets to finance structural transformation.

7. **Leverage private sector financing for transformation and climate justice.** The scale of public resources that can be mobilized through a scaling up of domestic revenue mobilization and concessional financing from official multilateral and bilateral creditors to support Africa's structural transformation to meet the SDGs and Agenda 2063 in the near term will be very modest relative to the scale of resources required, even in the best-case scenarios. The private sector offers significant opportunities to fill the resource gap. Measures to incentivize private finance for climate and green growth in Africa are therefore critical for

structural transformation in Africa.[92] Reforms of the GFA could support asset recycling by transferring existing assets of debt distressed countries to the private sector to generate funding for infrastructure and other catalytic projects to accelerate structural transformation. Reforms could also embed mechanisms for a portfolio-based approach toward private sector investment rather than a project-by-project approach to leverage economies of scale and existing synergies of projects within the same portfolio than projects managed in silos can achieve.

NOTES

1. G20 Eminent Persons Group on Global Financial Governance 2018.
2. G20 Eminent Persons Group on Global Financial Governance 2018.
3. AfDB 2022, 2023.
4. According to UNCTAD (2018), the Global South comprises Africa, Latin America and the Caribbean, Asia (excluding Israel, Japan, and South Korea), and Oceania (excluding Australia and New Zealand).
5. https://am.afdb.org/en/news/high-level-presidential-dialogue-changing-global-financial-architecture-and-role-multilateral#:~:text=This%20is%20even%20more%20evident,of%20international%20trade%20remain%20below.
6. AfDB 2023.
7. AfDB 2023.
8. https://www.ifw-kiel.de/topics/war-against-ukraine/ukraine-support-tracker/?cookieLevel=not-set.
9. Other multilateral creditors include several MDBs, collectively accounting for about 11 percent of total multilateral debt owed by African countries in 2022.
10. Cohen et al. 2024.
11. AfDB 2023. This means that for every dollar of public climate finance, African countries mobilized only $0.16, the lowest share among world regions. In North America, the leverage ratio is $18.50, and in South Asia and Latin America, at least $0.50.
12. AfDB 2023.
13. Kelhoffer 2020.
14. OECD 2023.
15. https://www.un.org/en/un75.
16. United Nations 2021.
17. https://www.un.org/en/common-agenda/summit-of-the-future. The UN has called for a Summit of the Future to take place on September 22–23, 2024, with Germany and Namibia acting as co-facilitators. This will bring together world leaders to forge a new international consensus on how to deliver on humanity's broad objectives as defined in key documents like the UN Charter, the Universal Declaration of Human Rights, the 2030 Agenda, the SDGs, and the Paris Agreement.
18. United Nations 2023.
19. G20 Eminent Persons Group on Global Financial Governance 2018.
20. G20 2022.
21. G20 2023.
22. IEG 2023.
23. See G20 (2023, p. 14).
24. UNECA 2023.
25. https://philanthropynewsdigest.org/news/other-sources/article/?id=14911972&title=19-African-Heads-of-State-call-for-$120bn-IDA21-replenishment.
26. For example, see Coulibaly and Dervis (2022) and Prizzon et al. (2022).
27. https://pmo.gov.bb/wp-content/uploads/2023/10/Bridgetown2.0-2pager-2.pdf.
28. https://www.imf.org/en/Topics/special-drawing-right/2021-SDR-Allocation.
29. This means that $100 billion in SDRs rechanneled through the AfDB could deliver up to $400 billion in new financing for African countries, covering the financing required for accelerated structural transformation in Africa.
30. IMF 2024a.
31. So, for the entire 3-year ADF cycle, the total financing gap is estimated to be $735.9 billion, reflecting the large number of ADF countries in Africa, many of which are significantly below the threshold of high performing developing countries in other regions on the key identified areas relevant to accelerate structural transformation.
32. Okunogbe and Santoro 2023.
33. Okunogbe and Santoro2023.
34. See https://www.afdb.org/sites/default/files/2023_05_27_inauguration_lecture_nigeria_president_akinwumi_adesina.pdf.
35. Okunogbe and Tourek 2024.
36. Okunogbe and Tourek 2024.
37. Ali et al. 2015
38. Okunogbe and Tourek 2024.
39. Garcia-Bernardo and Jansky 2021.
40. Debrun and Kinda 2014; AfDB 2015.
41. Comelli et al. 2023.
42. A description of the MPA is found in IMF (2020).
43. IIF 2019.
44. For more on the OECD's debt transparency initiative, see OECD (2022).
45. See IMF (2023).
46. The World Forum on Natural Capital defines natural capital as the stock of natural resources, which includes geology, soil, air, water, and all living things. It underpins the economy and society and thus makes human life possible. Some natural capital

provides people with free goods and services, usually referred to as ecosystem services. See https://naturalcapitalforum.com/about/.
47. AfDB 2023.
48. Georgieva 2023a.
49. Guzman et al. 2022.
50. Gbohoui et al. 2023
51. APRM 2024.
52. Coulibaly and Abedin 2023a.
53. Canuto et al. 2023.
54. Krueger 2002; UN 2009.
55. For more on the potential statutory options to encourage private sector participation in debt workouts, see World Bank (2022).
56. Coulibaly and Abedin 2023c.
57. IMF 2024b.
58. IMF 2024b.
59. IMF 2024b.
60. Archibong and Annan 2023; Carleton and Hsiang 2016.
61. AfDB 2022.
62. AfDB 2023.
63. Disasters in the EM-DAT database are defined as situations or events that overwhelm local capacity, necessitating a request for external assistance at the national or international level.
64. Guzman et al. 2022.
65. Archibong 2024.
66. IEA 2022; Songwe 2023.
67. AfDB 2023.
68. AfDB 2023.
69. Archibong and Annan 2023.
70. https://www.afdb.org/en/topics-and-sectors/initiatives-and-partnerships/african-green-banks-initiative#:~:text=What%20is%20the%20African%20green,sustainable%20growth%20in%20the%20continent.
71. AfDB 2023.
72. AfDB 2023.
73. ACMI 2023.
74. Netshitumbu 2023.
75. ACMI 2023.
76. Bedair et al. 2023.
77. Guepie et al. 2023.
78. Mustapha et al. 2023.
79. Volz 2021.
80. Japan's exact share of voting rights at the IMF is 6.14 percent.
81. Georgieva 2023b.
82. The Council of the EU applies a double majority (qualified majority) rule for some of its decisions. For a decision to pass, it needs the support of 55 percent of EU member states representing at least 65 percent of the bloc's population.
83. Bretton Woods Committee n.d.; Levy et al. 2024.
84. Levy et al. 2024.
85. Levy et al. 2024.
86. UNDP 2017.
87. AfDB 2022, 2023.
88. UNCTAD 2023.
89. Georgieva 2023b.
90. Bretton Woods Committee n.d.; Levy et al. 2024.
91. Levy et al. 2024.
92. AfDB 2023.

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COUNTRY NOTES

CENTRAL AFRICA

Cameroon

Recent macroeconomic and financial developments

The economic growth rate rose from 3.6% in 2022 to 3.8% in 2023 thanks to the good performance of the forestry and logging sector and the dynamism of the services sector. On the demand side, growth was driven mainly by private investment. Inflation, which stood at 6.3% in 2022, rose to 7.4% in 2023, driven by food prices, which rose 11.1%.

The budget deficit improved from 1.1% of GDP in 2022 to 0.9% in 2023 due to greater rationalization of public spending, policies aimed at broadening the tax base (from the current tax burden of 12.6% of GDP, and rising oil prices. Public debt fell from 45.3% of GDP in 2022 to 41.8% in 2023, though the International Monetary Fund still classifies the country as being at high risk of debt distress. The current account deficit narrowed from 3.4% of GDP in 2022 to 2.7% in 2023 due to improved primary income balances and increased gas production. The quality of the banking system's portfolio deteriorated slightly, with the gross delinquency ratio rising from 13% to 15.4% between end-2022 and mid-2023. But the equity ratio rose from 15% to 16.3% over the same period.

According to the World Bank, among the economically active population, the $2.15 a day poverty rate was an estimated 23% in 2023, and the unemployment rate was an estimated 3.7%, due to weak economic growth.

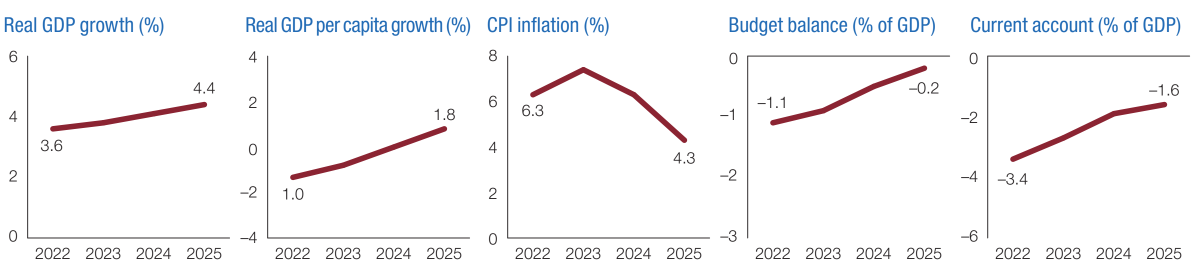
Outlook and risks

GDP growth is projected to reach 4.1% in 2024 and 4.4% in 2025 thanks to a gradual increase in domestic gas production and higher world commodity prices. Inflation is projected to fall to 6.3% in 2024 and 4.3% in 2025 due to the continued tightening of monetary policy by the Bank of Central African States. The budget deficit is projected to further improve to 0.5% in 2024 and 0.2% in 2025 thanks to continued tax reforms and rationalization of public spending. The current account deficit is also projected to improve to 1.9% in 2024 and 1.6% in 2025 as gas exports continue to increase. Risks of this growth outlook are linked to Russia's invasion of Ukraine and the Israel–Hamas war, with negative consequences for product supply chains, as well as a possible resurgence of social tensions within the country.

Reform of the global financial architecture

Structural transformation has been slow. Between 2000 and 2023, there was a net increase in the contribution of the services sector to GDP, from 44.3% to 51.9%, at the expense of the industrial sector, whose hare declined from 34.1% of GDP to 25%. The structure of employment changed considerably between 1990 and 2019, with a net decrease in the share of employment in the agricultural sector from 70% in 1990 to 43% in 2019, while the share in services rose from 20% to 42%. The share of employment in industry remained largely stable over the period.

To ensure structural transformation, the country must step up efforts to mobilize not only domestic resources but also the concessional external resources needed to finance energy and transport infrastructure projects at affordable rates. Reforming the global financial architecture to increase Africa's decisionmaking power in the major international financial institutions is imperative. This will enable Africa's priorities to be better taken into account, especially with respect to access to stable, long-term resources. For Cameroon, a Congo Basin country rich in natural resources, such reform would enable better valorization of its natural capital, revalue its national wealth, and provide access to additional financial resources, notably from a potential carbon market.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Central African Republic

Recent macroeconomic and financial developments

Although weak since 2020, economic growth has picked up slightly, from 0.5% in 2022 to 1% in 2023. On the supply side, this slight recovery was driven by the agriculture sector (up from 0.3% in 2022 to 1.2% in 2023). The industrial sector recorded growth of 0.5%, up from a decline of 0.8% in 2022, and the services sector a growth of 0.7%, up from 0.6%. Sectoral contributions to GDP were 52% for agriculture, 23% for industry, and 25% for services. On the demand side, growth was driven by final consumption (up 15.6%). Investment (up 0.9%) was limited by insufficient domestic and external financing. Inflation fell from 7.9% in 2022 to 5.6% in 2023 thanks to recovery in agricultural production and fuel price subsidies since July 2023.

The budget deficit narrowed from 5.4% of GDP in 2022 to 3.7% in 2023, reflecting the gradual modernization of public revenue collection. But the risk of external and global debt distress remains high, with the debt-to-GDP ratio at 49% in 2023. The current account deficit narrowed from 12.4% of GDP in 2022 to 8.5% in 2023 thanks to favorable balances in primary and secondary income accounts. The financial sector was marked by increased deposits (10.7%) in 2023. Nonperforming loans rose from 15.5% of gross loans in December 2022 to 16.4% in December 2023.

Poverty remains widespread. 68% of the population (4.2 million people) lives below the national poverty line (with €401 in annual income), and 10% of the non-poor population is vulnerable to poverty and likely to become poor in the event of a shock. Unemployment stands at 28% for men and 42.5% for women, and the Gini coefficient is 43.

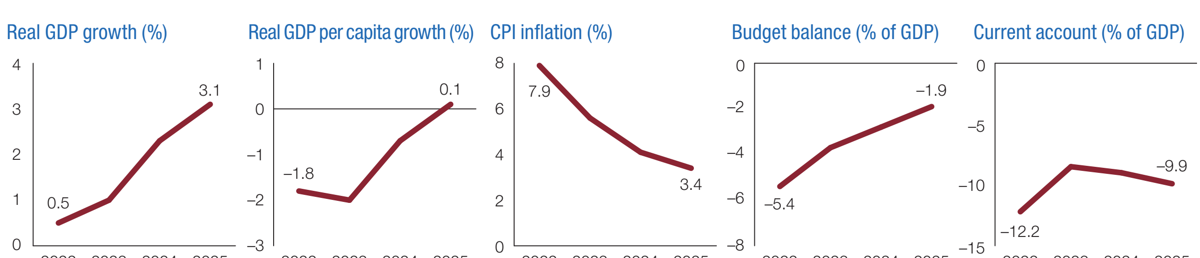
Outlook and risks

Economic recovery is projected to continue, with growth of 2.3% in 2024 and 3.1% in 2025 and inflation of 4.1% in 2024 and 3.4% in 2025. Likewise, prospects for reducing the public deficit are improved by measures under way to substantially boost domestic revenue mobilization through ongoing reforms, notably those affecting both tax and nontax revenues. Tailwinds for this outlook include consolidation of peace and internal security, improvements in energy and fuel supplies, and acceleration of implementation of ongoing projects, notably the Pointe-Noire–Bangui Corridor financed by the African Development Bank.

Reform of the global financial architecture

The economy remains heavily dependent on agriculture. Its contribution to GDP fell from an average of 42% over 2001–2010 to 35% over 2011–2020, while that of the services sector rose from 33% to 40% and that of the industrial sector remained mostly stable at 25% and 22%. Agriculture employs 70% of the workforce, and services employs 22%. This dynamic is strongly influenced by multiple conflicts that have led to the destruction of the capital stock that could have contributed to structural transformation.

To relaunch structural transformation, the country needs to improve its institutional governance and natural resources management, mobilize domestic and external resources without compromising debt sustainability, and boost overall factor productivity, particularly human capital. This would allow the landlocked country to take advantage of the opportunities under the African Continental Free Trade Area by industrializing by integrating into regional value chains. Achieving these ambitious aims will require substantial resources. Reforming the global financial architecture could facilitate access to financing opportunities offered by financial products based on valorizing natural resources, such as green bonds, and could encourage the establishment of a regional carbon market. To achieve this, the country will need a strategy for valuing and transforming its natural resources.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Chad

Recent macroeconomic and financial developments

The economic growth rate stood at 4.3% in 2023, up from 3.4% in 2022, driven on the supply side by the oil sector (up 13.3% in 2023) and on the demand side mainly by net exports (up 7.4% in 2023). Inflation eased from 5.8% in 2022 to 4.8% in 2023, above the Economic Community of Central African States (ECCAS) target of 3%, fueled by high food prices (18.8% at end-December 2023).

The budget balance, in surplus since 2022, was 4.8% of GDP in 2023, due to an exceptional increase in oil revenues. The debt-to-GDP ratio was 20.5% in 2022. The country has benefited from the Group of 20's (G20) Debt Service Suspension Initiative and, in November 2022, reached an agreement in principle through the G20 Common Framework on close to $3 billion of debt. In 2022, public debt servicing fell to 5.7% of GDP, and the risk of debt distress is expected to be moderate in the medium term. The current account surplus improved from 5.9% of GDP in 2022 to 1.8% in 2023, underpinned by strong growth in oil exports. The banking system remains fragile. Bad debts accounted for 39.7% of total bank loans in 2023, up from 36.1% in 2022, and the risk coverage ratio was 5.8% in 2022, down from 9% in 2021.

The national incidence of poverty is 42.3%, and the Gini coefficient is 0.34. The unemployment rate was 18.5% in 2018, according to the country's National Institute of Statistics, Economic and Demographic Studies. Because of the Covid-19 pandemic, the extreme poverty rate rose from 31.2% in 2018 to 34.9% in 2021 and 35.4% in 2023, according to the World Bank.

Outlook and risks

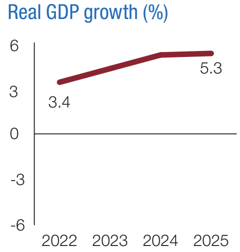
The economic outlook remains favorable, with projected growth of 5.2% in 2024 and 5.3% in 2025, driven by the buoyant oil sector. On the demand side, growth drivers are investment and exports. Inflation could fall to 3.4% in 2024 and to 3.2% in 2025, remaining above the ECCAS target of 3%. The budget balance is projected to be in surplus, at 2.7% of GDP in 2024 and 2.2% in 2025. Over the same period, the current account balance is also projected to remain in surplus, at 1.3% of GDP in 2024 and 0.8% in 2025, due to higher oil exports. The main risks to the medium-term macroeconomic outlook are possible tensions following the 6 May 2024 presidential election, subregional insecurity, volatile world oil prices, global geopolitical crises, and climate change impacts. Conclusion of the third review of the program signed with the International Monetary Fund in 2021 and supported by an Extended Credit Facility will further strengthen the macroeconomic framework, increase mobilization of nonoil fiscal resources, and improve debt sustainability.

Reform of the global financial architecture

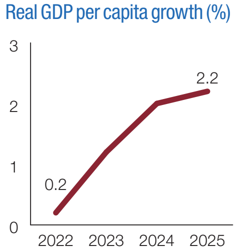
From 2005 to 2023, agriculture accounted for almost 50% of GDP, followed by services and industry. Economic diversification is now the centerpiece of the country's development strategy, particularly in the agricultural sector, which has immense potential for creating value chains. In 2022, the agricultural sector (farming and livestock breeding) accounted for an average 25% of GDP and employed 69% of the working population. Services accounted for 21% of employment, and industry for 9.6%. But the pronounced shortfalls in agricultural production, energy, transport, and infrastructure development are major impediments to inclusive and sustainable growth. Added to these are constraints linked to climate change, which is affecting the ecological balance of some of the country's regions, specifically arid regions, and the livelihoods of people who depend heavily on livestock breeding and rain-fed agriculture.

To finance and accelerate structural transformation, the country could take advantage of its enormous natural capital, valued at $75.4 billion, to mobilize more international financing. Better access to both public and private climate financing (green bonds), substantial concessional resources, and innovative financing, such as partial risk guarantees, would help the country meet the enormous financing needs of the National Development Plan 2024–2028, estimated at $22.25 billion, including $4.33 billion to be raised from the international financial community.

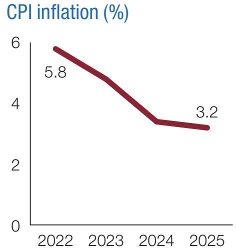
Real GDP growth (%)



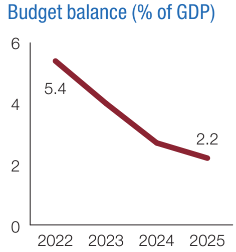
Real GDP per capita growth (%)



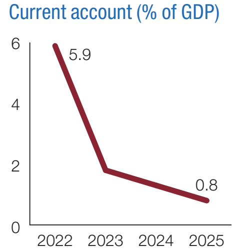
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Democratic Republic of Congo

Recent macroeconomic and financial developments

The economic growth rate fell from 8.8% in 2022 to 7.5% in 2023, due to underperformance in extractive industries (where the growth rate fell from 22.3% in 2022 to 15.4% in 2023). Growth in nonextractive sectors rose from 3.1% in 2022 to 3.6% in 2023, driven by agriculture (up 0.45%), construction and public works (up 0.57%), and transport and telecommunications (up 0.61%). Growth was also supported by exports (up 17.3%) and investment (up 9.2%). Inflation rose from 9.3% in 2022to 19.9% in 2023, due to the Congolese franc's depreciation against the US dollar (down 21.8%) and constraints on food and energy supplies. As a result, the central bank has kept its prime rate at 25% since August 2023 to curb the monetary depreciation caused by budget deficit financing.

The budget deficit rose from 0.5% of GDP in 2022 to 1.7% in 2023 due to a 56.4% increase in exceptional spending (security and elections), despite a 5.4% increase in revenue and grants in 2023 (13.6% of GDP). The country faces a moderate risk of debt distress, with the public debt-to-GDP ratio falling from 22% in 2022 to 21.5% in 2023, and external debt rising from 14.8% of GDP in 2022 to 17.8% in 2023. The current account deficit widened from 4.9% of GDP in 2022 to 6.3% in 2023, driven by deteriorating terms of trade (–8.1%) and high imports. International reserves increased by 18% to 2.8 months of import cover in 2023. With the re-establishment of credit criteria by the central bank, the nonperforming loans ratio fell from 7.4% in 2022 to 6.5% in 2023.

The government is targeting inclusive growth and reduced inequality. The Gini coefficient was 0.511 in 2020, the poverty rate was 56.2%, and underemployment was 15.1%.

Outlook and risks

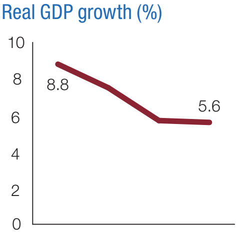
Growth prospects for the economy are projected to remain favorable, at 5.7% in 2024 and 5.6% in 2025, driven by the mining sector, construction and public works, and trade. Inflation is expected to fall to an average of 13.5% over 2024–25, in line with the central bank's restrictive policy. The budget deficit is projected to rise to 2% of GDP in 2024 as postelectoral institutions are installed and to fall to 1.1% in 2025. The strategy for clearing certified domestic arrears ($2.4 billion) is operational, and the average debt-to-GDP ratio is expected to remain below 20%. The current account deficit is projected to improve to an average of 4% of GDP due to foreign direct investment. Cumulative reserves are expected to reach $6.1 billion, or 2.3 months of import cover. Upside risks include uncertainties linked to Russia's invasion of Ukraine, the Israel–Hamas war, falling commodity prices, inflationary and foreign exchange tensions, and insecurity in the east of the country, with the looting of minerals. Solutions for carrying out structural transformation and improving GDP per capita (currently $731.3) include coordinating fiscal and monetary policies, implementing structural investments (in particular industrialization and agricultural transformation programs), and pursuing structural reform.

Reform of the global financial architecture

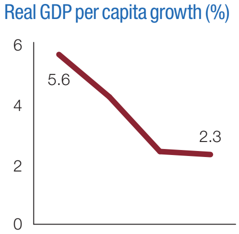
Structural transformation is slow and remains a major challenge. Over 2005–20, agriculture's share of employment fell from 71.1% to 60%, while industry's share rose from 7% to 10.7%. Services' share climbed even more, from 22% to 29.3%. Employment is shifting from agriculture to industry and services due to the low productivity of agricultural jobs, a large informal sector, and the dominance of the capital-intensive mining sector. Capital accounts for 82% of production inputs and labor for 18%. Constraints to structural transformation include border insecurity, infrastructure challenges, an unattractive business environment, and weaknesses in human capital, institutions, governance, and financing.

Financing problems are hampering structural transformation. To cover its development needs, the country would gain most by pursuing better governance of its natural capital and financial resources and would thus benefit from reform of the global financial architecture. The country could benefit from concessional financing and innovative financing windows (climate funds). But speeding up structural reforms by abolishing unfair mining contracts, improving public revenue and spending efficiency, and invigorating the business climate to take advantage of foreign direct investment and regional integration is expected to bring more financing for the country's structural transformation.

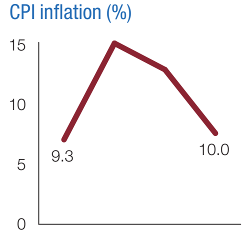
Real GDP growth (%)



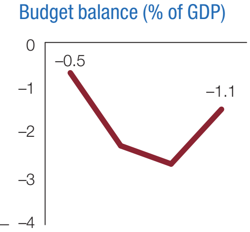
Real GDP per capita growth (%)



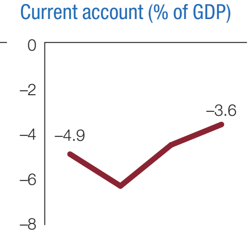
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Republic of Congo

Recent macroeconomic and financial developments

The economic recovery strengthened in 2023, with growth of 3.9%, up from 1.7% in 2022. This was driven by the strong performance of the oil sector (up 1.4%) thanks to higher oil prices, as well as the nonoil sector (up 2.8%), with good dynamism in the agricultural sector (up 5.7%), especially food crops. On the demand side, growth was underpinned by domestic consumption (up 5.6%), the clearance of government arrears, and public investment spending (up 6.6%). Monetary policy was accommodating, enabling credit to the economy to grow 11.1% in 2023. Inflation stood at 4.1% in 2023, up from 3.3% in 2022, in line with the adjustment in fuel prices and rising domestic demand.

The country recorded a budget surplus of 4.2% of GDP in 2023, down from 8.9% in 2022, as a result of fiscal discipline and major reforms such as the 30% increase in fuel prices at the pump. The public debt-to-GDP ratio, up from 92.5% in 2022 to 96% in 2023, is considered sustainable. But the country still faces debt overhang due to the accumulation of temporary external arrears and the unfinished restructuring of domestic arrears. The current account posted a surplus of 3.5% of GDP in 2023, down 15 percentage points from 2022. Foreign exchange reserves stood at 2.6 months of import cover, up from 1.5 in 2022. On the financial front, overdue receivables were up 1.4% in 2023.

Though economic activity has picked up, stronger, more inclusive growth is needed to reduce the estimated rates of poverty (46.8% in 2023) and unemployment (21.8%).

Outlook and risks

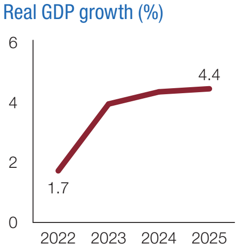
Economic growth is projected to accelerate to 4.3% in 2024 and to 4.4% in 2025 on increased oil production, planned investments in the gas sector, and planned clearance of the state's arrears to national economic operators. Inflation is projected to fall to 3.4% in 2024, slightly above the Central African Economic and Monetary Community (CEMAC) target of 3%, in anticipation of improved food supplies in the domestic market. The budget surplus is projected to reach 4% of GDP in 2024 and 2.6% in 2025 thanks to improved revenue and partly financed by the issuance of government securities on the regional market. The current account is expected to remain in surplus, at 3.2% of GDP in 2024 and 2.3% in 2025, due to increased oil and gas exports. However, economic performance remains subject to a number of risks, including persistent insecurity in the subregion; volatile oil production and prices due to restrictive policies by the Organization of the Petroleum Exporting Countries plus other oil-producing countries, which may affect oil prices and supply; rising food prices; and unfavorable weather.

Reform of the global financial architecture

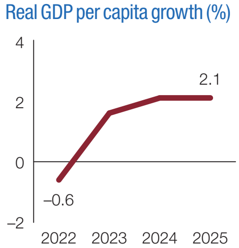
Structural transformation has not yet occurred. Services, at 47.1% of GDP, and industry, at 45.3% of GDP, dominate the economy, with agriculture accounting for just 7.6% of GDP. From 1991 to 2021, agriculture's share of employment declined from 43.3% to 33.5%, while services' share rose from 31.1% to 45%, and industry's share rose very slightly, from 21.5% to 25.7%. The main obstacles to economic transformation are dependence on oil, weak human capital, poor governance, and an unattractive business environment. Accelerating structural transformation will require investment in transport and energy infrastructure and skills development.

The major challenge for structural transformation remains financing. In addition to mobilizing more domestic resources (from the current tax burden of 10.7% of GDP), the country should use its considerable natural capital to generate additional resources. After it restructures its debt and benefits from the Group of 20's Debt Service Suspension Initiative, reforming the global financial architecture should enable it to benefit from more concessional financing through improved access to regional and global financing windows (notably climate funds and carbon and green bond markets).

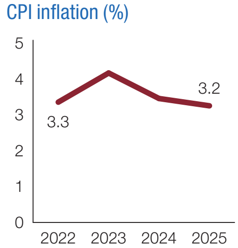
Real GDP growth (%)



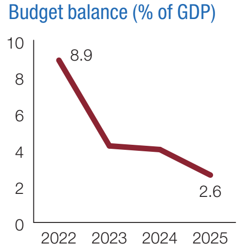
Real GDP per capita growth (%)



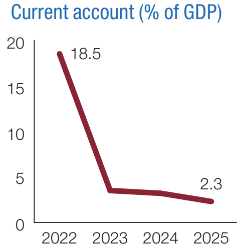
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Equatorial Guinea

Recent macroeconomic and financial developments

The economy went into recession in 2023, with real GDP contracting 5.7% after growing 3.7% in 2022, due to oil contracting to 12.8% of GDP in 2023 after growing 1.7% in 2022. Demand-side drivers were slowed by a 26.7% drop in net exports. Inflation fell from 4.9% to 2.5% in 2022, due to government measures to reduce prices (import of products resold at preferential prices). The monetary policy of the Bank of Central African States (BEAC) remained restrictive, with tighter bank refinancing conditions, a halt to liquidity injections, and larger liquidity withdrawals. These measures also helped curb inflation.

The budget recorded a 0.8% surplus in 2023, down from 11.9% in 2022, due to a 59% drop in oil tax revenue in 2023. The public debt-to-GDP ratio rose from 34.6% in 2022 to 42.1% in 2023, driven by domestic debt (31.9% of GDP). External debt servicing also rose from 4.3% of exports to 7.8% but remains low. The current account surplus shrank from 2.1% of GDP in 2022 to 0.9% in 2023, due to underperforming hydrocarbon exports (down 35%). As a result, international reserves stood at 5.4 months of import cover in 2023, down from 6.1 in 2022, but remain above the three-month target set by the BEAC.

Poverty was 76.8% in 2006 (the most recent data), and the Gini coefficient was 0.502. Provisional results from the second household survey are expected by the end of June 2024. The unemployment rate is 8.5%.

Outlook and risks

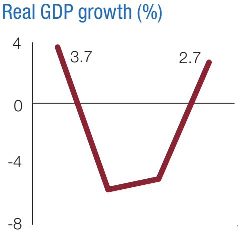
The recession is projected to continue, with GDP contracting 5% in 2024 and hydrocarbon production falling 6.3%. But development of new gas wells is expected to boost gas production by 2025. The budget balance is projected to improve in 2024 to a surplus of 2.7% of GDP, due to greater mobilization of nonoil revenue, but then to deteriorate in 2025 to a deficit of 3.7% of GDP. The current account balance is projected to continue to worsen, reaching a deficit of 3.5% of GDP in 2024 and 5.1% in 2025, driven by a structural deficit in the balance of services and income. Inflation is projected to rise to 4.7% in 2024, above the Economic Community of Central African States target of 3%, with the planned reduction in fuel subsidies, before falling back to 2.6% in 2025. The prospects of lower oil prices combined with aging oil fields and the consequences from the war in the Middle East and Russia's invasion of Ukraine present risks for the government's planned social programs.

Reform of the global financial architecture

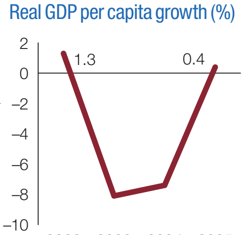
The country has undergone some structural transformation. Agriculture's share of employment fell from 55% in 1991 to 40% in 2019, while industry's share rose from 10% to 19% and services' share rose from 35% to 41%. The main challenges to structural transformation are a downward trend in labor productivity in the industrial sector, weak development of value chains, and low mobilization of internal resources in the nonoil sector.

To finance structural transformation, the country needs to rehabilitate the financial sector in the short term and reduce the share of hydrocarbons in the economy (42% of GDP, 95% of exports, and 90% of total revenue) in the medium and long terms. The country could benefit from reforms to the global financial architecture by enhancing the value of its natural capital to revalue its national wealth and make itself more solvent for its financial partners. The country could also implement a regional carbon exchange among the Congo Basin countries.

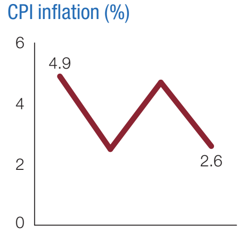
Real GDP growth (%)



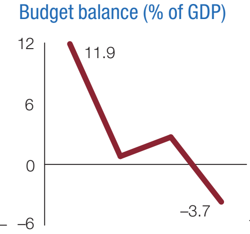
Real GDP per capita growth (%)



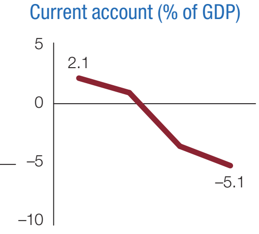
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



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Gabon

Recent macroeconomic and financial developments

The economic growth rate slowed from 3% in 2022 to 2.3% in 2023 thanks to an 18% drop in oil prices linked to weak international demand. Growth was driven on the supply side by strong performances in construction and public works (up 25.3%) and cash crop farming (up 17.3%) and on the demand side by government consumption (election-related spending). During 2023, the central bank's monetary policy remained restrictive, with tighter bank refinancing conditions, a halt to liquidity injections, and larger liquidity withdrawals. These measures helped bring inflation down from 4.3% in 2022 to 3.6% in 2023.

The budget balance swung to a 0.1% deficit after a 1.4% surplus in 2022, due to a greater increase in public spending (election-related expenses) than in revenue. The debt-to-GDP ratio at the end of 2023 was 57.4%, up from 54.3% in 2022. Debt servicing amounted to 53.1% of budget revenue in 2023, up from 47.4% in 2022, due to the size of eurobond refinancing maturing in 2025 and 2031. The current account surplus was estimated at 2.8% of GDP in 2023, an improvement from 0.9% in 2022, due to a decline in the trade surplus and a more pronounced deficit in services and income. International reserves fell to 2.7 months of import cover in 2023 from 3.3 in 2022.

In 2023, high rates of poverty (34.3%) and unemployment (21.5%), combined with substantial income inequality (Gini coefficient of 0.38), will maintain social divisions in a country where GDP per capita is among the highest in Africa.

Outlook and risks

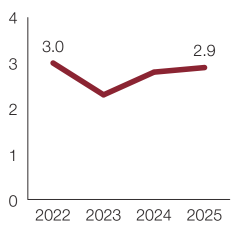
Economic growth is projected to accelerate slightly to 2.8% in 2024 and 2.9% in 2025, driven by the dynamism of the mining sector (manganese, iron) and public infrastructure investment. Inflation is projected to fall below the Economic Community of Central African States target of 3%, reaching 2.5% in 2024 and 2.3% in 2025, thanks to the central bank's restrictive monetary policy. The public budget deficit is set to further deteriorate, to 1.1% of GDP in 2024, before improving to 0.7% in 2025, due to increased government spending (salaries, capital expenditure). The current account balance is projected to improve in anticipation of higher prices for exported materials (oil, manganese, wood, and the like), swinging to a deficit of 0.9% of GDP in 2024 before returning to a surplus of 0.5% in 2025.However, this economic performance depends on developments in the national political and institutional situation following the coup of 30 August 2023 and on the state's capacity to mobilize resources, both internally and externally. Short-term growth could also be influenced by geopolitics in the Middle East as well as restrictive policies by Organization of the Petroleum Exporting Countries and other oil-producing countries, which will affect the price and supply of oil.

Reform of the global financial architecture

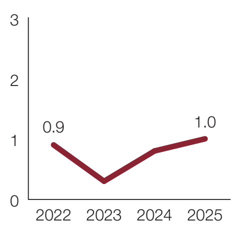
The Gabonese economy has begun a structural transformation but is proceeding slowly. Over 1992 to 2022, agriculture's share in employment fell from 44% to 29%, industry's share rose from 9% to 16%, and services' share rose from 46% to 55%. But productivity in the services sector and employment in industry are too low for the economy to benefit from these changes. The main obstacles to economic transformation are inadequate infrastructure, overdependence on oil, weak human capital, poor governance, and an unattractive business environment.

A key issue for structural transformation remains financing. Access to international financing often remains limited by criteria such as credit ratings, public indebtedness, and the ability to offer adequate guarantees, especially for the new transitional government in place since the August 2023 coup. The country can benefit from the global financial architecture to mobilize resources by taking advantage of concessional financing from multilateral banks, raising funds on regional and international financial markets, strengthening its domestic financial sector to facilitate local business financing and the issuance of green bonds, focusing on efficient and productive investment, and leveraging its substantial natural capital to generate additional resources.

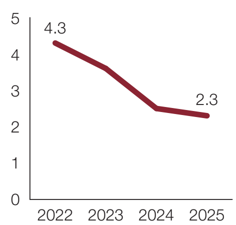
Real GDP growth (%)



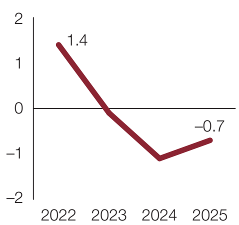
Real GDP per capita growth (%)



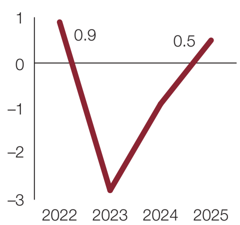
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

EAST AFRICA

Burundi

Recent macroeconomic and financial developments

Real GDP grew 2.8% in 2023, up from 1.8% in 2022, driven mainly by industry (up 4.7%) and services (up 2.7%) on the supply side and by public investment and private consumption on the demand side. Inflation rose from 18.8% in 2022 to 27.1% in 2023, due mainly to higher food prices (up 37.2%), driven by weak agricultural production and the 38.5% depreciation of the Burundian franc against the US dollar.

The budget deficit worsened from 5% of GDP in 2022 to 5.3% of GDP in 2023, following a greater increase in spending (29.2%) than in revenue (24%). Public debt rose from 68.4% of GDP in 2022 to 72.7% in 2023. According to the International Monetary Fund, the risk of external and global debt distress remain high. The current account deficit improved considerably from 13.7% in 2022 to 8.2% of GDP in 2023. But financial sector performance deteriorated, with the solvency ratio falling from 20.7% in 2022 to 19.8% in 2023 and nonperforming loans rising from 2.7% to 3.3% of gross loans.

According to the World Bank, the population living on less than $1.90 a day fell from 65.10% in 2013 to 62.10% in 2020. This was accompanied by a slight reduction in inequality, with the Gini coefficient dropping from 0.386 to 0.375 over the same period. The country has one of the lowest Human Development Index values in the world, 0.420 in 2022, ranking 187 out of 193 countries.

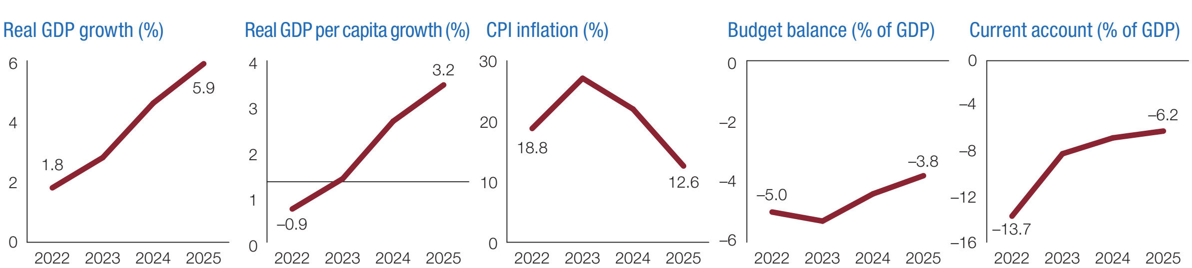
Outlook and risks

The outlook for 2024 and 2025 remains favorable, with real GDP growth projected at 4.6% in 2024 and 5.9% in 2025, boosted by investment in the mining sector and public investment. Inflation is expected to fall to 22% in 2024 and to 12.6% in 2025, following an improvement in local food supplies. The budget deficit is projected to improve to 4.4% of GDP in 2024 and to 3.8% in 2025, following a return to fiscal consolidation. The current account deficit is projected to improve to 6.8% of GDP in 2024 and to 6.2% in 2025. But Russia's invasion of Ukraine, climate hazards, deterioration in the country's political and regional security context, and weak mobilization of financing could compromise these prospects. Thus, Burundi needs to pursue the economic and financial reforms supported by the African Development Bank and other partners, the dialogue around inclusive governance, the integration of climate change resilience into development projects, and the continued support of development partners for the country.

Reform of the global financial architecture

The structure of the economy has changed little in recent years. From 2018 to 2022, the agricultural sector's share of GDP remained stable at 40%, while that of services stagnated at an average of 42% and that of industry stagnated at an average of 18%. Over the same period, the share of employment in the agricultural sector, which is characterized by low productivity, averaged 86.1%, while that in services (dominated by the informal sector) averaged 10.4% and that in industry averaged 3.5%. Improving agricultural productivity, promoting high-value-added manufacturing industries, and investing in infrastructure and human capital would help bring about genuine structural change in the economy.

Accelerating structural transformation, which is at the heart of the country's 2018–2027 National Development Plan, requires substantial financial resources. With a tax burden already at around 16%, the country will need access to external financing. Reforming the global financial architecture is becoming a necessity and would enable the country to benefit from more concessional financing while facilitating better access to existing financing windows at the regional and global levels (particularly climate funds). To achieve this, the country will need to step up reforms to public debt management and monetary and exchange rate policies to ensure macroeconomic and financial system stability and attract more private investment.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Comoros

Recent macroeconomic and financial developments

Economic recovery continued in 2023, with real GDP growth of 3.1%, up from 2.6% in 2022. Growth in 2023 was driven by services (up 3.6%) and agriculture (up 3.3%) on the supply side and by household final consumption (up 5.1%), supported by strong remittances from the diaspora, on the demand side. Inflation fell from 12.4% in 2022 to 9.1% in 2023 thanks to stable world prices. The central bank continued its liquidity recovery operations but reduced the reserve requirement rate in October 2023 from 15% to 12.5% to boost bank lending.

The budget deficit deteriorated from 3.8% of GDP in 2022 to 4.3% in 2023, due to higher civil servant salaries, lower grants, and spending on the country's presidency of the African Union, despite higher tax revenue (up 12%). The debt-to-GDP ratio was 38.2% in 2023. But the risk of debt distress is high, due to limited repayment capacity for nonconcessional loans. The current account deficit widened from 0.6% of GDP in 2022 to 6.1% in 2023, due to an increase in imports linked to major public infrastructure projects, a drop in clove exports, and a decline in external financing. Foreign exchange reserves were estimated at 6.9 months of import cover in 2023, up from 6.6 in 2022. The banking system's bad debt ratio rose from 13.9% in 2022 to 15% in September 2023.

The social situation remains precarious. The poverty rate was an estimated 38.4% in 2023, down slightly from 39% in 2022. The unemployment rate has stabilized at 6.5%, but underemployment remains high.

Outlook and risks

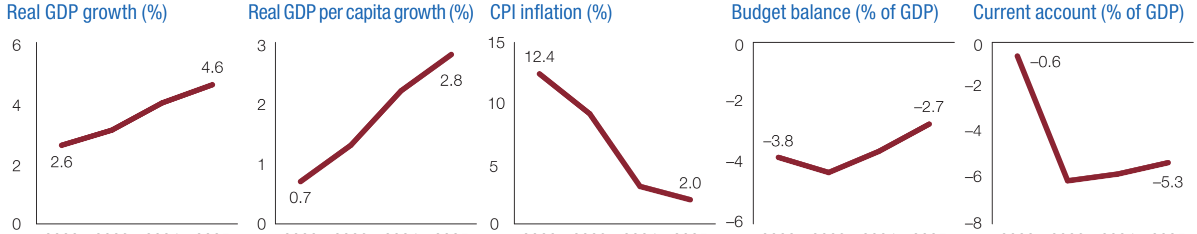
The economic outlook is favorable, though fragile, with projected growth of 4% in 2024 and 4.6% in 2025. This is expected to be underpinned by the acceleration of major government projects under the Emerging Comoros Plan, the International Monetary Fund Extended Credit Facility arrangement, and the initial economic benefits anticipated from accession to the African Continental Free Trade Area and the World Trade Organization. On the supply side, services and agriculture are projected to drive growth, while household consumption is projected to stimulate demand. Inflation is projected to continue to fall as world prices stabilize. The budget deficit is projected to remain high, due to rising public spending linked to support for economic recovery, notably public investment. The current account deficit is projected to remain high (5.8% of GDP in 2024) due to the continuing deterioration in the trade balance. Public debt is projected to increase moderately, and foreign exchange reserves are projected to remain high. Risk factors likely to disrupt this outlook include escalating geopolitical crises around the world, which would keep import prices high; declining external aid and financing; and spreading of the cholera epidemic.

Reform of the global financial architecture

The structural transformation of the economy has been slow to materialize despite changes in the structure of GDP and employment. From 2000 to 2022, the contribution of services to GDP rose from 47.2% to 56.1%, while that of agriculture fell from 40.9% to 34.5% and that of industry from 11.9% to 9.4%. This change in GDP structure was accompanied by the migration of some workers from agriculture to services. But this migration reflects nothing more than the disaffection of better-educated young people regarding agricultural occupations in favor of urban, often informal, services. To truly trigger structural transformation, the government should promote private investment as a new engine of growth in areas that bring greater value added, such as digital services, the blue economy, industry, and tourism while filling the human and physical capital deficits.

Because of the country's weakly developed financial sector, financing structural change requires strengthening the mobilization of domestic resources, strengthening the financial sector, optimizing transfers from the diaspora, and facilitating access to external financing through reform of the global financial architecture. Financing should be used to improve the business climate, bridge the infrastructure gap in the electricity and transport sectors, strengthen human capital, and reinforce the fight against climate change. It is also essential to consolidate the rule of law, promote political stability, and improve public governance.

Real GDP growth (%) | Real GDP per capita growth (%) | CPI inflation (%) | Budget balance (% of GDP) | Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Djibouti

Recent macroeconomic and financial developments

The upturn in economic activity was consolidated in 2023, with GDP growth estimated at 7.3%, up from 3.7% in 2022, driven mainly by trade (thanks to the revival of port activities) and transport. Services accounted for around 85% of GDP in 2023, followed by industry (14%) and agriculture (1%). Inflation fell from 5.2% in 2022 to 1.3% in 2023, due in particular to the slowdown in world food prices.

Despite an increase in debt servicing (up from 0.7% of GDP in 2022 to 1% in 2023), the budget deficit improved from 1.4% of GDP in 2022 to 0.5% in 2023, due mainly to higher grants (1.9% of GDP in 2023). The tax burden remains low, at an estimated 11% of GDP in 2023. Public external debt was stable at around 76% of GDP between 2022 and 2023. The current account surplus improved from 17.9% of GDP in 2022 to 21.2% in 2023. Nonperforming loans fell from 6.7% of gross loans in 2021 to 4.3% in 2022. The solvency ratio strengthened from 14.1% in 2021 to 16.8% in 2022. Foreign exchange reserves fell from 7.3 months of import cover in 2022 to 5.1 months (excluding the Free Zone) in 2023.

According to World Bank data, the poverty rate was an estimated 39.0% in 2022, down marginally from 39.8% in 2021. A quarter of the working-age population is employed; according to the International Labour Organization, the youth unemployment rate was around 73% in 2021, due mainly to a skills deficit.

Outlook and risks

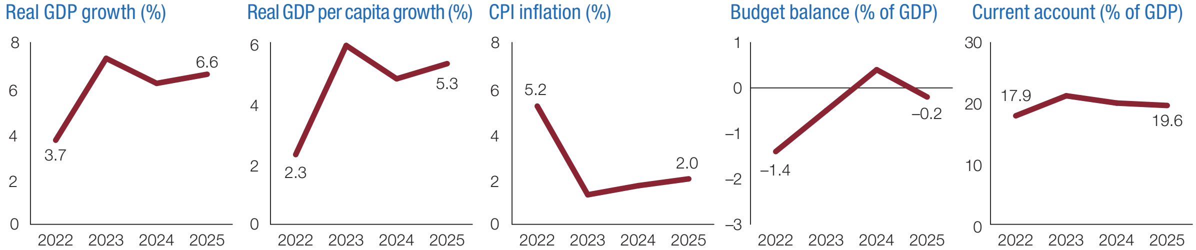
The economic outlook is favorable, with GDP growth projected at 6.2% in 2024 and 6.6% in 2025, driven in particular by the revival of port and logistics activities, the dynamism of transport and communications, and the strengthening of the public administration and defense sectors. Inflation is projected at 1.7% in 2024 and 2.0% in 2025, reflecting the impact of international prices. Fiscal balance is expected in 2024 (a surplus of 0.4% of GDP) but will be very fragile, with a contraction of 0.2% of GDP in 2025, due in particular to a projected decline in revenues and grants. The current account surplus is expected to contract to 20% of GDP in 2024 and 19.6% in 2025 due to declines in trade and services balances.

Factors likely to work against the favorable outlook include a slowdown in port traffic due to renewed instability in Ethiopia and heightened geopolitical tensions, particularly in the Middle East; difficulties repaying external public debt; Russia's invasion of Ukraine; and the effects of climate change.

Reform of the global financial architecture

Structural transformation has been slow. Services accounted for an annual average of 83% of value added over 2004–23, with trade predominating (29%), suggesting the importance of informal activities. During the period, manufacturing accounted for around 3% of value added. Over 2010–19, labor migration to higher-productivity sectors was low. The share of employment in industry has stagnated at 13% a year. Diversifying production could accelerate structural transformation, as recommended in the African Development Bank's 2023 study on a new economic growth model for Djibouti.

Given the high risk of debt overhang, mobilization of domestic resources should be accelerated, with priority given to concessional financing. Financing structural transformation would help reduce the country's debt to a sustainable level. The Djibouti Sovereign Wealth Fund, launched in 2020, represents an opportunity to mobilize domestic and foreign investors to finance infrastructure in particular. Reforming the global financial architecture could help mobilize more private funding at lower cost as the perception of risk in African countries would decline and could facilitate access to external financing such as climate funds.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Eritrea

Recent macroeconomic and financial developments

Real GDP expanded from 2.6% in 2022 to an estimated 2.9% in 2023. Growth was driven by industry, notably mining and services, on the supply side, and by household and public consumption on the demand side. Monetary policy was contractionary. Inflation subsided to 6.4%, supported by improved supplies and stability in global supply chains. The exchange rate is fixed at 15 nakfa to the US dollar.

The fiscal deficit narrowed to 0.1% of GDP in 2023 due to fiscal consolidation, with the tax-to-GDP ratio remaining stable at about 17%. The public debt-to-GDP ratio was estimated at 164% for 2022, with domestic debt accounting for 68%, implying minimal foreign currency risk. Eritrea's last debt sustainability analysis was undertaken in 2019 and is not publicly available. The current account surplus increased to an estimated 14.1% of GDP in 2023 with improvements in the merchandise trade balance as exports increased, mainly of minerals. The financial sector comprises a state-owned commercial bank and two nonbank institutions.

The working poverty rate declined from 55% in 2010 to 50% in 2020, and the uptick in real GDP growth per capita in 2023 may have reduced poverty further.

Outlook and risks

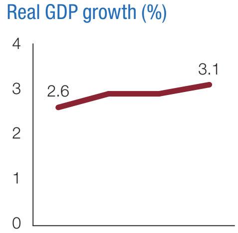
Real GDP growth is projected to stabilize at 2.9% in 2024 and increase to 3.1% in 2025. Growth will be led by mining and services on the supply side, consistent with strong growth in the mining sector. On the demand side, private consumption and investment will drive growth, reflecting improved per capita income and planned expansion in the mining sector. Inflation is projected to drop to under 5%, consistent with improved food supplies. Eritrea's fiscal balance is expected to improve to a surplus in 2024 and 2025, supported by fiscal consolidation. The current account surplus is projected to drop to 12.4% in 2024, reflecting fluctuations in global demand and prices for commodities. The key downside risks include delays in production at the Colluli potash mine due to challenges with mobilizing the necessary financing, fluctuations in international prices for metals, and insecurity in the Horn of Africa region.

Reform of the global financial architecture

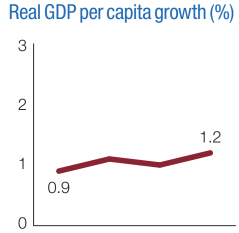
Structural transformation remains nascent and could benefit from an industrial policy and investments in physical and human capital. Agriculture's share of GDP increased from 10.6% in 2004 to 17.6% in 2023, and industry's share from 19.6% to 32.0%. However, the share of manufacturing remains meagre despite increasing from 1.1% in GDP to 9.8%, consisting mostly of low-value agro-processing. The share of services in GDP dropped from 61.7% to 52.5%. Sectoral shares in employment remained basically unchanged between 2004 and 2021, at 62% for agriculture, 29.0% for services, and 9.0% for industry. Unprocessed minerals, ores, and metals account for 60% of merchandise exports.

Structural transformation will benefit from diversification of export products and markets to catalyze stable foreign exchange inflows and technology. Signing the African Continental Free Trade Area agreement and acceding to the World Trade Organization will enhance Eritrea's participation in regional and global value chains, enabling productivity growth and expanding market access. Negotiation of bilateral cooperation agreements will help Eritrea crowd-in investment and finance, notably in the natural resources sector. More clarity on the concept of comparable treatment of creditors, as part of reforms of the global financial architecture, will benefit Eritrea should debt restructuring be considered.

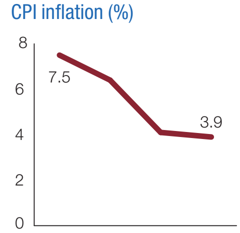
Real GDP growth (%)



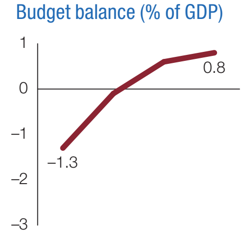
Real GDP per capita growth (%)



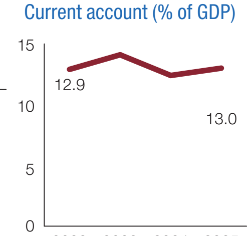
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Eritrea's fiscal year, which runs from July 1 to June 30.

Ethiopia

Recent macroeconomic and financial developments

Ethiopia's economy grew 7.1% in 2022/23, up from 6.4% in 2021/22, led by 7.9% growth in the services sector, which accounts for 40% of GDP. Industry, at 28% of GDP, grew 6.9% and agriculture, at 32% of GDP, grew 6.3%, also supporting growth. Demand-side drivers of growth included private consumption and investment. Although inflation remained high, due to money supply growth and imported inflation, it dropped from 34% in 2021/22 to 29.2% in 2022/23 due to a tightening of monetary policy. The exchange rate depreciated by 5.3% on the official market and 15% on the parallel market, due to slow export growth.

The fiscal deficit, including grants, narrowed from 4.2% of GDP in 2021/22 to 3.3% in 2022/23 owing to fiscal consolidation, the peace dividend, and improved tax revenues, which grew by 35.8% in 2022/23 compared with 12.3% in 2021/22. The current account deficit narrowed from 3.9% of GDP in 2021/22 to 3.0% in 2022/23, due to a 60.3% increase in net services and a 5.3% reduction in imports. The financial sector is stable, with nonperforming loans at 3.5% of gross loans and a liquidity ratio of 24.2%, against thresholds of 5% and 15%, respectively. Ongoing reforms to allow foreign investment in the sector will increase competition and innovation.

Poverty declined from 31.1% in 2016 to 27% in 2019. Unemployment is estimated at 8% (youth unemployment at 23.1%) in 2020/21, with about 2.5 million new jobs needed annually to absorb new entrants. About 31.4 million people require humanitarian support due to conflict and climate-related shocks.

Outlook and risks

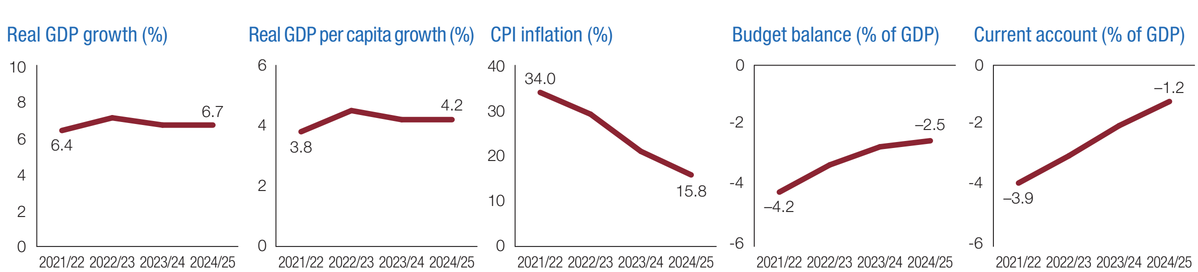
Growth is projected at 6.7% during 2024–25 due to fiscal consolidation. An envisaged slowdown in investment due to protracted debt restructuring negotiations could hold back access to development financing. Tighter monetary policy is expected to reduce inflation to 21.0% in 2023/24 and 15.4% in 2024/25. The fiscal deficit is projected to narrow in 2023/24 and 2024/25 as tax revenues improve, with the current account deficit reflecting similar trends as imports continue to decline consistent with reduced public investment and gradual growth in exports.

Key downside risks include structural bottlenecks, debt and climate vulnerabilities, conflicts, and high oil and food prices due to supply chain disruptions. Risk mitigation measures include ongoing homegrown economic reforms focusing on monetary, fiscal, financial, public debt, investment, and trade policies and on productive and public sectors. Implementation of the peace agreements and national dialogue will enhance stability and support recovery of tourism and investment.

Reform of the global financial architecture

Ethiopia's structural transformation has been slow. Agriculture's share of GDP declined from 54% in 2000 to 32.0% in 2023, accounting for 62.8% of employment in 2022 (90.2% in 1990). The service sector's share of GDP increased from 37.6% in 2000 to 40.0% in 2023, accounting for 30% of employment (7.8% in 1990). Industry's share of GDP increased from 10.0% in 2000 to 28.8% in 2023, accounting for 7% of employment in 2022 (2% in 1990). Manufacturing contributed only 6.9% of GDP in 2023 (2% in 2000). Addressing macroeconomic imbalances, curbing structural rigidities, easing sectoral bottlenecks in tourism and information and communication technologies, and modernizing the financial sector will spur structural transformation.

Reforming the global financial architecture, notably clarifying the notion of comparable treatment of creditors, will facilitate debt restructuring and create fiscal space for investments in productive sectors. Negotiations are under way on a new International Monetary Fund program that is expected to facilitate Ethiopia's debt restructuring under the G20 Common Framework. Furthermore, channeling unused Special Drawing Rights through multilateral development banks and preparing bankable climate finance proposals will help to crowd in financing. Ethiopia could also leverage financing from its home-grown economic reforms, including expanding public-private partnerships, restructuring state-owned enterprises, and developing money and capital markets.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Kenya

Recent macroeconomic and financial developments

Kenya's economy grew 5.2% in 2023, up from 4.8% in 2022, as agriculture rebounded, and services grew moderately. On the supply side, services accounted for 69% of the growth and agriculture for 23%, while on the demand side, household consumption accounted for 70%. Inflation edged up to 7.7% in 2023 from 7.6% in 2022, driven by core inflation (32% of the change), fuel inflation (26%), and cost-push inflation (9% year on year increase in the producer price index).

The policy rate was hiked 375 basis-points, to 12.5%, and central bank operations sought to anchor inflation expectations. The fiscal deficit widened from 6.3% of GDP in 2022 to 7% in 2023, as revenues underperformed, and interest costs rose. Public debt expanded from 66.7% of GDP in 2022 to 70.2% in 2023, driven by increased loans to finance the primary deficit and by exchange rate depreciation. The current account deficit narrowed from 5.2% of GDP in 2022 to 4.9% in 2023, as trade deficits shrank, and secondary incomes increased. The deficit was financed by drawing down reserves, which declined from 4.3 months of import cover to 3.6 months. The shilling depreciated by 24% year on year in 2023. The capital adequacy ratio of 18.6% in 2023 was above the prudential minimum of 14.5%, and the liquidity ratio of 49.7% was above the 20% prudential minimum. Nonperforming loans increased from 13.6% of gross loans in 2022 to 14.5% in 2023 due to rate hikes and public sector debt arrears (or outstanding government payments to contractors). Credit-risk concentration was high in manufacturing, real estate, and personal and household sectors.

Poverty increased from an estimated 33.6% in 2019 to 36.1% in 2021, and unemployment rose slightly, from 13.3% in 2021 to 13.9% in 2022. Income inequality from a Gini coefficient of 0.36 in 2020 to 0.39 in 2021.

Outlook and risks

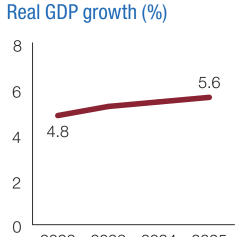
Kenya's GDP is projected to grow 5.4% in 2024 and 5.6% in 2025, driven by services and household consumption. Inflation is expected to fall to 6.2% in 2024 and 5.5% in 2025, as food and global inflation both decline. Monetary policy is expected to be accommodative due to projected stable inflation and exchange rates. The fiscal deficit is projected to narrow to 5.9% of GDP in 2024 and 5.0% in 2025 in response to a revenue-led fiscal consolidation program. The current account deficit is projected to narrow to 4.6% of GDP in 2024 and 4.5% in 2025 as a recovery in global trade reduces the trade deficit. However, the outlook is subject to considerable risks, including tight global financing, drought, political instability in neighboring countries, and slow recovery of global growth. Risk mitigation measures in the medium to long term include building fiscal and external buffers (e.g., foreign exchange reserves), strengthening disaster preparedness, and accelerating structural transformation.

Reform of the global financial architecture

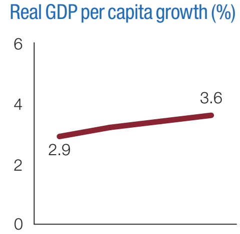
Kenya's GDP growth averaged 4.6% between 2019 and 2023, lower than its 10% target in Vision 2030. Growth has been noninclusive, attributable to the minimal contribution of structural transformation to growth. This has resulted in the low poverty-reduction and employment-creation capacity of growth. On average, structural transformation accounted for 28% of labor productivity growth between 2007 and 2022. A quarter of GDP growth came from sectors resilient to shocks. Output growth of 5.8% a year is needed to absorb the 680,000 people entering the labor market. With accelerated structural transformation, GDP growth of 7.3% could create 1.36 million new jobs and cut unemployment to 7%. Achieving this requires improving governance, infrastructure, human capital development, access to finance, and macroeconomic stability.

The global financial architecture presents challenges to Kenya in meeting its financing gap. Kenya needs $12 billion annually by 2030 and $2 billion annually by 2063 to close its financing gap to fast-track structural transformation. Some of the funds could be raised through domestic resource mobilization; the current tax-to-GDP ratio of 13% is below its 27% potential. Other options include deepening the domestic financial market and mobilizing private capital and rents from natural resources. Kenya raised resources equivalent to 5% of GDP from external sources recently. Kenya is calling for changes to the global financial architecture, including the debt architecture, concessional finance, and voice and power in decisionmaking.

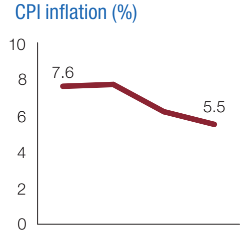
Real GDP growth (%)



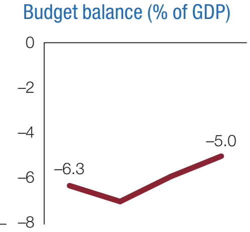
Real GDP per capita growth (%)



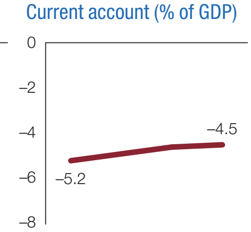
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Kenya's fiscal year, which runs from July 1 to June 30.

Rwanda

Recent macroeconomic and financial developments

Real GDP growth stabilized at 8.2% in 2022 and 2023, buoyed by expansion in industry and services on the supply side and public sector expenditures on the demand side. GDP per capita growth stabilized at 5.9% in 2022 and 2023. Headline inflation increased from 13.9% in 2022 to 14.3% in 2023, reflecting the passthrough effects of the high cost of imported goods and low domestic food production. The exchange rate rose from 1,051 Rwandan francs to the US dollar in 2022 to 1,234 in 2023. The Central Bank monetary policy rate was raised from 6% in August 2022 to 7.5% in August 2023 to counter rising inflation.

The overall fiscal deficit declined from 7.7% of GDP in 2022 to 7.0% in 2023 due to improved domestic resource mobilization. The debt-to-GDP ratio declined from 71.3% in 2022 to 66.6% in 2023 due to budget rationalization. The current account deficit averaged 10.7% of GDP in 2022 and 2023 because of the high import bill. Foreign exchange reserves provided 4 months of import cover in 2023. Banks' capital adequacy ratio was 21.1% at the end of September 2023, above the prudential limit of 15%. The ratio of nonperforming loans to gross loans dropped from 4.3% in June 2022 to 3.6% in June 2023, reflecting prudent management of the loan portfolio.

Extreme poverty declined from 47% in 2019 to 45% in 2021, and unemployment fell from 43.4% in August 2022 to 40.2% in August 2023. Skills mismatch is one of the major causes of unemployment. About 20.6% of Rwanda's population is food insecure, with 18.8% experiencing moderate food insecurity and 1.8% facing severe food insecurity.

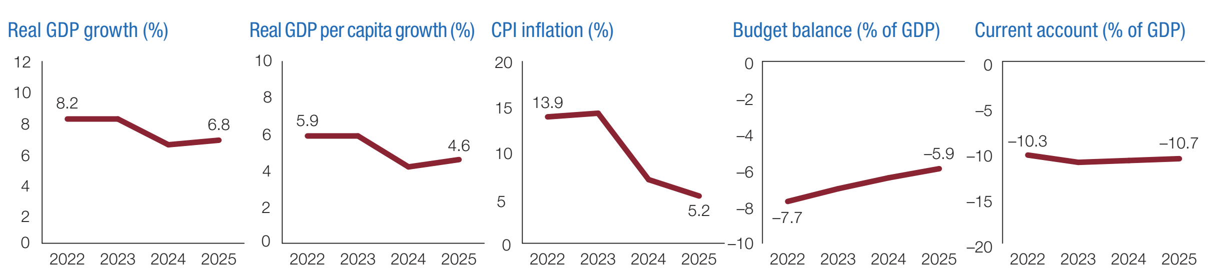
Outlook and risks

Real GDP growth is projected to drop to an average of 6.6% in 2024 and 2025, driven by climate shocks to agriculture. Inflation is expected to moderate to 7.0% in 2024 and 5.2% in 2025, reflecting stabilization of supply chains, monetary policy tightening, and falling international commodity prices. The fiscal deficit is projected to improve to 6.4% in 2024 and 5.9% in 2025 due to continued fiscal consolidation and stronger domestic revenue mobilization. Rwanda has committed to achieving a debt-to-GDP ratio of 65% by 2031. The current account deficit is projected to rise slightly to 10.9% of GDP in 2024 before narrowing to 10.7% in 2025 as capital imports decline, conference tourism receipts recover, and remittances from the diaspora improve. Foreign exchange reserves are expected to moderate to 4.8 months of import cover in 2024 and 5.2 months in 2025. The overall moderate economic performance is attributed to mitigation of climate shock risks by government climate risk action plans.

Reform of the global financial architecture

Rwanda has experienced very little structural transformation in the decade from 2013 to 2023. Sectoral shares of GDP remained almost unchanged: services declined from 49.8% to 47.9%, agriculture barely changed from 24.9% to 24.8%, and industry inched up from 17.6% to 18.9%. Factor deployment in production remained unchanged, with capital's contribution to growth estimated at 55% and total factor productivity at 22%. Capital-intensive services, including conferences and air transport, contributed to output growth without adding many nonfarm jobs. To accelerate structural transformation, the second National Strategy 2025–2029 is preceded by output-based costing with different scenarios highlighting required resources to meet structural transformation needs in the medium term.

In response to calls for global financial architecture reforms, development partners have committed to support Rwanda in mobilizing additional resources on competitive terms for transformative, sustainable, inclusive, and climate-smart investments. The interventions will support livelihood improvement by channeling resources to sectors that can promote structural transformation toward industry and services. Additionally, since March 2024, Rwanda has hosted the $1 billion African Continental Free Trade Area Adjustment Fund managed by Afreximbank's Fund for Export Development in Africa; $50 million has already been mobilized from the fund for transformative investments. Rwanda continues to attract international financial institutions through initiatives such as the Kigali International Financial Centre, where greater benefits are also expected.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Rwanda's fiscal year, which runs from July 1 to June 30.

Seychelles

Recent macroeconomic and financial developments

Real GDP growth in Seychelles moderated from a peak of 15% in 2022 to 2.5% in 2023. Tourism and fisheries remained supply-side growth drivers, while household consumption and investment were the main demand-side growth drivers. Tourist arrivals rose 5.7% in 2023 compared with 2022. Monetary policy remained accommodative, as inflation dipped from 2.6% in 2022 to –1.0% (deflation) in 2023. The main reasons for the deflation were low global fuel and food prices (the country's main imports), falling freight costs, and appreciation of the rupee (owing to increased tourist arrivals).

The fiscal balance widened from 1.5% of GDP in 2022 to 1.9% in 2023. The debt-to-GDP ratio declined from 58.9% in 2022 to 56.7% in 2023, reflecting a strong recovery and good public debt management. The current account deficit widened from 6.9% of GDP in 2022 to 8% in 2023 as import costs rose. External reserves improved from 3.2 months of import cover in 2022 to 3.7 months in 2023. The financial sector remained well capitalized although highly concentrated, with the three largest banks holding 80% of total assets, deposits, and loans. Bank nonperforming loans rose slightly from 6% of gross loans in 2022 to about 7% in 2023, mainly related to borrowing during the Covid-19 pandemic.

Social development indicators remain strong. Poverty is low at 0.5% in 2022/23, down from 0.7% in 2021. Unemployment remained low, at 3% in 2022 and 2023.

Outlook and risks

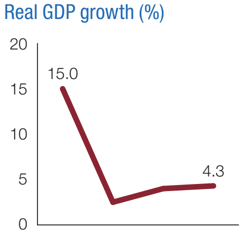
GDP growth is projected to improve to 4.0% in 2024 and 4.3% in 2025 amid sustained tourism receipts and enhanced performance of information and communication and financial services in line with priorities of the 2024–2028 National Development Strategy. Inflation is projected to rise to 1.4% in 2024 and 2.2% in 2025 as electricity tariffs and global food and fuel prices rise. Tourism and fisheries will remain key supply-side growth drivers. The fiscal deficit is projected to improve to 1.5% in 2024 and 1.3% in 2025 as revenue collection improves. The current account deficit is expected to narrow slightly and stabilize at 7.2% in 2024 and 2025, reflecting continuing recovery of tourism, while foreign reserves are projected to reach 3.9 months of import cover in 2024 and 2025. Downside risks to the economic outlook include disruptions to global supply chains from Russia's invasion of Ukraine and the Israel–Hamas war. Economic diversification and a continuing focus on renewable energy sources remain key for sustained growth and resilience.

Reform of the global financial architecture

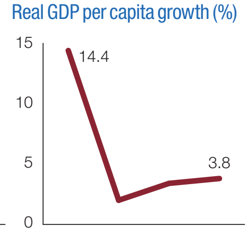
Structural transformation of the economy has been slow over the last decade. Agriculture's share of GDP remained unchanged at about 2.5% from 2010 to 2021, and industry's share remained at around 15%. Within industry, manufacturing's share was low and falling, declining from 10.5% in 2012 to 8.3% in 2021. Consequently, services' share remained dominant, at 82% to 84%. Within services, tourism maintained it top position, at around 31%. Movement of labor from high- to low-productivity sectors was slow. Agriculture's employment share remained around 1% between 2012 and 2021, and manufacturing's at around 9%. The employment shares of emerging sectors such as financial and information technology services hovered around 5%–6%. The small size of the domestic market, shortages of skilled labor, inadequate access to finance, high electricity cost, and climate change risks impede structural transformation.

With the declining availability of financing from international markets and Seychelles' small domestic market, the global financial architecture is impeding its efforts to address these challenges of structural transformation. Moreover, as a high-income economy, Seychelles is not eligible for concessional financing. The global financial system should evolve to consider the unique challenges and vulnerabilities of small island developing countries like Seychelles to offer financing that can enable them to accelerate their structural transformation. Structural transformation is one of the six pillars of the country's 2024–2028 National Development Strategy.

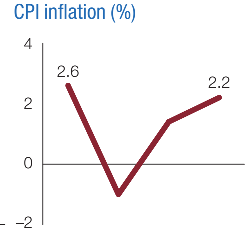
Real GDP growth (%)



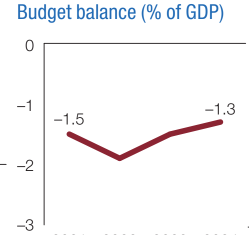
Real GDP per capita growth (%)



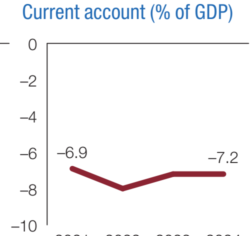
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Somalia

Recent macroeconomic and financial developments

GDP growth accelerated from 2.4% in 2022 to 2.8% in 2023. Growth was driven by services and the agricultural sector's recovery from drought on the supply side and by household consumption and investment on the demand side. A deceleration in global inflation boosted remittances, and the return of rains improved livestock output and growth. The stability of global supply value chains eased inflation in Somalia from 6.8% in 2022 to 6.1% in 2023. As part of its monetary and exchange rate policy reforms, Somalia is implementing a currency exchange program to gradually replace US dollars and counterfeit Somali shillings with new Somali shillings by 2026.

The fiscal deficit widened from a zero-cash fiscal balance in 2022 to 0.4% of GDP in 2023, as spending on security and social sectors offset the strong performance in domestic revenues. The fiscal deficit was financed by the government's cash savings. Somalia's public debt-to-GDP ratio plummeted from 64% in 2018 to 6.4% in December 2023 as Somalia reached the completion point in the Heavily Indebted Poor Countries (HIPC) debt reduction initiative, and its debt classification improved from in debt distress to moderate. The current account deficit was 12.4% of GDP in 2023, reflecting a rising trade deficit (estimated at 61% of GDP in 2023) driven by reduced livestock exports because of the drought. Nonperforming loans in the financial sector, which comprises 13 banks and 11 money transfer agents, dropped slightly, from 2.7% of gross loans in 2022 to 2.6% in 2023.

Poverty declined from 69% in 2021 to 54.4% in 2022, while youth unemployment remained high at 30.1% in 2022, well above the 21.7% overall unemployment rate.

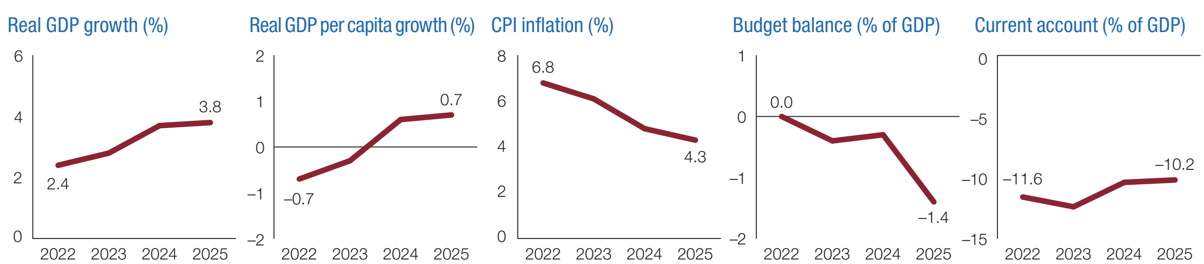
Outlook and risks

Real GDP growth is projected at 3.7% in 2024 and 3.8% in 2025 due to gradually increasing spending on infrastructure and social sectors, supported by an envisaged uptick in development financing after reaching the completion point in the Heavily Indebted Poor Countries debt reduction initiative. Growth will be driven by agriculture and services on the supply side and private consumption and public investment on the demand side. Inflation is projected to decline to 4.8% in 2024 and 4.3% in 2025 due to improved agricultural production. The downside risks to growth relate to the Somalia–Ethiopia contestations over ports in the Red Sea, climate shocks, insecurity, weaker remittance inflows, and slow domestic revenue growth. The fiscal deficit is projected to narrow to 0.3% of GDP in 2024 before widening to 1.4% in 2025, reflecting the uptick in public spending. The current account deficit is projected to narrow to 10.4% of GDP in 2024 and 10.2% in 2025, as livestock exports improve.

Reform of the global financial architecture

Somalia has yet to achieve structural transformation of its economy, with progress stymied by fragility arising from conflict, climate change, institutional weaknesses, and a poor business environment, including complex land tenure and licensing regulations. Services' share of employment rose marginally, from 55.9% in 2020 to 56% in 2021, and industry's share rose from 15% in 2020 to 17.7% in 2021. Meanwhile, agriculture's share of employment declined from 39% in 2020 to 26.3% in 2021. Exports of unprocessed livestock products accounted for 76% of total exports in 2022, followed by gold and fish exports.

Somalia needs to invest in growth enablers, including state and institutional strengthening, infrastructure, and agricultural technologies. Also, greater development of value chains, notably in leather and leather products, is needed to increase integration into global leather value chains. Developing special economic zones will help to generate agglomeration benefits. Sustaining economic and financial governance reforms, notably in the financial sector, and strengthening the business environment will improve economic competitiveness and Somalia's integration into the global financial architecture. Ongoing domestic revenue mobilization reforms, especially modernization of customs, will expand the fiscal space. Somalia is a major beneficiary of the global financial system, notably arrears clearance in 2020 and debt forgiveness after reaching the HIPC completion point in 2023. Reforms to enhance access to concessional and climate financing will expand Somalia's development financing.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

South Sudan

Recent macroeconomic and financial developments

Real GDP contracted by an estimated 0.4% in 2022/23, reflecting the easing of economic challenges resulting from the conflict in Sudan. That conflict has increased the cost of oil production, as South Sudan relies on Sudan's oil pipelines. Persistent floods also damaged some oil fields, partially offsetting the gains from improved global oil prices. Production in the agriculture sector remained stagnant, due largely to devastating floods. On the demand side, the growth contraction was driven by lower net exports due to decreased oil production. Inflation rose to an estimated 16.5% in 2022/23 due to supply chain disruptions caused by the war in Sudan.

The money supply grew from 47% in 2021/22 to about 72% in 2022/23 due to monetization of the fiscal deficit. The fiscal deficit improved to 4% of GDP in 2022/23, responding to fiscal consolidation. South Sudan is at high risk of debt distress, with the debt-to-GDP ratio estimated at 34.5% in 2023. The current account balance improved to a surplus of 7.0% of GDP in 2022/23, due to a gradual uptick in oil export revenues. International reserves were estimated at 0.5 month of import cover in 2022/2023, due partly to currency depreciation. Nonperforming loans rose from 9% of gross loans in 2021/22 to 14% in 2022/23, due to high interest rates.

Poverty remains high in this economy in transition, and 7 million people are food insecure. Unemployment increased from 12% in 2022 to 12.5% in 2023. In October 2023, there were more than 41,000 refugees from Sudan and more than 290,000 million returnees.

Outlook and risks

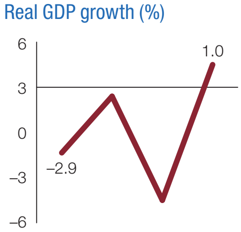
Real GDP is projected to contract by 5% in 2023/24 following vandalization of an oil pipeline due to the ongoing conflict in Sudan. GDP is expected to recover to 1% in 2024/25 as oil production and exports stabilize. Growth will be supported by industry, especially oil, and services on the supply side and consumption and investment on the demand side. The fiscal deficit is projected at 6% of GDP in 2023/24, narrowing to 2% of GDP in 2024/25 as oil production stabilizes and public revenues improve. Inflation is projected to average 17% between 2023/24 and 2024/25, reflecting high food prices and an expected uptick in elections-related spending. The current account deficit is projected at 7.0% of GDP in 2023/24, improving to 4% in 2024/25 as oil exports pick up. Key headwinds to growth relate to the conflict in Sudan and climate change impacts.

Reform of the global financial architecture

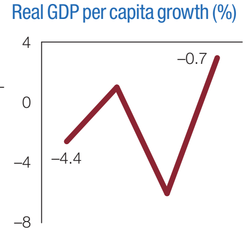
South Sudan is a young nation facing several challenges affecting its structural transformation, including low productivity and skills. The industry sector's (largely oil and mining) share of GDP dropped from 56.8% in 2012 to 41.6 % in 2022, driven by the impact on oil production of war-damaged oil infrastructure. The share of services in GDP increased from 39.1% to 52.5% in the same period. Manufacturing accounted for an average of 2% of GDP in 2022. Industry employs about 13% of the workforce, and services employs about 25%. Agriculture's share of GDP increased from 4.1% in 2012 to 6.0% in 2022, owing to partners' support including the Bank through access to quality seeds and fertilizers, which increased productivity.

Financing structural transformation in the short term requires ramping up domestic revenue mobilization and improving public spending efficiency to create fiscal space for investments in growth enablers. In the medium to long term, emphasis could be placed on debt restructuring, which would benefit from reforms to the G20 Common Framework, especially comparable treatment of creditors. Access to risk-sharing instruments could crowd in private investment and finance.

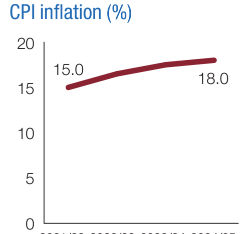
Real GDP growth (%)



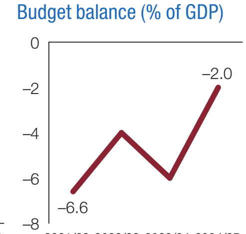
Real GDP per capita growth (%)



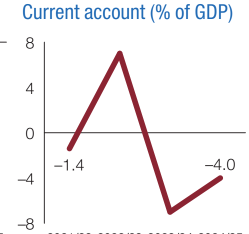
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to South Sudan's fiscal year, which runs from July 1 to June 30.

Sudan

Recent macroeconomic and financial developments

The ongoing armed conflict, which has resulted in about 15,000 deaths, 33,000 injuries, and 11 million people displaced and has created regional spillovers, has had a devastating impact on Sudan's economic performance. Real GDP contracted by 37.5% in 2023 due to destruction of production capacity and disruption of economic activities, with a decline in services dragging down growth on the supply side. On the demand side, the loss of income and the massive displacements have reduced consumption.

The fiscal deficit widened to 9.1% of GDP in 2023 as tax revenue declined from 5.6% of GDP in 2021 to 2.0% in 2023. Reduced government revenues together with increasing expenditures resulted in monetization of the fiscal deficit, driving inflation to 245.3% in 2023. Inflation was exacerbated by a shortage of consumer goods and by currency depreciation. Sudan remains in debt distress as political instability halted progress toward the completion point of the Heavily Indebted Poor Countries (HIPC) debt reduction initiative. The current account deficit, which was financed by remittances and international reserves, widened to 7.3% of GDP in 2023 due to weak export performance. Reserves dropped from 2.7 months of import cover in 2022 to 1 month in 2023. Whereas nonperforming loans remained below 5% of gross loans in 2022, subdued economic activities reduced borrowers' ability to service debt, raising nonperforming loans to above 10% of gross loans in 2023.

Poverty was high in 2022, at 66.1%, and has likely increased due to conflict and lower GDP per capita. Unemployment was high at 20.6% in 2022, with youth unemployment at 40%.

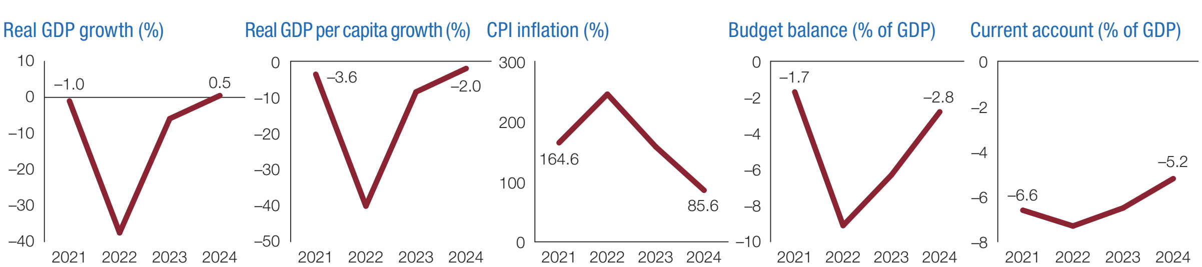
Outlook and risks

Because of the conflict, GDP is projected to contract another 5.9% in 2024, before a recovery to 0.5% in 2025, assuming that peace is restored in 2024. The recovery would be supported by reconstruction spending, especially on social services and infrastructure, and resumption of economic activity across sectors. If peace is restored, the anticipated increase in government revenues would moderate inflation to 157.9% in 2024 and further to 85.6% in 2025. The fiscal deficit would narrow slightly to 6.3% in 2024 and further to 2.8% in 2025. The current account deficit is expected to improve to 6.5% of GDP in 2024 and 5.2% 2025, reflecting an uptick in exports following the restoration of peace. Key downside risks to the outlook are the possibility of conflict persisting beyond 2024, the impacts of climate change, and weak institutional capacities. There is an urgent need to end hostilities, build climate resilience, and strengthen institutional capacities.

Reform of the global financial architecture

The ongoing conflict has reversed the limited progress Sudan has made in structural transformation. In recent years, productivity declined 30% in services, the main employment sector, while increasing 20% in industry and remaining unchanged in agriculture. Between 2010 and 2022, the share of employment in agriculture declined from 49.7% to 40%, while that of services increased from 41.8% to 45% and that of industry remained stable at 15%. To accelerate structural transformation, Sudan must restore peace and create an environment in which it can address infrastructure bottlenecks, develop the skills needed to support industrialization, and strengthen institutional capacities to enhance the governance framework for private sector growth.

In a postwar Sudan, effective financing of structural transformation will require greater domestic resource mobilization through targeted reforms in tax administration and natural resources management, and strengthened financial and economic governance for efficient government spending and public debt management and sustainability. Sudan has benefited from the global financial architecture through the clearance of debt arrears and attainment of the HIPC decision point in 2021. Sudan would benefit from further reforms to the global financial architecture, notably greater clarity of the concept of comparable treatment of creditors once the HIPC process resumes, as well as reforms to increase access to concessional financing.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Tanzania

Recent macroeconomic and financial developments

Real GDP grew 5.3% in 2023, up from 4.7% in 2022, driven by agriculture, construction, and manufacturing on the supply side and private investments on the demand side. Tight monetary policy, together with moderation in food and energy prices, helped reduce inflation from 4.3% in 2022 to 3.8% in 2023. The Tanzanian shilling depreciated by 8% in 2023, reflecting shortages of foreign exchange.

The fiscal deficit declined slightly from 3.6% of GDP in 2021/22 to 3.5% in 2022/23, responding to expenditure controls, and was financed by external and domestic borrowing. Public debt increased from 43.6% of GDP in 2021/22 to 45.5% in 2022/23 due to an increase in loans. The current account deficit narrowed from 7.3% of GDP in 2022 to 3.8% in 2023, benefiting from higher tourism receipts, and was financed by external commercial debt and official flows. Reserves declined from 4.7 months of import cover in 2022 to 4.5 months in 2023, explained by the authorities' response to the foreign exchange shortage. The banking sector, which accounts for 71% of financial assets, remained sound with the ratio of nonperforming loans to gross loans declining from 5.7% in 2022 to 4.3% in 2023, below the regulatory requirement of 5%.

The 2017/18 Household Budget Survey reported a decline in poverty from 28.2% in 2011/12 to 26.4% in 2017/18, although recent assessments by United Nations agencies estimate that poverty increased from 26.1% in 2019 to 27.7% in 2020 due to Covid-19. The 2021/22 Integrated Labor Force Survey revealed a decline in unemployment from 10.5% in 2014 to 9.3% in 2021/22.

Outlook and risks

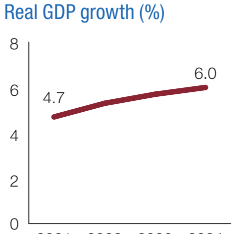
Real GDP growth is projected at 5.7% in 2024 and 6% 2025, driven by agriculture, manufacturing, and tourism and supported by public investments and reforms to improve the business environment. Inflation is projected to decline to 3.3% in 2024 and 3.4% in 2025, helped by stability in food and energy prices. The fiscal deficit, financed by domestic and external borrowing, is expected to decline to 2.5% of GDP in 2023/24 and stabilize at that level in 2024/25, supported by improvements in revenue performance. The current account deficit, financed by external borrowing, is projected at 4.0% of GDP in 2024 and 4.2% in 2025, supported by merchandise exports and tourism receipts. The major downside risks to the outlook include spillovers from geopolitical tensions and regional conflicts, sluggish global growth, the narrow tax base, and climate shocks.

Reform of the global financial architecture

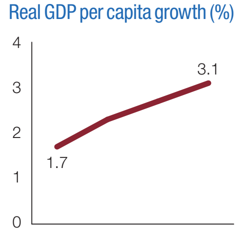
Structural transformation in Tanzania has been slow and constrained by several challenges, including declining industrial productivity and competitiveness and shallow financial markets. Agriculture's share in employment declined from 84.8% in the early 1990s to 65% in 2022, while industry's share rose from 2.6% to 6.8% and services' share rose from 12.6% to 29%. Agriculture's share in GDP dropped from 42% in the early 1990s to 26% in 2022. Manufacturing's share in GDP has remained unchanged at around 8% since the mid-1990s, and its share in total exports has remained below 25%. The slow pace of structural transformation is holding back labor productivity growth.

Actions to expedite structural transformation include adjusting the regulatory framework to improve the business environment and boost investments in manufacturing; addressing infrastructure bottlenecks, especially in energy and transport; and investing in human capital. Financing Tanzania's structural transformation requires deepening financial markets through digital financial solutions; increasing domestic revenue mobilization, notably by expanding the tax base; and strengthening capacities for negotiation of natural resources contracts. Reforms of the global financial architecture to increase access to concessional, low-cost, and long-term development and climate financing would be most beneficial to Tanzania.

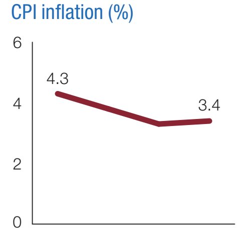
Real GDP growth (%)



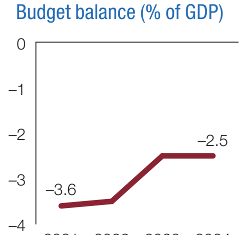
Real GDP per capita growth (%)



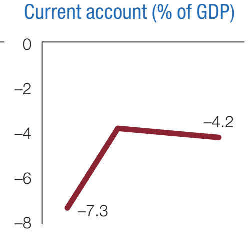
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Tanzania's fiscal year, which runs from July 1 to June 30.

Uganda

Recent macroeconomic and financial developments

Uganda's economy expanded 4.6% in 2023, lower than the 6.3% registered in 2022. Despite strong performance in mining, construction, and hospitality, lower manufacturing output and contractions in food production and public administration led to the slowdown. Tight fiscal policy contributed to slower economic growth, despite large investments in oil and gas. Consumer demand and foreign investment remain robust. Monetary policy has been tight, with the Bank of Uganda setting the policy rate at 10.25%. Inflation declined from 7.2% in 2022 to 5.5% in 2023. Net foreign assets declined during the second half of 2023, marginally depreciating the shilling–US dollar exchange rate by 1.8% in 2023.

The government continues its fiscal consolidation, focusing on reducing current and development expenditures more than on boosting domestic revenue. The deficit narrowed from 7.4% of GDP in 2021/22 to an estimated 5.1% in 2022/23. Since the rapid rise in public debt in response to the Covid-19 pandemic, public borrowing has been stabilizing. Despite a small increase in the debt-to-GDP ratio from 46.3% in 2020 to 49.6% in 2023, the risk of public debt distress is moderate, with the debt level considered sustainable. The current account deficit narrowed in 2023 but remained elevated at 7.9% of GDP. With the ratio of nonperforming loans to gross loans at 4.6% and a capital adequacy ratio (tier-1 capital to risk-weighted assets) of 25.3% in 2023, the financial sector remains well capitalized and able to withstand external shocks.

Previous gains in poverty reduction are reversing, with the poverty rate rising from 21.4% in 2017 to 30.1% in 2020.

Outlook and risks

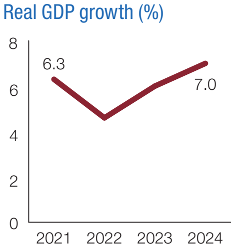
The economy is projected to expand by 6.0% in 2024 and 7.0% in 2025, buoyed by stronger regional growth as global supply chains normalize. The oil sector will continue ramping up investments in wells and pipelines, further underpinning growth and future exports. Rising imports of goods and services will keep the current account deficit elevated. Inflation is expected to converge to 5% as the Bank of Uganda maintains its tight monetary policy. The fiscal position is expected to further improve with continuing consolidation efforts. Nonetheless, external risks are tilted toward the downside. Supply chain disruptions around the Red Sea could slow trade as risk premiums rise, while intensifying regional insecurity could delay investments. Domestic risks are related to unexpected increases in public spending on infrastructure amid weak tax revenue performance. The International Monetary Fund's Extended Credit Facility will bolster reserves and set performance targets to guide the authorities.

Reform of the global financial architecture

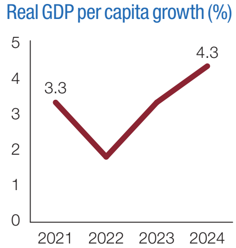
Despite a shift from agriculture to services, Uganda's structural transformation remains incomplete. Agriculture's contribution to GDP has declined from 53% in 1990 to 24% in 2022, yet 7 of 10 Ugandans are still subsistence farmers and working in low-value-added agricultural jobs, with agricultural labor productivity rising by just 26%. While productivity has advanced 294% in manufacturing and 164% in trade services, these sectors employ a small fraction of the workforce. Manufactured exports constituted only 13% of total exports in 2022. Accelerating structural transformation requires boosting agricultural productivity and investing in firms and jobs in industrial sectors and services. Also critical is scaling up skilling, promoting innovation through research, and boosting mechanization of agriculture.

The transition to higher value-added jobs requires greater investment in industry and services. Uganda receives $2 billion annually from development partners, but most of it is directed to social sectors. In the short term, the government could negotiate a reallocation of financing to productive sectors. Stronger collaboration between international financial institutions and the private sector is vital to providing risk capital for investment, for example, a green industrial finance facility. Over the medium term, government should increase financing for quality infrastructure and production factors to improve Uganda's export competitiveness, for example, by harnessing Global Gateway or Belt and Road Initiatives.

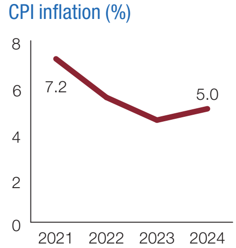
Real GDP growth (%)



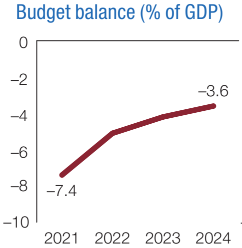
Real GDP per capita growth (%)



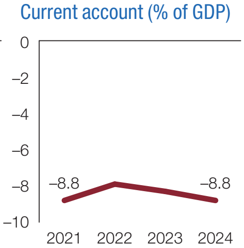
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Uganda's fiscal year, which runs from July 1 to June 30.

NORTH AFRICA

Algeria

Recent macroeconomic and financial developments

Economic growth rate accelerated from 3.6% in 2022 to 4.2% in 2023, driven by the hydrocarbon sector, industry, construction, and services. Inflation remained high (9.3% versus 9.2% in 2022) due to rising food prices. Monetary policy remained accommodative despite the central bank's decision in April 2023 to increase reserve requirements and accelerate liquidity absorption in the banking sector.

The budget deficit worsened, from 7.8% of GDP in 2022 to 10.2% in 2023, reflecting higher wage and pension payments for civil servants. Budget revenue rose around 5% from 2022, despite a slight drop in oil revenue. Public debt, mainly domestic, fell from 62.1% of GDP in 2021 to 55.1% in 2023. The external current account surplus narrowed substantially, from 8.6% of GDP in 2022 to 2.3% in 2023, leading to a drop in foreign exchange reserves from 18 months of import cover to 14 months. A new monetary and banking law was passed to stimulate financial innovation and inclusion and modernize financial supervision tools. The first two Algerian banks to open branches abroad were the Algerian Union Bank in Mauritania and the Algerian Bank of Senegal.

Unemployment remains high at 14.9% in 2022 and 14.5% in 2021. Since 2021, the government has instituted an unemployment benefit scheme, increasing the monthly amount to around $110 in December 2022.

Outlook and risks

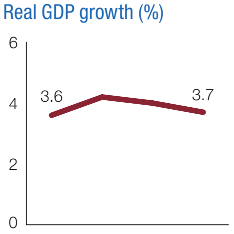
Real GDP growth is projected to continue at around 4% in 2024 and then slow to 3.7% in 2025. The hydrocarbon sector is expected to maintain its growth, with oil and natural gas exports growing at around 5% in 2024 and 2025. The upward trend in inflation is projected to reverse in 2024, falling to 6.8% in 2024 and 5.7% in 2025 as agricultural production increases. The budget deficit is projected to deteriorate to 11.1% of GDP in 2024 and 12% in 2025, under pressure from social spending, which is set to continue rising. The current account is projected to benefit from global disruptions to hydrocarbon supplies and remain in surplus, at 1.0% of GDP in 2024. The presidential election to be held in September 2024 is not considered a macroeconomic risk, given the stability of the national sociopolitical context. If the elections go well, the main risk for the economic outlook is the country's heavy dependence on the hydrocarbon sector.

Reform of the global financial architecture

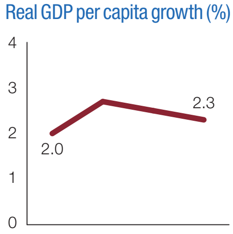
Economic growth depends heavily on the performance of the oil and natural gas sectors. Nevertheless, the share of hydrocarbons in GDP has been declining, from 44.3% in 2005 to 34.2% in 2012 and 19.5% in 2019, while that of services has been rising. The nonhydrocarbon industry's share of GDP has also been declining, from almost 15% in the early 1980s to 5.9% of GDP over 2015–19. Agriculture's share of GDP fell from 14% over 1990–99 to 10% over 2000–09 and then rose to 13% over 2010–16. By contrast, market services are on the rise, with their contribution to GDP rising from 25% in 2000–09 to 31% in 2010–16. The services sector's share of employment doubled from 13% in 2010 to 26% in 2018, while agriculture's share was almost halved, from 20.1% in 1990 to 10.4% in 2018.

The main development challenge remains the need to diversify its economy. Reforming the mechanisms of the global financial architecture would be in line with the government's vision of consolidating economic recovery and improving the business climate by accelerating the digital transition and developing the sectors driving development and economic growth, including agro-industry and fisheries. In the short term, it will be necessary to support local industries and invest in the technologies required for the industrialization strategy (digital economy and digitalization in particular).

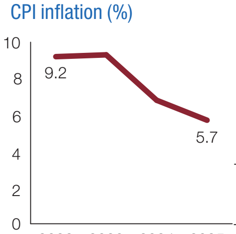
Real GDP growth (%)



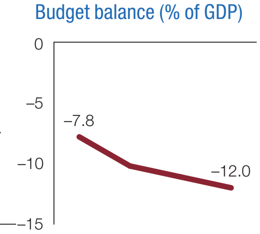
Real GDP per capita growth (%)



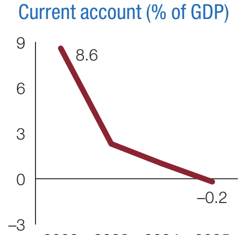
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Egypt

Recent macroeconomic and financial developments

Egypt's GDP growth declined to 3.8% in 2022/23, reflecting low performances in manufacturing and petroleum refining. Growth was propelled by private consumption and exports, despite high inflation. At 24% in 2022/23, inflation was well above the Central Bank of Egypt's (CBE) target of 7%, driven by rising international prices, domestic supply shocks, and exchange rate movements. The Egyptian pound lost 70% of its value against the US dollar between May 2022 and January 2023. To curb inflationary pressures, the CBE increased interest rates three times between March and August 2023.

The fiscal deficit decreased slightly to 6.0% of GDP in 2022/23, buoyed by higher tax revenues that raised the primary surplus to an estimated 1.6% of GDP. Central government debt increased to 95.7% of GDP in 2022/23, due largely to the devaluation of the Egyptian pound. The current account deficit narrowed to 1.2% of GDP in 2022/23 thanks to higher tourism receipts and Suez Canal revenues. Gross official reserves recovered slightly to $34.8 billion at the end of June 2023 (5.6 months of import cover).

The banking system remained well capitalized, at above the CBE's minimum threshold of 12.5%. Nonperforming loans improved from 3.4% in 2022 to 3% of gross loans in 2023. Government expenditures on subsidies and social protection programs increased to 20.4% of total expenditures in 2022/23 to reduce the impact of high inflation on households' purchasing power.

Despite these measures, the poverty rate, estimated at 29.7% in 2020, is expected to increase. Unemployment remained stable at an estimated 6.9% in 2023.

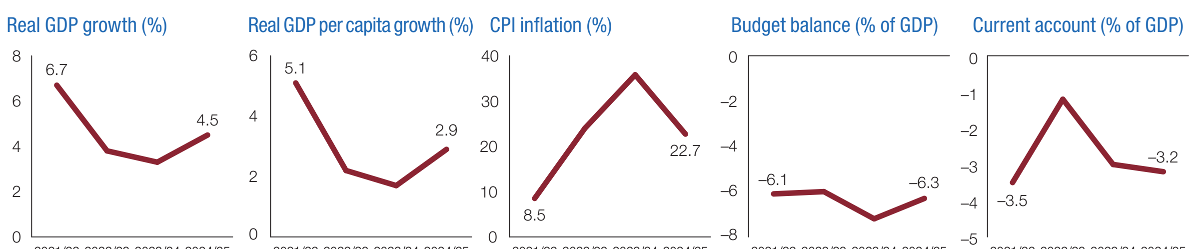
Outlook and risks

Egypt's economic outlook is positive, thanks to the strong financial support of international financial institutions and development partners. Egypt signed a $35 billion deal with the United Arab Emirates in February 2024 to develop the North Coast area of Egypt (Ras El Hekma). GDP growth is expected to decline slightly to 3.3% in 2023/24 before rising to 4.5% in 2024/25 within a more favorable economic context. The fiscal deficit is set to widen in 2023/24 due to higher interest payments but is then projected to improve in 2024/25. Inflation is expected to rise to 35.8% in 2023/24 before moderating to 22.7% in 2024/25 due to exchange rate movements. The current account deficit is projected to deteriorate slightly as tourism receipts and Suez Canal revenues decline. In the short term, Egypt remains vulnerable to global economic shocks, notably the war in Gaza, which poses a security risk in the Red Sea and could impair tourism receipts and Suez Canal revenues.

Reform of the global financial architecture

The structure of the Egyptian economy remained unchanged over the period 2012–2022, dominated by services (51% of GDP) and industries (34%). Manufacturing, estimated at 16.3% of GDP for the same period, has not yet emerged as an engine of structural transformation. Although employment in agriculture decreased by 9 percentage points over the period, employment shares in agriculture (19%) and services (53%) in 2022 remained higher than their output shares, indicating low productivity. The Egyptian economy benefits from a large consumer base, diversified economy, strategic geopolitical location, and several free trade agreements. However, structural transformation is impeded by slow private sector growth.

Creating an enabling environment for private sector development requires substantial public investment and additional resources, while Egypt is looking to reduce its public debt and interest service. Egypt could continue lengthening the maturity of its debt and diversifying its investor base to manage its refinancing needs. Reform of the global financial architecture, notably the proposal to increase development lending and improve terms of lending, could support Egypt's structural transformation and economic resilience. Egypt has always benefited from strong support from international financial institutions. A strategic partnership worth $8 billion was signed with the European Commission in March 2024, while the $3 billion International Monetary Fund program approved in December 2022 was increased to about $8 billion.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data in the figure correspond to Egypt's fiscal year, which runs from July 1 to June 30.

Libya

Recent macroeconomic and financial developments

Libya's economy is heavily dependent on oil and gas, which constitute 97% of exports, more than 90% of fiscal revenues, and 68% of GDP. In 2023, as the country recovered from the 2022 recession, GDP grew 12.6%, thanks to sustained oil production made possible by the improved security situation. On the demand side, growth remained driven by private consumption and exports. The inflation rate fell to 2.4% in 2023 as domestic supply chains improved.

The current account surplus shrank to 18.5% of GDP and the fiscal surplus to 0.1% of GDP as global oil prices declined. In the absence of a unified state budget for the East and West of the country, public salaries, operating expenses, and subsidies continue to be prioritized at the expense of public investment. Foreign exchange reserves stood at $82 billion at the end of 2023 (more than 4 years of import cover). In August 2023, the Central Bank announced its reunification with its eastern branch. The capital adequacy ratio averaged 17.5% over 2019–2022, above the Central Bank's threshold of 12.5%. The ratio of nonperforming loans to gross loans is high, estimated at 23.1% in the third quarter of 2023.

The number of people in need of humanitarian assistance declined from 1.5 million in 2021 to 803,000 in 2022 as security improved. The unemployment rate was estimated at 19.3% in 2022 (51.4% for youth), attributable to a labor market dominated by public sector and informal employment.

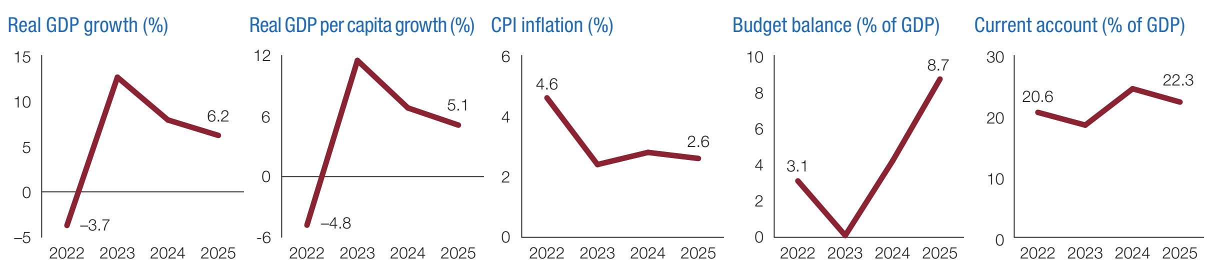
Outlook and risks

Libya's peace remains fragile as election challenges are still unresolved. The economy is projected to grow at 7.9% in 2024 and 6.2% in 2025, under the assumption that oil and gas prices and production remain stable. Inflation is forecast to remain subdued, at around 2.8% in 2024 and 2.6% in 2025, reflecting expected stability in global food prices. The fiscal surplus is projected to improve to 4.2% of GDP in 2024 and to 8.7% in 2025, while the current account surplus is expected to remain at double digits in 2024 and 2025 due to projected increases in oil and gas exports. Libya's political and security environments are fragile, highly dependent on the oil and gas sector, and vulnerable to climate change. A rise in insecurity could lead to an oil blockade and slow GDP growth, while a slowdown in global economic growth could negatively affect international oil prices, shrinking Libya's fiscal space.

Reform of the global financial architecture

Over 2004–2022, the industrial sector (led by oil and gas) contributed an estimated 61.7% to GDP, while manufacturing contributed just 4.0% and agriculture just 2.8%. In 2022, the employment shares of services (70%) and agriculture (9.2%) were higher than their output shares, indicating low productivity. Structural transformation in Libya has been hindered by limited political will and interest in economic diversification, weak capacity of institutions and policy coordination, and political instability and insecurity since 2011. Many sectors have been paralyzed by more than a decade of conflict.

Libya has the necessary financial resources to support a structural reform program. Historically, Libya has relied little on external borrowing thanks to its abundant foreign reserves from oil and gas exports. However, reform of the global financial architecture to increase development lending and make it more affordable could create incentives for Libyan authorities to turn to external borrowing. Indeed, substantial financing needs are expected for the country's reconstruction and post-conflict recovery. Structural transformation will require achieving political stability and building strong and efficient institutions, in addition to implementing a holistic structural reform program to create a conducive environment for private investment and build modern and sustainable infrastructure.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Mauritania

Recent macroeconomic and financial developments

The economic growth rate fell from 6.4% in 2022 to 3.4% in 2023, reflecting a drop in industrial and fisheries production on the supply side and lower public investment on the demand side. Inflation fell from 9.6% in 2022 to 5% in 2023, due to tighter monetary policy and deceleration in food prices.

The budget deficit improved from 3.6% of GDP in 2022 to 2.3% of GDP in 2023, as tax revenue rose from 13.1% of GDP in 2022 to 14% in 2023. Public debt fell from 52.4% of GDP in 2021 to an estimated 48% in 2023 following a debt restructuring agreement with Saudi Arabia. As a result, the risk of debt distress dropped from high to moderate in 2023. The current account deficit improved from 14.7% of GDP in 2022 to 9.8% in 2023, due to the rising value of exports, iron ore specifically, and reduced imports of food and petroleum products. The soundness of the banking sector improved. Nonperforming loans fell from 43.3% of gross loans in 2021 to 35% in 2022. The overall capital adequacy ratio was 18% in 2022, against a 10% norm.

The Covid-19 pandemic, inflationary pressures in 2022, and climate shocks had a negative impact on people's social circumstances, leading to an increase in the extreme poverty rate from 5.4% in 2019 to 6.3% in 2022. Youth unemployment, estimated at 24% in 2023, remains high.

Outlook and risks

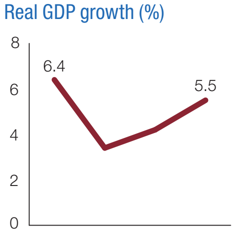
The economic outlook remains favorable, with real GDP growth projected at 4.2% in 2024 and 5.5% in 2025, underpinned by the expected export receipts from gas production scheduled for late 2024, which is projected to generate approximately $500 million in annual revenue over 2024–51. With a continuing restrictive monetary policy and good agricultural prospects, the country is projected to contain inflation at 4.7% in 2024 and 4.2% in 2025. The budget deficit is projected to improve to 2% of GDP in 2024 and to 1.6% in 2025, linked to additional revenue generated by the gas sector. Public debt is projected to fall in the short term, keeping the risk of debt distress moderate. The current account deficit is projected to improve to 8.5% of GDP in 2024 and 7.4% in 2025, due to projected increases in gas exports and a drop in food and oil import costs. These forecasts face major risks, including security tensions in the Sahel, unfavorable fluctuation in iron ore prices, delays in the launch of the Grand Tortue Ahmeyim gas project, and the impacts of climate change.

Reform of the global financial architecture

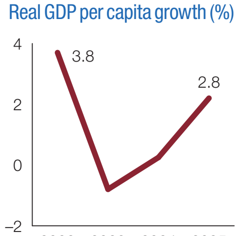
Progress in structural transformation has been slow, attributable to a growth model based on extractive resources. Manufacturing's share of GDP fell from 10.4% in 2000 to 6.5% in 2022, and agriculture contracted from 26.1% to 23.2%. The economy is dominated by services, which accounted for 46% of GDP in 2022, compared with 42.4% in 2000. Agriculture's share of employment fell from 44.8% in 2000 to 33% in 2022, and industry's share fell from 15.3% to 14.7%. Employment migrated to informal services (52.3%, up from 39.9%). To accelerate structural transformation and avoid Dutch disease will require redirecting gas revenues to diversify the economy; developing local value chains and infrastructure; improving the business climate to develop the private sector; strengthening human capital; and accelerating digitalization of the economy.

In addition, the country should improve its access to international financial markets to finance its structural transformation. To enable Mauritania to take greater advantage of the global financial architecture, development partners must support its sovereign credit rating process, which is a prerequisite for issuing debt on international markets, and increase concessional financing. The government must ensure sound management of debt and gas revenue, improve the business climate, and develop the domestic financial market with the introduction of green bonds.

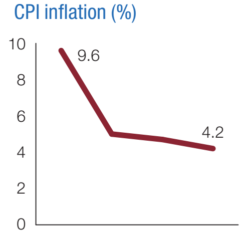
Real GDP growth (%)



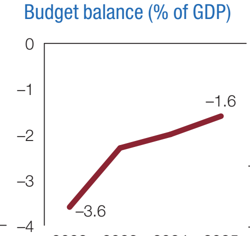
Real GDP per capita growth (%)



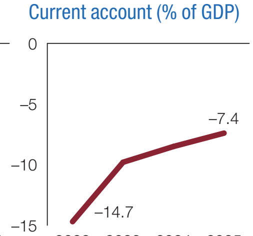
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Morocco

Recent macroeconomic and financial developments

After weak economic performance in 2022, with growth of just 1.3%, growth rebounded in 2023 to 3.02%, due to the revival of agricultural activities and services and moderate recovery in domestic demand. Inflation fell to 6.1% in 2023, after peaking at 6.6% in 2022, as imported inflationary pressures eased. The budget deficit improved from 5.2% of GDP in 2022to 4.7% in 2023, due to the combined effect of strong budget revenue and lower subsidies. The 2023 financing requirement was covered mainly by issuing eurobonds, after a period when government securities were used. Public debt was estimated at 69.7% of GDP in 2023, compared with 71.5% in 2022. The current account deficit decreased by 2 percentage points, from 3.5% in 2022 to 1.4% in 2023, due to a smaller trade deficit, record tourism receipts, and higher remittances. Foreign exchange reserves covered 5.1 months of imports in 2023, down from 5.5 months in 2022. The financial system is sound, with an average bank solvency ratio of 15.8% at the end of June 2023, compared with 15.6% in 2022, and nonperforming loans stabilized at 8% of gross loans.

Morocco, an upper-middle-income country, had an income per capita of $9,410 in purchasing power parity terms in 2022. Progress must be consolidated through more inclusive growth to reduce the poverty rate, which rose from 3% in 2021 to 4.9% in 2022, and mitigate the rise in the unemployment rate, which rose from 11.8% in 2022 to 13% in 2023, affecting especially young people (35.8%), college graduates (19.7%), and women (18.3%).

Outlook and risks

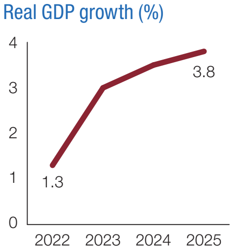
GDP growth is projected to rise moderately to 3.5% in 2024 and strengthen to 3.8% in 2025, boosted by higher investment. Inflation is projected to fall slightly to 4.1% in 2024 and 3.8% in 2025, as world food prices decline. The budget deficit could fall gradually to 4.4% of GDP in 2024 and 4.2% in 2025, benefiting from economic recovery and lower subsidies on butane gas prices. The current account is projected to record a small deficit of 0.4% of GDP in 2024, worsening moderately to 0.9% of GDP in 2025, as a result of higher imports. Growth prospects could be reduced by poor rainfall or slower economic growth in the European Union, which could worsen terms of trade. Rising tensions related to Russia's invasion of Ukraine could trigger another shock in food prices. Risk mitigation factors include implementing structural mechanisms to manage climate shocks and natural disasters and the royal social protection initiative.

Reform of the global financial architecture

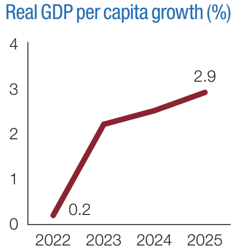
Structural transformation has been slow and has benefited the services sector, with the workforce shifting from agriculture to services and industries. From 2011 to 2022, the services sector accounted for 52% of GDP and employed 42.3% of the working population. Over the same period, the industrial sector accounted for approximately 25% of GDP, and the manufacturing sector for 14.7%. Manufacturing's share of employment fell from 12.2% in 2000 to 11% in 2019. Agriculture accounted for approximately 35% of employment in 2011–2022.

The country has prepared a new development model to strengthen its structural transformation by making it more inclusive. The model promotes manufacturing, trade integration, infrastructure connectivity, and human capital development. To implement this model while taking advantage of the global financial architecture, Morocco must maintain access to high volumes of lower-cost external financing with long maturities. The country can take advantage of increased Special Drawing Rights at the International Monetary Fund, partial guarantees of credit risk from multilateral development banks, and climate funds to mitigate water stress. It must implement reforms to position itself in global value chains, mobilize more domestic resources by developing the private sector, rationalize tax spending, and make public procurement more open to micro, small, and medium enterprises.

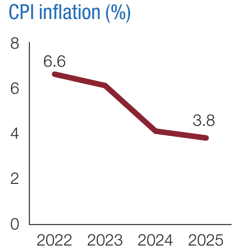
Real GDP growth (%)



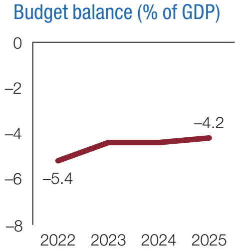
Real GDP per capita growth (%)



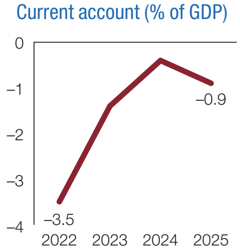
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Tunisia

Recent macroeconomic and financial developments

The GDP growth rate fell to 0.4% in 2023, due to the drought that hurt the agricultural sector and a decrease in domestic demand. Inflation continued to rise, reaching 9.3% in 2023 fueled by higher commodity prices.

Despite a tax burden of 24.5%, the budget deficit remained unchanged at 6.8% of GDP in 2023. The current account deficit improved to 2.8% of GDP, due to reduced imports and resilience in manufacturing exports, tourism receipts, and remittances. The improvement in the current account deficit bolstered foreign exchange reserves ($7.3 billion by end-2023). But the dinar–US dollar exchange rate, which remains volatile, depreciated over 2023. Public debt, 60% of which is external, rose from 77.6% of GDP in 2022 to 80.2% in 2023. A February 2024 law authorized the central bank to grant exceptional financing of 7 billion dinars ($2.2 billion) to the treasury on advantageous terms, enabling the government to meet some of its external debt repayments. The bank solvency ratio consolidated to 14% in 2022, up from 13.3% in 2021, and the share of nonperforming loans fell from 13.1% of gross loans in 2021 to 12.6% at the end of 2022, due to loan writeoffs.

Tunisia ranks 101st of 193 countries worldwide on the 2022 Human Development Index and 5th of 54 African countries. Unemployment stood at 16.4% in the fourth quarter of 2023, particularly affecting youth ages 15–24 (40.9%), college graduates (23.2%), women (22.2%), and inland regions. The poverty rate, at 15.3% nationally, is higher in rural areas (26%) than in major urban centers (6.3%).

Outlook and risks

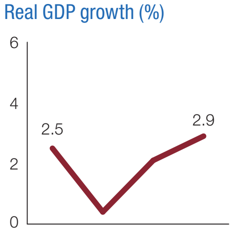
GDP growth is projected to remain modest in the medium term, at 2.1% in 2024 and 2.9% in 2025. Inflation is projected to be 7.1% in 2024 and to fall gradually to 6.7% in 2025, as global inflationary pressures ease. The budget deficit is projected to improve to approximately 6% in 2025 as fiscal discipline is maintained. But the current account deficit is expected to worsen gradually to 4% in 2025, due to imports of capital goods needed to boost economic growth. The medium-term economic outlook could worsen due to high risk of debt distress limiting access to external financing, social tensions caused by the high cost of living, and continued high interest rates in developed economies. But accelerating reforms (in particular, those aimed at improving governance of public enterprises, the business climate, and control of current spending) could boost growth and reverse the debt trajectory. Moody's outlook on the country's sovereign rating (Caa2) was upgraded from negative to stable in March 2024, due to the rise in foreign exchange reserves.

Reform of the global financial architecture

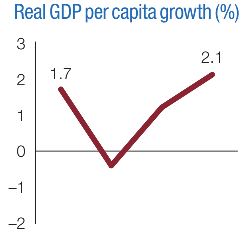
The structural transformation of the economy is benefiting the services sector (which accounts for 65% of GDP) rather than industry (which accounts for 25% of GDP). From 1990 to 2020, agriculture's share of employment fell from 24% to 14.5%, mainly favoring services, which accounts for 52% of employment. Industrial productivity has been declining for two decades. Around 96% of businesses are micro, small, or medium enterprises, and the informal sector accounts for almost two-thirds of employment.

Reforming the global financial architecture would facilitate the mobilization of resources for the structural transformation of the economy. The reform could include the adoption of guarantees and risk-sharing instruments to mobilize more private resources for green industrialization and the creation and modernization of regional financial markets to favor the deployment of green bonds and access to local currency financing for small and medium enterprises. Other measures that Tunisia could implement to accelerate structural transformation include restoring public finance sustainability to secure the support of development partners and improve investors' risk perceptions; accelerating the upgrading of industry; improving the business climate; developing human capital; facilitating access to financing and formalization for micro, small, and medium enterprise; and digitalizing and strengthening the resilience of its economy.

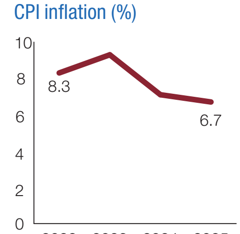
Real GDP growth (%)



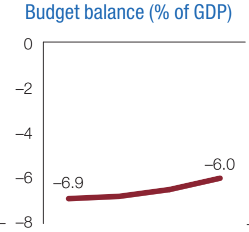
Real GDP per capita growth (%)



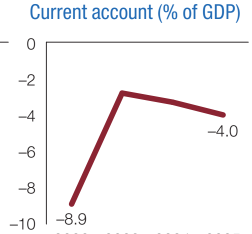
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

SOUTHERN AFRICA

Angola

Recent macroeconomic and financial developments

Angola is one of the most oil-dependent African countries, with oil accounting for 28.9% of GDP and 95% of exports. Oil also affects growth indirectly in non-oil sectors. GDP grew an estimated 0.9% in 2023, much lower than the 3.5% projected at the beginning of the year and the 3% growth in 2022. The first half of 2023 was marked by falling oil production and prices, higher external debt amortizations as the debt service moratorium ended, and a 60% currency devaluation. Driven mostly by the devaluation and the high share of dollar-denominated debt, the public debt-to-GDP ratio rose to 84% at the end of 2023 after falling to 69.2% in 2022. On the positive side, the ratio of debt service to total income declined from 279% in 2022 to 100% in 2023, reflecting the efficacy of the authorities' strategy to reduce financing costs.

Inflation dropped from 21.7% in 2022 to 13.6% in 2023, with food prices accounting for 68.8% of the national consumer price index. The National Bank of Angola raised the basic interest rate to 18% in November 2023 and 19% in March 2024 and increased the reserve requirement ratio in national currency. The decline in imports compensated for the 28% drop in exports in 2023, leaving international reserves basically unchanged at the end of 2023 ($14.7 billion) from the end of 2022 ($14.6 billion), equivalent to 7.5 months of import cover.

Angola was ranked 148 of 191 countries on the Human Development Index in 2021, and the official monetary poverty rate was 40.6% in 2019. Most jobs in Angola are informal (79.9%), and the unemployment rate is high (29.6%), driven by rural areas (38%) and youth (52.9%).

Outlook and risks

The short-term outlook has deteriorated. Inflation is expected to peak at 18.1% in 2024 and then drop to 12.4% in 2025, driven largely by the currency devaluation in 2023. The basic interest rate was raised to 19% in March 2024. The government is managing this shock by tightening fiscal policy (the 2024 budget considers lower oil production and prices) and taking fiscal consolidation measures (including reducing fuel subsidies), showing enhanced resilience.

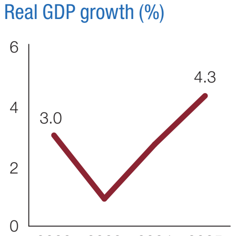
After debt repayments of $18 billion in 2023 and $14 billion in 2024, the debt repayment profile is projected to decline going forward, opening up more fiscal space. The International Monetary Fund shares this positive perspective on Angola's risks, projecting a 14 percentage point decline in the debt-to-GDP ratio in 2024, from 84% to 70%, in its March 2024 Country Report.

Reform of the global financial architecture

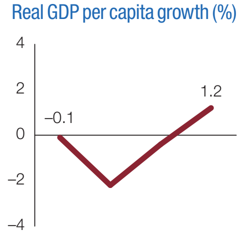
Economic diversification remains elusive as oil production declines and global decarbonization looms in the medium term. The agriculture sector has grown faster than the economy for four consecutive years, and several indigenous private sector companies have diversified their portfolio from oil services and construction into agro-processing. However, structural transformation must be accelerated and consolidated, and several sectors still need to be opened to foreign direct investment. The government has identified agribusiness and agriculture as the drivers of industrialization and job creation over the next five years. Additional support will come from investment in infrastructure, especially through integrated development corridors such as the Lobito corridor, the first public-private partnership in the country.

The government has a stated policy of longer-term borrowing from multilateral institutions to fund its development expenditures. It has progressively substituted more expensive resource-backed loans and prefers issuing longer-term debt instruments to smooth out repayment peaks. Under the country's decarbonization agenda, the energy system received the largest share of climate finance, at 69%. Cross-sectors followed, with 19%, while agriculture, forestry, other land use, and fisheries together received 11%. Public finance sources account for the majority of climate finance in Angola, at 88%. Among these finance sources, development finance institutions hold the largest share, at 44%, and the private sector accounts for 17%.

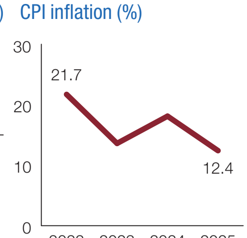
Real GDP growth (%)



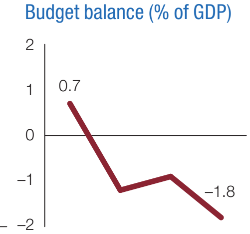
Real GDP per capita growth (%)



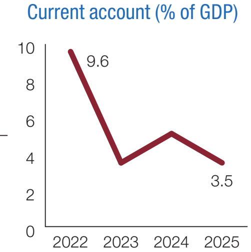
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Botswana

Recent macroeconomic and financial developments

Real GDP growth shrank to 2.7% in 2023 as water and electricity production declined and the diamond trade slowed. The declines reflected drought conditions and weak global diamond demand. Average inflation fell to 5.3% in 2023—within Bank of Botswana's 3%–6% acceptable range—reflecting downward domestic fuel price adjustments and lower imported inflation. In April 2024, with inflation expectations well anchored, the central bank maintained its monetary policy rate at 2.4% after having reduced it by 25 basis points in December 2023.

The 2023/24 fiscal deficit widened to 2.5% of GDP, driven by lower -than -expected mineral earnings and higher -than -planned recurrent spending. Public debt was sustainable at 22.0% of GDP. The decline in the current account surplus to 0.9% of GDP in 2023 reflected lower mineral exports and Southern African Customs Union (SACU) revenues. International reserves improved to $4.8 billion in January 2024 (8.7 months of import cover), up from $4.0 billion at the end of 2022 (7.6 months). Year on year, the pula appreciated by 0.8% against the South African rand and depreciated by 3.4% against International Monetary Fund Special Drawing Rights in March 2024.

The banking sector's capital adequacy ratio averaged 19.7% in 2023, above the 12.5% prudential floor. The nonperforming-loan-to-gross-loan ratio was stable at 3.7% in December 2023 against 3.8% in December 2022.

Botswana's poverty headcount ratio shrank from 17.0% in 2019 to 14.5% in 2022. In 2021, 20.8% of the population was multidimensionally poor. Unemployment was high, at 25.9% (25.4% in 2022), driven by 34.4% youth unemployment (third quarter of 2023).

Outlook and risks

Growth is expected to rebound to 4.0% in 2024 as diamond sales recover. The outlook's downside risks include higher than expected inflation from supply chain disruptions as geopolitical tensions rise, weaker diamond trade if demand remains depressed, El Niño-driven weather patterns, and the potential for persisting weak economic conditions in South Africa. With the economy operating below full capacity, inflation may fall to 4.5% in 2024, staying within the central bank's range. A narrowed fiscal deficit of 1.8% of GDP in 2024/25 will be supported by improved public finance management, business environment reforms, and successful implementation of the two-year Transitional National Development Plan. A current account surplus is projected, with higher diamond earnings and SACU revenues. Unemployment may be addressed in part by the 2023 De Beers diamonds sales deal in which Botswana's higher control of diamond production (from 25% to 50%) is expected to generate new jobs along the industry's value chains.

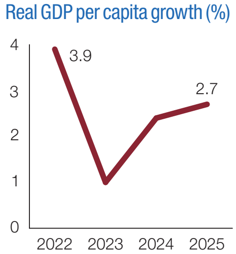
Reform of the global financial architecture

Botswana is stable with strong institutions and democratic governance. The country prudently manages its diamond flows through the Pula Sovereign Wealth Fund and has been diversifying away from mining. The contribution of non-minerals in real GDP rose from 71.1% in 2013 to 76.2% in 2023. Over the same decade, the mining sector's GDP contribution fell from 20.0% to 16.7%, and its share of employment dropped from 5.8% to 1.4%. Industry's contribution fell from 18.2% to 16.6%, and its share of employment dropped from 31.4% to 16%. Agriculture's GDP contribution declined from 2.0% to 1.6%, but its share of employment rose from 3.1% to 9.8%. Services' contribution increased from 59.6% to 65.1%, and its share of employment rose from 39.7% to 56.1%. To advance its structural transformation, Botswana should target higher value addition in sectors with the highest job creation potential.

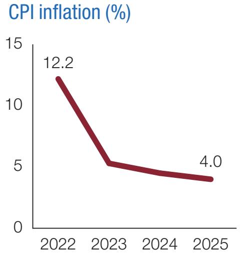
To close the 41% financing gap in its $4.7 billion public investment program and position itself to take full advantage of the redesigned global financial architecture, Botswana could emphasize reforms that sustainably improve its legal and operational efficiencies to attract higher private capital flows. Botswana could also strengthen and mainstream the technical skills necessary for effective engagement in global financial negotiations and identification of well-targeted bankable projects for investment.

Real GDP growth (%)

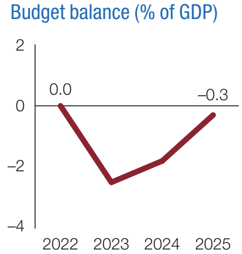
Real GDP per capita growth (%)



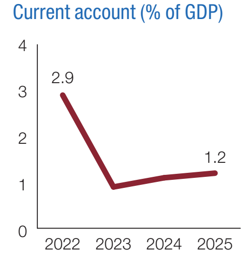
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. The fiscal years start in the named April and conclude the end of March in the following year.

Lesotho

Recent macroeconomic and financial developments

Lesotho's economic growth decelerated from 1.3% in 2022 to an estimated 0.9% in 2023 owing to slowing manufacturing and agricultural activities. Inflation dropped from 8.3% in 2022 to about 6.4% in 2023, as food inflation declined in South Africa, Lesotho's main trading partner. Public debt fell from 60.6% of GDP in 2022 to 57.5% in 2023, mainly because of the redemption of treasury bonds. Official reserves stood at 4.7 months of import cover in 2023.

The loti, which is pegged at par with the South African rand, depreciated against all major currencies in 2023, including the euro (12.58%), the pound (24.73%), and the US dollar (29.63%) as the rand depreciated. Following a deficit of 4.3% of GDP in 2022, the fiscal balance was estimated at a surplus of 1.0% in 2023 as South African Customs Union (SACU) revenues recovered. The current account deficit improved from 8.4% of GDP in 2022 to an estimated 3.4% in 2023, due to rising textile exports. The deficit was financed with South African capital transfers (foreign direct investment flows). The banking sector is sound. Monetary policy tightening led to a decline in nonperforming loans from 4.2% of gross loans in 2020 to 3.84% in December 2023. The capital adequacy ratio dropped from 22.95% in December 2020 to 17.16% in December 2023, which is still above the 8% minimum prudential requirement.

Outlook and risks

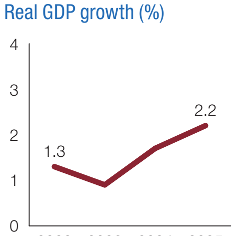
Real growth in GDP is projected to rise to 1.7% in 2024 and 2.2% in 2025 with expected recovery in the mining and manufacturing sectors. The fiscal balance is projected to deteriorate from a surplus of 1% in 2023 to a deficit of 0.4% of GDP in 2024 and then to 3.3% in 2025 owing to elevated expenditures associated with the second phase of the Lesotho Highlands Water Project. The current account deficit is projected to deteriorate further to 3.4% in 2024 and 4.2% in 2025 due to an increase in imports associated with the second phase of the Lesotho Highlands Water Project. The risks to the domestic outlook are diverse. Inflation could remain high if some of the upside risks to inflation materialize. Global economic growth could come out weaker than projected, negatively affecting Lesotho's export-oriented industries, especially textiles. Declining manufacturing activity could slow economic growth and job creation, compounded by the uncertainty surrounding renewal of the US African Growth and Opportunity Act. Finally, South Africa's persistent economic underperformance is likely to spill over to Lesotho, given the close commercial ties between the two countries. Fiscal consolidation and improvements in public financial management are expected to restore fiscal sustainability.

Reform of the global financial architecture

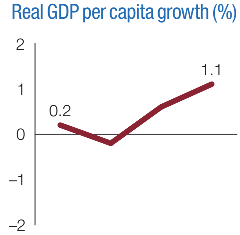
Lesotho's economy has undergone some structural transformation since the 1990s. Between 1990 and 2022, manufacturing grew from 13.2% of GDP to about 22%, and the service sector's share expanded from 40.3% to about 60%. At the same time, agriculture's share of GDP plummeted, from 20% to 5.12%. Despite this structural transformation, Lesotho lacks the financial capacity to address its challenges. The global financial architecture has not provided Lesotho with the resources needed to support its development agenda. For example, of the total $650 billion in Special Drawing Rights issued by the International Monetary Fund, Lesotho received only $43.028 million.

The global financial architecture needs to be reformed in order to help countries in need like Lesotho. Multilateral financial institutions should expand their contingency financing to such countries, which are frequently stricken by drought and other shocks, and scale up their development and climate finance to resource-poor countries like Lesotho. Lesotho should enhance its domestic resource mobilization and strengthen its public finance management. It should also build fiscal buffers using revenues from diamond exports. Finally, the government should restore fiscal sustainability through fiscal consolidation.

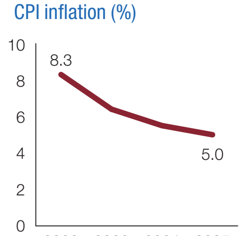
Real GDP growth (%)



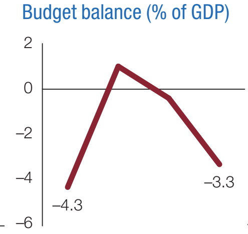
Real GDP per capita growth (%)



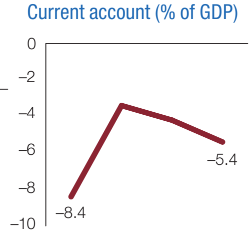
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Lesotho's fiscal year, which runs from April 1 to March 31.

Madagascar

Recent macroeconomic and financial developments

Economic activity remained robust in 2023, with growth estimated at 4.4%, up from 4.3% in 2022. Growth was driven by extractive industries (up 5.2%), tourism (up 14.6%), and telecommunications (15.2%) on the supply side and by buoyant exports and booming public investment (12.2% of GDP in 2023, up from 5.4% in 2022) on the demand side. Inflation rose from 8.2% in 2022 to 9.9% in 2023, driven by the continuing rise in energy and food prices.

Higher spending, linked to measures for mitigating the effects of the Covid-19 pandemic and Russia's invasion of Ukraine, increased the budget deficit from 5.4% of GDP in 2022 to 6.1% in 2023. The deficit was financed by public debt, which rose from 54.9% of GDP in 2022 to 56.1% in 2023. But the risk of debt distress remains moderate. Buoyant prices for export products (nickel, cobalt, graphite) and the upturn in tourism narrowed the current account deficit from 5.3% of GDP in 2022 to 4.5% in 2023. Overall, the financial system is healthy, with credit to the economy up 11% in 2023, and the bad debt ratio down from 9.1% at the end of 2022 to 8.3% at the end of 2023.

According to the World Bank, the national poverty rate remains high, at 75.2% in 2022. Poverty is especially high in the south and the southeast, where it exceeds 91.2%, due to climate shocks (droughts, cyclones, and floods). Income inequality is high, with a Gini coefficient of 0.368 in 2022. The unemployment rate was an estimated 6.6% in 2022, according to the country's National Institute of Statistics, and youth ages 15–30 account for 70% of the unemployed according to the International Labour Organization. .

Outlook and risks

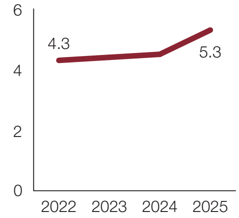
The economic outlook is good, with projected growth of 4.5% in 2024 and 5.3% in 2025. Growth is expected to be driven by strong performance in the mining sector, recovery in tourism, a surge in public investment, and buoyant exports (graphite, nickel, cobalt) due to sustained global demand for these minerals, which support the country's energy transition. Continuing restrictive monetary policy is expected to lower inflation to 8.1% in 2024 and 7.5% in 2025. The budget deficit is projected to improve to 4.1% of GDP in 2024, due to an anticipated rise in oil product revenue as a result of reforms, but then to worsen to 4.6% in 2025. The current account deficit is projected to narrow to 4.4% of GDP in 2024 and to 4% of GDP in 2025. The main downside risks to the outlook are climate shocks, rising energy and food prices, and geopolitical tensions (Russia's invasion of Ukraine and the war in the Middle East). These risks could be mitigated by implementing the General State Policy and reforms in public finance, mining, telecommunications, and energy, with the support of development partners.

Reform of the global financial architecture

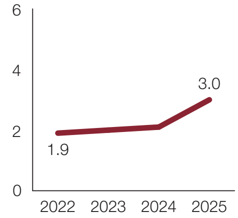
Over the past two decades, the country's economic structure has undergone a structural change in favor of industrialization, with increased investment in the mining sector. But because mining is not labor intensive, the transformation has been too slow to substantially reduce poverty. The industrial sector's share of GDP rose from 16% in 2000 to 27% in 2021, but its share of employment remained at an average of 8.5%. Agriculture's share of GDP fell from 29% in 2000 to 25% in 2021, and services' share fell from 55% to 48%. But services' share of employment rose from 14.7% in 2000 to 27.4% in 2021, though mostly in informal activities, to the detriment of employment in agriculture, which fell from 77% to 64.1% .

The structural transformation should be accelerated by implementing the Industrial Programming Agreement, which aims to speed up and diversify industrialization by 2040. Similarly, the country should boost domestic revenue, develop the domestic financial market, improve the business environment, and build resilient infrastructure. It should also take advantage of a reformed global financial system, enabling access to more concessional resources, co-financing, mixed financing (climate, green, and blue bonds), International Monetary Fund Special Drawing Rights mobilization, and facilitation of private investment and trade.

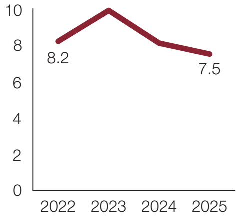
Real GDP growth (%)



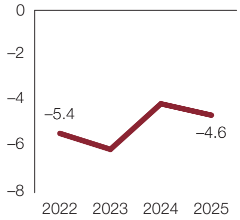
Real GDP per capita growth (%)



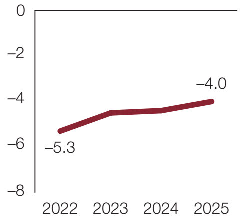
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Malawi

Recent macroeconomic and financial developments

Real GDP growth is estimated at 1.5% in 2023, a moderate recovery from 0.9% in 2022. Cyclone Freddy reduced agricultural output and disabled a third of the country's power generation, slowing industrial activity. Falling real incomes due to elevated inflation, monetary tightening, and foreign currency shortages reduced both corporate and consumer demand. Inflation rose from 20.8% in 2022 to 28% in 2023 despite a tightening of monetary policy that raised the policy rate by 400 basis points to 22% by end of 2023. The Malawi kwacha remains under pressure as indicated by an increasing parallel foreign exchange market premium. Following devaluations of 25% in May 2022 and 44% on 9 November 2023, exchange rate premium fell from 50% to 4.1% but quickly rose to 12.1% by the end of November 2023. Official foreign exchange reserves of $198.8 million in 2023 represent less than one month of import cover.

The fiscal deficit widened from 9.6% of GDP in 2022 to 10.1% in 2023 reflecting a budget-exceeding wage bill and underperforming revenues. Public debt was 82.1% of GDP in 2023, an increase of 5.6% over the previous year. The current account deficit widened from 2.8% of GDP in 2022 to 7.3% in 2023 as the economic recovery led to rising import demand. Weak overall export performance has kept international reserves low. At 6.6% of gross loans on 31 December 2022, nonperforming loans were above the internationally accepted level of 5%. Despite the financial sector's profitability in 2023, its increasing exposure to government poses a threat to stability. The core capital ratio for the banking sector rose from 17% in 2021 to 19% in 2022 and the total capital ratio rose from 20% to 22.4%.

Poverty remains a challenge, with 72% of the population below the $2.15 international poverty line in 2023, up somewhat from 70.1% in 2019. The unemployment rate improved slightly, from 6.8% in 2022 to 6.7% in 2023.

Outlook and risks

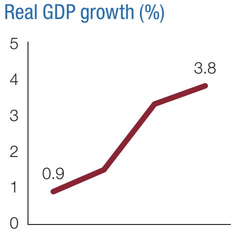
Economic growth is projected at 3.3% in 2024 and 3.8% 2025, lower than the January 2024 projections due to the negative impact of drought on agriculture. Growth will be driven by the mining, retail, and tourism sectors. Inflation is projected to remain elevated due to a poor agricultural season. Fiscal consolidation measures are expected to narrow the fiscal deficit to 8.7% in 2024 and 7.6% in 2025. As the economy recovers, the current account deficit is projected to widen in both 2024 and 2025, when it could reach 9.5%. Malawi's economy faces significant headwinds, most notably a shortage of international reserves, macroeconomic instability, and drought. Dependence on rain-fed agriculture, given the increasing vulnerability to climate change, is also a major risk. Ongoing debt restructuring negotiations, if successful, could reduce debt to sustainable levels. Increased inflows of donor resources following the approval of the International Monetary Fund Extended Credit Facility in late 2023 are likely to reduce the foreign currency squeeze.

Reform of the global financial architecture

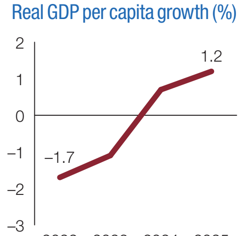
Since 1990, Malawi's economy has been dominated by services, at 55% of value added, and agriculture, at 31%. Manufacturing contributed an average of about 10% of value added over the same period, while all the other sectors contributed a meagre 5%. Agriculture's share of employment has fallen from its peak of 86% in 1990 to about 60% in 2021, while services' share has more than trebled, from 9% to about 30%. To radically transform the economy, manufacturing capacity, underpinned by agricultural-based diversification and beneficiation in the minerals sector, needs to expand. Increased inflows of global climate funds are needed to help Malawi adapt to climate change and mitigate its challenges.

The International Monetary Fund estimated that Malawi needed about $1.6 billion (almost 5 times larger than 2023 receipts) in external financing to meet its development needs in 2023 alone. Meeting the financial needs of the country requires increasing both external and domestic resource mobilization, including debt and nondebt sources. Because of its debt distress, Malawi must emphasize nondebt or highly concessional financing, including the restructuring of existing debt under the G20 Common Framework to achieve debt sustainability. Malawi needs to tap into global nondebt financing instruments such as carbon trading; enhance private sector financing, including through domestic financial sector deepening; and access cheaper foreign financing through blended financing instruments.

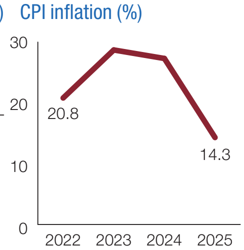
Real GDP growth (%)



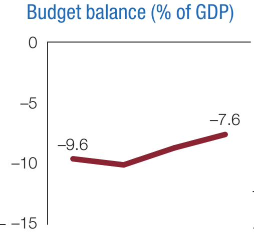
Real GDP per capita growth (%)



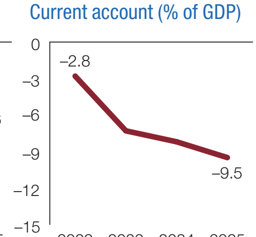
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Malawi's fiscal year, which runs from July 1 to June 30.

Mauritius

Recent macroeconomic and financial developments

Real GDP growth remained robust at 7% in 2023, though down from 8.9% in 2022. Growth was driven by services (construction and tourism) on the supply side and by consumption and investment on the demand side. Since the beginning of 2023, the authorities have paused monetary policy tightening as inflationary pressures eased. Average headline inflation declined from 10.8% in 2022 to 7.0% in 2023 as international commodity prices fell.

The fiscal deficit narrowed from 6.1% of GDP in 2021/22 to 5.3% in 2022/23 as fiscal consolidation measures focused on boosting revenues and containing expenditure. Gross public debt decreased from 86.1% of GDP in 2022 to 79% in 2023 due to sustained economic recovery and measures to improve debt sustainability. The current account deficit narrowed from 11.7% of GDP in 2022 to 5.1% in 2023, driven by tourism earnings and a larger surplus in the primary income account. The current account deficit was financed by the financial account. Gross international reserves stood at $6.7 billion at the end of October 2023, offering 10 months of import cover, a decline from 13.5 months at the end of October 2022. Nonperforming loans stood at 5.8% of gross loans in September 2023, up from 5.2% in September 2022, while the ratio of regulatory capital to risk-weighted assets was 21.3% in September 2023.

The poverty rate (at the international poverty level of $6.85 a day for upper-middle-income countries) was estimated at 13% in 2023, down from 17% in 2020. Unemployment was an estimated 6.1% at the end of 2023, while youth unemployment was 17.3%.

Outlook and risks

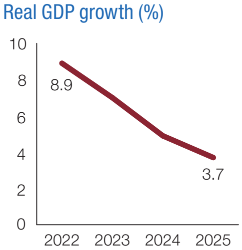
Growth is projected to slow to 4.9% in 2024 and 3.7% in 2025 on expected weaker external demand for exports. Inflation should decline to 5.8% in 2024 and 5% in 2025 due to a projected easing of global commodity prices. The fiscal deficit is expected to narrow further to 4.5% of GDP in 2024 and 4.3% in 2025, attributable to higher tax revenues supported by robust economic growth and expenditure rationalization. The current account deficit is projected to narrow further to 4.2% of GDP in 2024 and 4.5% in 2025, driven largely by solid performance in the tourism sector. Risks to the growth outlook remain, however, and include uncertainties due to persistence of the economic effects of Russia's invasion of Ukraine, an elevated debt burden, geopolitical fragmentation, and the impact of climate change. Moreover, the rapidly aging population could put greater fiscal pressure on the universal welfare system, making long-term growth more vulnerable. Risk mitigation measures could include strengthening tax enforcement and compliance, prioritizing domestic debt to reduce foreign exchange risks, stepping up reforms to gain greater access to global climate funds, and more tightly targeting welfare programs.

Reform of the global financial architecture

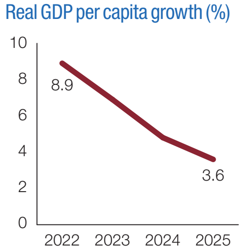
Agriculture's (including forestry and fishing) share of GDP declined from 6.1% in 2001 to 3.5% in 2022, while its share of total employment shrank from 11.7% to 5%. Over the same period, industry's shares also declined, from 26.7% of GDP to 18% and from 36.5% of employment to 21.5%, while services' shares increased from 56% of GDP to 66% and from 51.6% of employment to 73.4%. The declining shares of agriculture and the rising shares of services highlight the remarkable progress Mauritius has made in structural transformation. To consolidate these gains, the country should foster economic diversification and address climate change vulnerabilities so that it can move up the value chain and become a high-income country.

To finance its development priorities and address structural vulnerabilities, Mauritius needs to enhance its domestic resource mobilization and tackle its debt vulnerability risks, including limiting its exposure to foreign exchange risks and adjusting the maturity structure and interest mix of its public debt. As a small island developing country, Mauritius is extremely vulnerable to climate change, making adaptation to climate change particularly critical. However, according to the International Monetary Fund, current donor funding to the country is directed mainly to mitigation efforts. To fully finance both adaptation and mitigation, Mauritius needs to focus on mobilizing more resources through grants, concessional loans, global climate funds, and climate financing debt instruments (such as green bonds) and on rechanneling unused Special Drawing Rights, a key proposal of the Bridgetown Initiative. In the long term, the country needs to deepen its capital market to attract more foreign direct investment, expand trade, and foster integration into regional and global value chains.

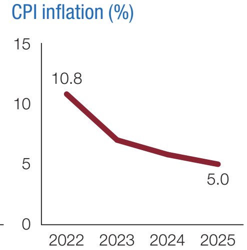
Real GDP growth (%)



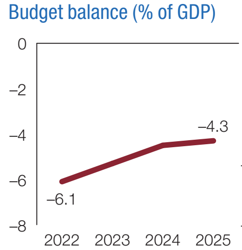
Real GDP per capita growth (%)



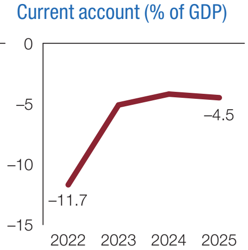
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Mozambique

Recent macroeconomic and financial developments

Real GDP grew by an estimated 5.0% in 2023, up from 4.2% in 2022, driven mainly by extractive industries as liquefied natural gas processing matured in the Coral South Field. The extractive and service sectors were the main drivers of growth on the supply side, while private consumption drove growth on the demand side. Tight monetary policy and lower local food and transport prices reduced inflation from 10.3% in 2022 to an estimated 7.1% in 2023.

The fiscal deficit improved from 5.1% of GDP in 2022 to about 2.8% in 2023, reflecting cuts in public spending and higher domestic revenue collection as the economy gradually recovered. Mozambique is in debt distress, but its debt is assessed as sustainable on a forward-looking basis. The current account deficit has improved from 34.2% of GDP in 2022 to an estimated 11.1% in 2023 led by increased exports and declining imports. Foreign direct investment and external borrowings were the main sources of financing of the current account deficit. International reserves dropped from 3.1 months of import cover in 2022 to 2.2 months in 2023 due to currency depreciation. Asset quality remains low, with nonperforming loans at 9.1% of gross loans in September 2023 and 9.3% in September 2022, driven by high lending rates.

Poverty remains high at an estimated 74.5% in 2023, with about 24 million people living in poverty. The employment rate fell from 75.6% in 2019 to 73.6% in 2020 as recent growth has not been inclusive.

Outlook and risks

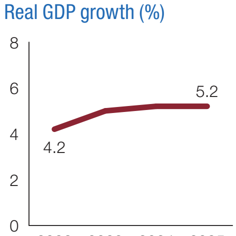
Real GDP is projected to grow by an average of 5.2% between 2024 and 2025, driven by the extractives sector, particularly gas production. Growth will be supported by extractives and agriculture on the supply side and by private consumption and foreign direct investments on the demand side. Key headwinds arise from climate change, a slowdown in reforms implementation with the upcoming general election in October 2024, and continuing global supply chain disruptions due to Russia's invasion of Ukraine. The fiscal deficit is projected to widen to 3.4% of GDP in 2024 before narrowing to 1.3% in 2025 as fiscal consolidation and improved revenue collection take hold. Inflation should fall to an average of 4.8% between 2024 and 2025, in response to prudent monetary policy. The current account deficit is projected to increase to 38.1% of GDP in 2024 and 43.0% in 2025 as imports rise.

Reform of the global financial architecture

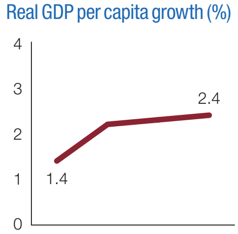
Mozambique's economic structure is determined largely by the extractives sector, with its large gas reserves of 180 million cubic feet, the third largest in Africa. There has been only limited structural transformation of the economy, with a slight shift from agriculture to services. In 2001, the services sector was the main contributor to GDP growth, accounting for 50%, followed by agriculture at 32.2%, industry (including extractives) at 18%, and manufacturing at 12.2%. Two decades later, economic activity continues to be driven by the services sector, which accounted for 51.7% of GDP in 2021, while agriculture's share had fallen to 28%. Mozambique's structural transformation is hampered by skills shortages and a high illiteracy rate among 15- to 34-year-olds (31.4%), skills mismatches, lack of infrastructure, high public debt, and a low level of industrialization.

Financing structural transformation in Mozambique requires multiple measures over different timeframes. In the short term, government needs to strengthen debt management capacity, fiscal discipline, and financial sector regulation. In the medium term, government needs to fast-track debt restructuring under the G20 Common Framework, and multilateral development banks need to deploy risk mitigation instruments to attract private investors and provide technical assistance to mobilize climate financing. In the long term, international private sector support is needed for identifying and mitigating key investment risks.

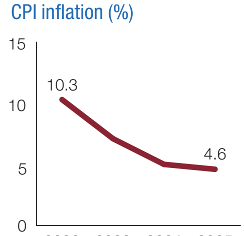
Real GDP growth (%)



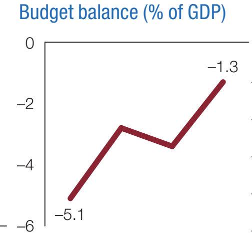
Real GDP per capita growth (%)



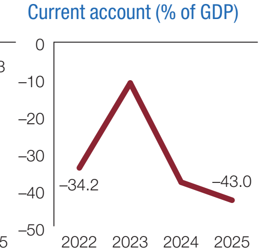
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Namibia

Recent macroeconomic and financial developments

The Namibian economy grew an estimated 4.2% in 2023, down from 5.3% in 2022, owing to weak global demand and contraction in agriculture. Inflation moderated slightly from 6.1% in 2022 to 5.9% in 2023 as demand for Namibian diamonds slowed.

The Namibia dollar depreciated 6.4% against the US dollar, 12.5% against the euro, and 12.2% against the British pound in 2023 owing to depreciation of the South African rand to which the Namibian dollar is pegged. The fiscal deficit narrowed from 5.1% in 2022 to 3.8% in 2023. The current account deficit declined from 12.9% of GDP in 2022 to 10.3% in 2023 down, reflecting slightly lower imports. Nonperforming loans declined from 6.4% of gross loans in 2019 to 1.1% in 2022, while the capital adequacy ratio reached 15.6% in 2022, just 0.776% less than in 2021.

In 2022, Namibia had an unemployment rate of 29.9%, a poverty incidence of 26.9%, an HIV prevalence rate of 16.9%, and a Gini coefficient of 0.61.

Outlook and risks

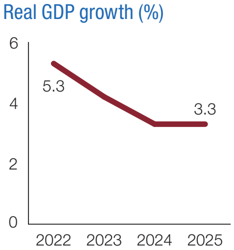
Real GDP is projected to decline to 3.3% in both 2024 and 2025 owing to anticipated weak global demand and contraction in agriculture. Inflation is expected to moderate further to 4.6% in 2024 and 4.4% in 2025. The fiscal deficit is projected to remain at 4% of GDP in 2024 and 2025 on expectations of improved revenue collection. The current account deficit is expected to moderate to 9.6% of GDP in 2024 and 8.5% in 2025. Downside risks are related to monetary policy tightening, which will slow growth; the high costs of key imports; and Russia's continuing invasion of Ukraine, which will raise commodity prices. Other domestic risks include water supply interruptions that affect mining production as well as impacts of climate change. As a mitigating measure, the Central Bank hiked its interest rates by 50 basis points in June 2023.

Reform of the global financial architecture

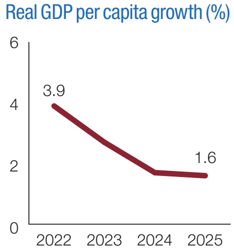
Overall, there has been very little, if any, structural transformation of the Namibian economy, as evidenced by the slow pace of change in the manufacturing sector. Manufacturing's share in GDP ranged from 7% in 1990 to 11% in 2022. Agriculture's share varied even less, ranging from 8% to 9%, while services' share declined from 54.2% in 1990 to 26.1% in 2022.

Though Namibia is an upper-middle -income country, it faces many of the same challenges as low-income countries owing to its past. The global financial architecture has failed to provide adequate resources to support Namibia's development. The International Monetary Fund should scale up financing for Namibia by increasing its Special Drawing Rights allocation. Its loans to Namibia should also contain a contingency clause. The country should also receive preferential treatment in accessing global grant funds. On the domestic front, Namibia should intensify efforts at financial market deepening, which has the potential of diversifying domestic sources of finance. The Aid-for-Trade Initiative will also help Namibia increase its exports. The country should also improve management of its sovereign wealth fund.

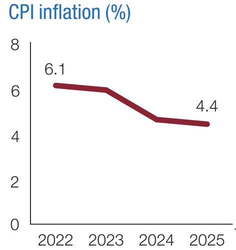
Real GDP growth (%)



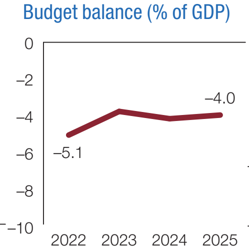
Real GDP per capita growth (%)



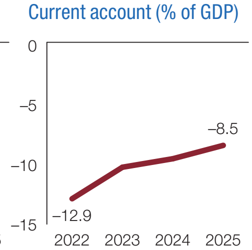
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data for the budget balance as a % of GDP reflect a financial year that begins April 1 and ends March 31 the following year.

São Tomé and Principe

Recent macroeconomic and financial developments

Real GDP growth rose slightly from 0.1% in 2022 to an estimated 0.5% in 2023. The slow growth was due mainly to the prolonged impact of power disruptions on the economy, aggravated by Russia's invasion of Ukraine, which led to higher food and oil prices in global markets. Inflation rose sharply, from 8.1% in 2021 to 17.9% at the end of 2022 and 21.3% at the end of 2023, responding to supply shocks and global demand on the back of the Covid-19 pandemic.

As a result of low revenues and high expenditures, the country continues to face a structural fiscal deficit, which is estimated at 4.2% of GDP in 2023, a decline from the 6.2% in 2022. The fiscal deficit is financed mostly through grants and loans from multilateral and bilateral partners. The current account deficit narrowed to 14.5% of GDP in 2022 and to 13.8% in 2023. São Tomé and Principe has a peg currency agreement with Portugal for the dobra. The country faces a major challenge in ensuring its energy and food security. As a result, net international reserves experienced a sharp decline, from $29.9 million in 2021 to $0.51 million in December 2023, covering less than a month of imports, including fuel. Nonperforming loans rose from 8.1% of gross loans in 2022 to 11.9% in 2023, reflecting the private sector's inability to meet its obligations in the unfavorable economic environment affecting the local market.

The multidimensional poverty rate fell from 40.7% in 2008 to 11.7% in 2019. The national unemployment rate rose to 15.7% in 2022 from 8.9% in 2017, with women (14.6%) and youth ages 15–24 (21.3%) being the most affected.

Outlook and risks

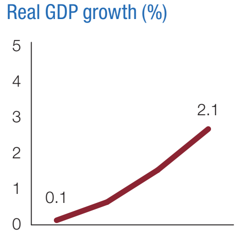
São Tomé and Principe's medium-term economic outlook is uncertain due to the combined impact of external shocks and structural weaknesses. The economy is projected to grow slowly, at 1.2% in 2024 and 2.1% in 2025. Meanwhile, inflation is projected to continue its downward trend, reaching an average of 16.1% in 2024. The fiscal deficit is expected to decline to 3.3% of GDP in 2024 and 2.9% in 2025. The current account is also expected to continue its downward trend and should stand at 11.4% of GDP in 2024 and 9% in 2025. The government is discussing a program with the International Monetary Fund to anchor the economic recovery. Medium-term risks to growth include the poor business environment, sometimes unstable energy supply, and lack of investment in key trade infrastructure.

Reform of the global financial architecture

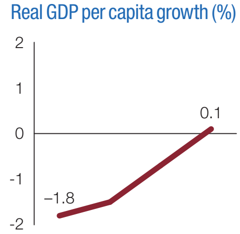
São Tomé and Principe's economy suffers from a limited production base that hinders economic diversification and reduces the country's resilience to economic and climate shocks. As a result, the country is unable to achieve the more inclusive and higher growth trajectory needed for sustainable poverty reduction. In 2022, services contributed the largest share of GDP, at 81.5%, followed by the agriculture, forestry, and fishery sector, at 13.4%, and industry, at 5.1%. There are only a few medium-size manufacturing companies in the country, and these focus on cacao, beverages, vanilla, and timber transformation. The investment inflow is insufficient to meet the country's overall investment needs for infrastructure and productive value chains. Meeting the infrastructure investment needs will require financing of around $5 billion for the next five years.

São Tomé and Principe would benefit from an easing of financing requirements from public international institutions, financial standard-setters for private finance, regional financial arrangements, and creditor groups to ensure adequate financing for infrastructure. It could also gain from technical assistance in setting up standards for governance policies, structured sectoral strategies, and dynamic and world-class financial services. There is need for reform of the global financial architecture to respond to São Tomé and Principe's urgent investment requirements. In the medium to long term, the country should strengthen the domestic financial sector by connecting to global markets and introducing low-cost digital financial services and a capital market.

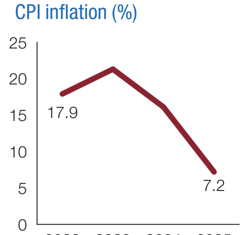
Real GDP growth (%)



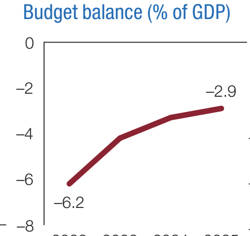
Real GDP per capita growth (%)



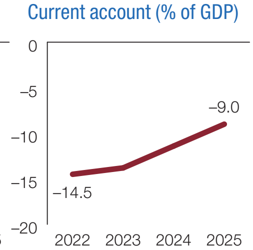
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

South Africa

Recent macroeconomic and financial developments

Real GDP growth decelerated from 1.9% in 2022 to 0.6% in 2023, due to persistent electricity shortages, transport sector constraints, and lower international prices for gold and platinum group metals. These factors resulted in a deceleration of growth in the key sectors of agriculture (down 3.2%) and mining (down 1.6%) in 2023 compared with 2022. Manufacturing picked up marginally (up 0.2%) owing to increased demand for petrochemicals and vehicles. Household consumption declined from 2.8% in 2022 to 0.7% in 2023 due to higher interest rates. Inflation declined from 6.9% in 2022 to 6.0% in 2023 reflecting lower international fuel prices. The exchange rate of the South African rand weakened by 12.4% against the US dollar in 2023, to 18.40 rand to the dollar, due to declining terms of trade for South Africa's main exports.

The fiscal deficit remained at 4.6% of GDP during 2021/22 and 2022/23. The current account deficit widened from 0.5% of GDP in 2022 to 1.6% in 2023 as the import bill grew due to depreciation of the rand and lower prices for commodity exports. Official reserves stood at $61.7 billion (5.3 months of import cover) as of November 30, 2023. The financial sector is resilient, well capitalized, and profitable. Capital adequacy stood at 17.3% in 2023 compared with 17.8% in 2022, nonperforming loans at 45% compared with 4.2%, and liquid assets ratios at 14.9% compared with 13.7%.

The poverty rate was estimated at 21.6% in 2023, and the Gini coefficient was 0.63. Overall unemployment stood at 32.1% and youth (25–34 years) unemployment at 39%. South Africa is among the top 10 most unequal countries globally.

Outlook and risks

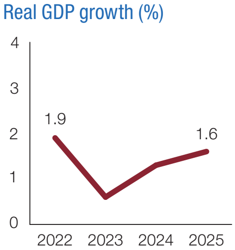
The outlook is weakly positive, with GDP growth projected at 1.3% in 2024 and 1.6% in 2025, as new infrastructure investments support construction and recovery of other sectors. Inflation is expected to moderate at 4.8% in 2024. The fiscal deficit is projected to decline to about 4.3% of GDP in 2023/24, as tax revenue collections improve. The current account deficit is expected to widen to 3.0% of GDP in 2024, due mainly to lower growth of exports than imports because of constraints in the transport sector and power shortages. Key risks include persistent electricity supply shortages, transport bottlenecks, fiscal vulnerabilities arising from bailouts of state-owned enterprises, volatile commodity prices, and climate change shocks. The 2024 general elections could also generate a risk of investor apprehension. However, macroeconomic reforms, investment, and trade are expected to stimulate the economy.

Reform of the global financial architecture

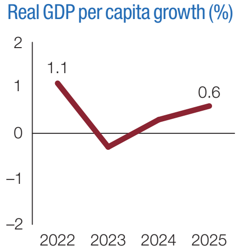
Progress on structural transformation has been mixed, with an expanding share of services in GDP but a declining share of industry. The services sector contributed 62.6% of GDP in 2022, up from 51.3% in 1990, driven by financial services, real estate, and transport. However, this expansion has shown limited capacity to absorb workers with low skills. Industry's share of GDP declined from 36% in 1990 to about 25% in 2023. Manufacturing's share halved to 12% of GDP in 2023 from 24% in 1990, while agriculture's contribution remained static at 13%. This pattern has led to growth stagnation and slowed job creation.

Deepening financial markets and promoting public-private partnerships for infrastructure development are needed to facilitate investment, particularly in the energy sector, which is essential for inclusive economic growth and structural transformation. Reform of the global financial architecture, to improve capitalization and investment, is needed to adequately respond to emerging shocks. Financial deepening is also critical for reducing inequalities by improving access to credit and other financial products that can stimulate economic growth.

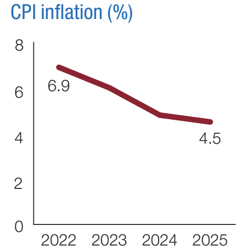
Real GDP growth (%)



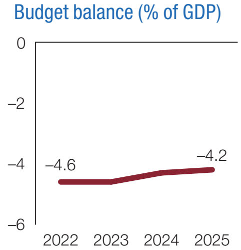
Real GDP per capita growth (%)



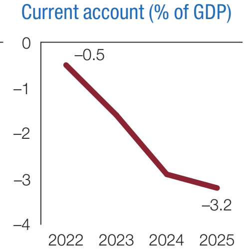
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to South Africa's fiscal year, which runs from April 1 to March 31.

eSwatini

Recent macroeconomic and financial developments

Eswatini's economy grew from 0.5% in 2022 to an estimated 4.8% in 2023, driven by stronger performance of the services sector. Aggregate demand is driven largely by consumption, which constitutes 84% of GDP, and investment, at 13% of GDP. Inflation rose to 5% in 2023, and in the context of the currency peg, monetary authorities gradually raised the discount rate from 3.75% in March 2022 to 7.75% in July 2023 before adjusting it to 7.5% since August 2023. The rand/lilangeni depreciated in 2022 and 2023 amid weak investor sentiment about South Africa's economic prospects.

The fiscal deficit widened from 4.5% in 2022 to an estimated 6.3% of GDP in 2023 as revenues underperformed. The debt-to-GDP ratio marginally declined from 43% in December 2022 to an estimated 41% in December 2023, above the desired level. Domestic tax revenues increased slightly from 15.6% of GDP in 2022 to about 16.1% in 2023. The current account balance recovered from a deficit of 2.6% of GDP in 2022 to an estimated surplus of 3.9% in 2023, buoyed by an improved trade balance and secondary income inflows. Reserves improved slightly to 2.7 months of import cover in 2023, from 2.5 months in 2022. The financial sector was stable, although nonperforming loans remained elevated at around 7.2% of gross loans in 2023. Banks maintained a strong capital adequacy ratio, which averaged around 18% in 2022/23, above the statutory minimum requirement of 8%.

Poverty (58.9% in 2017), youth unemployment (56% in 2023), and inequality (0.55 Gini coefficient in 2016) remain high.

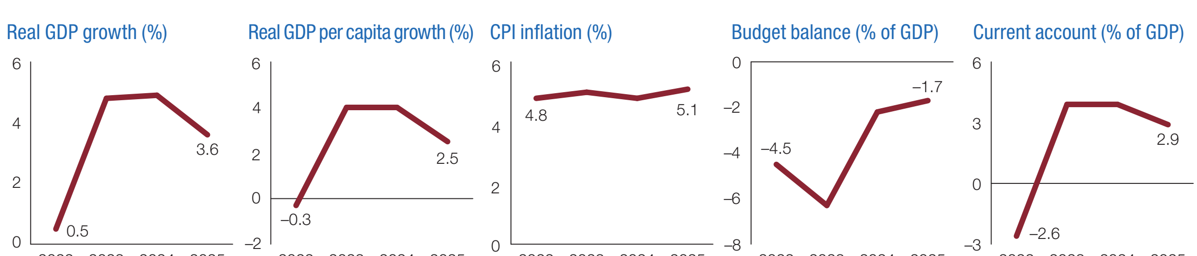
Outlook and risks

The economic outlook is positive, although downside risks remain. Growth is projected at 4.9% for 2024, underpinned by improvements in industry and services, then tapering in 2025 due to slowing agricultural growth. The fiscal deficit is expected to narrow further in 2024 and 2025 on the back of high Southern Africa Customs Union receipts. The public debt-to-GDP ratio is also poised to decline further because of positive growth prospects. The current account surplus is expected to rise to 4%, buoyed by improving trade balances and secondary income inflows. Inflation is projected to decline slightly to 4.8% in 2024 following global trends, but planned electricity tariff hikes, a weaker exchange rate, and high food prices could reverse the trend. Other downside risks stem from ongoing economic challenges in South Africa, especially energy supply, elevated prices, climate change impacts on agricultural output, and tighter credit conditions that may stymie new investments.

Reform of the global financial architecture

Eswatini is slowly shifting its output and employment from agriculture to services. The share of services in GDP rose from 45.6% in 2000 to 53.5% in 2023, while the share of agriculture dropped from 12.3% to 8.1% and industry from 39.1% to 33%. Manufacturing (85% of industry) is highly concentrated in food and beverages. Over the same period, service jobs increased by 5.2%, while agricultural jobs declined by 4.3% and industrial jobs by 1.3%. Accelerating structural transformation requires boosting total factor productivity through economic governance reforms aimed at attracting private investment, diversifying productive capabilities, and expanding local and regional value chains.

Eswatini's financing gap to achieve structural transformation by 2030 is estimated at 9.5% of annual GDP. Its status as a lower-middle-income country presents challenges to unlocking adequate concessional finance to propel structural transformation. The global financial system ought to be reformed to consider the unique situations and diverse needs of middle-income countries in order to boost their access to financial resources and accelerate their structural transformation. These include increasing concessional resources from multilateral development banks and special project funds for middle-income countries. Moreover, strengthening the financial sector through legal and regulatory reforms will ensure financial sector stability and greater economic diversification.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to eSwatini's fiscal year, which runs from April 1 to March 31.

Zambia

Recent macroeconomic and financial developments

Real GDP has grown steadily, from 5.2% in 2022 to 5.8% in 2023, driven by wholesale and retail trade, agriculture, and mining and quarrying on the supply side and by household and corporate consumption on the demand side. Inflationary pressures persist, with inflation at 11.0% at the end of 2022 and 10.9% at the end of 2023, driven mainly by food, transport costs, and the nominal exchange rate. The monetary policy rate has targeted curbing inflationary pressures, with upward revisions from 9.5% in September 2022 to 11.0% in November 2023.

The fiscal deficit improved marginally, from 8.2% of GDP in 2022 to 6.6% in 2023, owing to higher mining sector revenue collections. The current account went from a surplus of 3.8% of GDP in 2022, on higher export volumes and prices and subdued imports of consumer goods, to a deficit of 1.1% in 2023. International reserves declined from 4.4 months of import cover at the end of 2022 to 3.4 months in November 2023, on account of the use of the Extended Credit Facility and Special Drawing Rights from the International Monetary Fund. Improved financial sector performance in 2023 was due to increased economic activity. The ratio of nonperforming loans to gross loans improved from 6.1% in 2022 to 5.1% in 2023. The primary capital adequacy ratio was strong, at 23% at the end of October 2023 and 22.7% at the end of December 2022, owing to increased retained earnings.

About 60% of the population lives below the national poverty line, a slight improvement from 58% in 2015. Poverty levels are much higher in rural areas (78.8%) than urban areas (31.9%). Unemployment remains high, at 13%, especially among youth (24.7%).

Outlook and risks

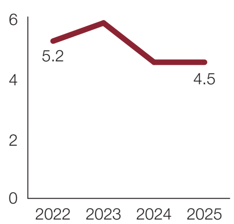
The economy is projected to grow at 4.5% in 2024 and 2025, as the mining, services, and manufacturing sectors continue to recover, and global copper prices rebound. Inflation is expected to decelerate from 9.3% in 2024 to 7.0% in 2025, driven by falling food and fuel prices. Fiscal deficits are projected to narrow to 5.2% of GDP in 2024 and 3.4% in 2025 in response to ongoing fiscal reforms. The current account balance is expected to improve from a deficit of 1.1% in 2023 to surpluses of 3.3% in 2004 and 8.4% in 2025 as copper output rises. Downside risks to the growth outlook include continuing drought, fluctuating copper prices, slippages in reform program execution, and the inflationary impacts of Russia's invasion of Ukraine on fertilizer and fuel prices. The government is expected to continue tightening monetary policy to curb inflation, maintaining a flexible exchange rate to reduce volatility, and shoring up foreign reserves through higher export earnings, the addition of locally mined gold bullion to foreign reserves, and the promotion of stable foreign investment flows.

Reform of the global financial architecture

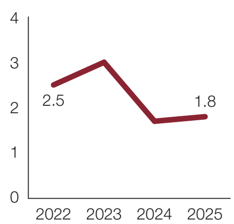
Zambia needs to accelerate its structural transformation and diversification. Copper contributed disproportionately to GDP in 2022 (12.9%) and to export revenues (70%). The service sector contributed about 57% of GDP, while industry contributed 33.8%, with manufacturing contributing just 8.1%. Construction, utilities, and industrial activities accounted for about 10.9% of GDP. Agriculture's contribution to GDP shrank from 9.3% in 2012 to 3.3% in 2022, even though the sector employs 24% of the labor force (58.5% men and 41.5% women). Productivity is low, as evidenced by widening productivity gaps between sectors. Structural transformation will require $3.5 billion in annual financing, along with improvements in institutional quality and sustained policy reforms.

Zambia's debt restructuring negotiations under the G20 Common Framework have taken considerably longer than the speedy process initially envisioned when the Common Framework was initiated. When Zambia was categorized as being in debt distress in 2017, multilateral development banks stopped providing nonconcessional financing. The major credit rating agencies may have escalated the debt crisis by overestimating sovereign risks. Thus, Zambia's experience with debt restructuring underscores the urgent need for reforms and transformation of the global financial architecture.

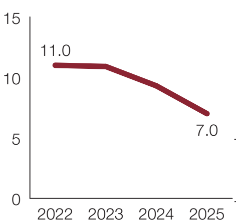
Real GDP growth (%)



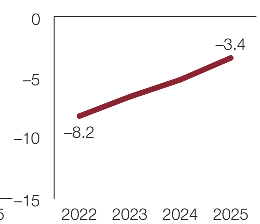
Real GDP per capita growth (%)



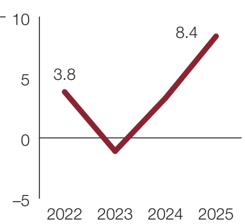
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Zimbabwe

Recent macroeconomic and financial developments

Real GDP growth moderated from 6.1% in 2022 to 5.0% in 2023, due mainly to drought and floods that affected agricultural output and to higher costs of fuel and food imports. Zimbabwe has a multicurrency monetary system, with the Zimbabwe dollar (ZWL) and the US dollar ($) as dominant currencies. The nominal exchange rate depreciated by 89.8% in 2023, reaching ZWL6,104/$1 by December 2023. To rebuild trust and confidence in the local currency, the Reserve Bank of Zimbabwe (RBZ) introduced a new currency on 5 April 2024, Zimbabwe gold (ZIG), which replaced the Zimbabwe dollar. The ZIG exchange rate is market determined and backed by the US dollar and mineral reserves. On its introduction, the exchange rate stood at ZIG13.55/$1. Inflation declined from 41.9% in December 2022 to 29.4% in December 2023 mainly due to the adoption of a blended inflation measure and rebasing of inflation estimates.

The fiscal deficit remained low, at 2.0% of GDP in 2023 from 2.1% in 2022, due to a combination of enhanced revenue mobilization and expenditure cuts. The current account surplus increased marginally from 1.0% of GDP in 2022 to 1.3% in 2023, reflecting increased export earnings. The financial sector remained strong in 2023, with a capital adequacy ratio of 33%, a ratio of nonperforming loans to gross loans of 1.5%, and a liquidity ratio of 60%, all above minimum regulatory requirements of 12%, 5%, and 30%, respectively.

Poverty remains high, estimated at 38.7% in 2023. Unemployment stood at 21% in the third quarter of 2023.

Outlook and risks

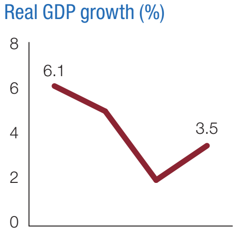
Slower GDP growth of 2.0% is projected for 2024, mainly on account of below average agricultural output due to the El Niño weather phenomenon. Mining output is also expected to remain subdued because of lower international mineral prices. Inflation is projected to average 24.9% in 2024 as the exchange rate stabilizes. The downside risks are elevated due to drought caused by El Niño weather patterns that has affected the agriculture sector, while unstable international commodity prices pose further risks to the mining sector. A slowdown in global economic growth would be a major risk to the outlook. Zimbabwe expects to adopt a Staff Monitored Program (SMP) of the International Monetary Fund (IMF) in second half of 2024. Maintaining ZIG exchange rate stability and eliminating the quasi-fiscal operations of the RBZ and transferring all its liabilities to the Treasury could underpin macroeconomic stability.

Reform of the global financial architecture

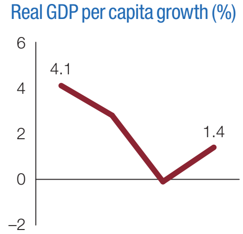
The economy has experienced only minimal structural transformation in the last two decades, with structural change impeded by crippling public debt accumulation estimated at 87% of GDP in 2023. The services sector has remained the major contributor to GDP over the last decade, averaging over 50% since 2010 and reaching 55% in 2023. Persistent socioeconomic pressures led to human capital flight of an estimated 3 million mostly skilled workers. Labor shifted from higher value-added sectors, such as agriculture, industry, and high-productivity services, to lower value-added sectors, including wholesale and retail trade. Zimbabwe's labor productivity growth remains depressed and ranked very low among 17 lower-middle-income countries in Africa.

Prerequisites for Zimbabwe's structural transformation are debt restructuring and clearance of arrears to create fiscal space for investment, attract foreign direct investment, and unlock access to global financing opportunities. Since 2022, the country has engaged with the international development community and has agreed to implement economic and governance reforms that would unlock arrears clearance. Zimbabwe's main creditors, including multilateral and bilateral donors, which account for 76% of its debt, have a key role in accelerating agreed reforms and arrears clearance.

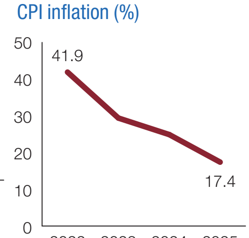
Real GDP growth (%)



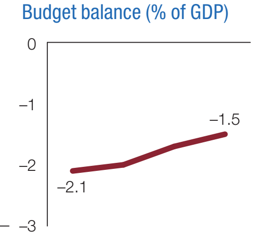
Real GDP per capita growth (%)



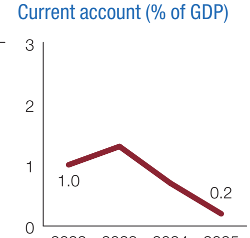
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

WEST AFRICA

Benin

Recent macroeconomic and financial developments

The economy continued its strong, sustained growth momentum in 2023. The main drivers were the beverage industries (up 14.7%) and telecommunications (up 9.2%) on the supply side and public and private investment (up 16%) on the demand side. In 2023, inflation doubled as contraband fuel prices rose, although remaining below the West African Economic and Monetary Union convergence standard of 3%.

To cope with the lingering effects of recent crises (the Covid-19 pandemic, Russia's invasion of Ukraine) and to finance infrastructure (roads, ports, urban sanitation, and energy), the government kept public spending high, at 19.3% of GDP in 2023, slightly below the 19.8% in 2022. Public revenue rose from 13.8% of GDP in 2022 to 14% in 2023. The budget deficit remained high, although slightly down from 2022, and was financed by public debt. Public debt outstanding rose from 46.1% of GDP in 2020 to 53.8% in 2023. Debt distress was moderate at the end of 2023, according to the International Monetary Fund. The current account deficit improved in 2023 as import prices stabilized. The financial sector continued to expand, with credit to the private sector up 9% in 2023 following a 21.4% increase at the end of 2022.

The poverty rate fell to 36.2% in 2022 from 38.5% in 2019, according to the National Institute for Statistics and Demography. This improvement was the result of investment in progress toward achieving the Sustainable Development Goals. Strengthening the social inclusion of vulnerable populations remains a challenge, which the government is tackling through social protection programs (health insurance, retirement insurance).

Outlook and risks

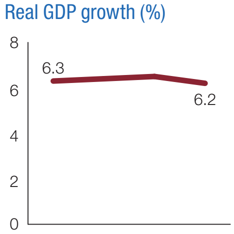
The startup of several industrial production units and the acceleration of public infrastructure projects are projected to keep growth strong at 6.5% in 2024 and 6.2% in 2025. Inflation is projected to remain below 3% in the short term. With reforms aimed at improving tax administration, the budget deficit is expected to continue to fall, reaching 3% in 2025. The current account deficit is projected to contract to 4.4% in 2024 and 4.2% in 2025 thanks to increased manufacturing exports. The main risks to the outlook concern the decline in trade with Nigeria, the negative effects of climate change, the deteriorating security situation in the north, and the uncertainty linked to the exit of Burkina Faso, Mali, and Niger from the Economic Community of West African States. To consolidate its economic resilience, the country should accelerate the economic transformation initiated through the Glo-Djigbé Industrial Zone, with the aim of moving up the value-added chain for agricultural products, including cotton. Climate action and resilience should also be emphasized.

Reform of the global financial architecture

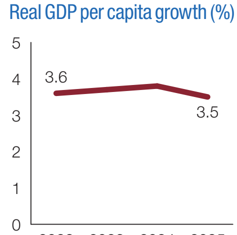
Structural transformation remains slow due to the low productivity of production factors and the mismatch between skills and jobs. Over the past two decades, the structure of the economy has evolved slightly, with the share of services increasing from 44.6% of GDP in 2003 to 51.6% in 2022, at the expense of industry, whose share fell from 25.8% to 18.7%. The share of agriculture has stagnated at 29.6%. The evolution of sectoral employment has differed from that of GDP, as workers have shifted from agriculture and industry to low value-added services (trade, transport).

From 2021 to February 2024, the public authorities raised $1.67 billion on international capital markets. Access to capital markets was facilitated by instruments such as the African Development Fund's €195 million partial credit guarantee, which enabled Benin to raise €350 million on favorable terms in 2023. To enable Benin to take advantage of the global financial architecture to accelerate its structural transformation, international financial institutions should strengthen their role as advisors and providers of guarantee instruments to mobilize innovative financial vehicles for sustainable finance (green, blue, and social bonds). Public authorities should pursue structural reforms (macroeconomic stability, debt management, tax revenue mobilization), which are essential to fostering sustainable access to capital markets.

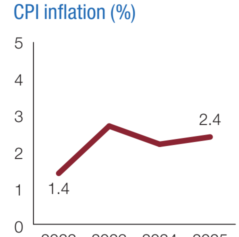
Real GDP growth (%)



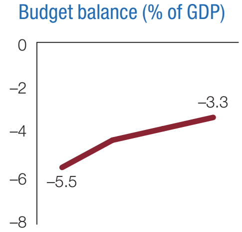
Real GDP per capita growth (%)



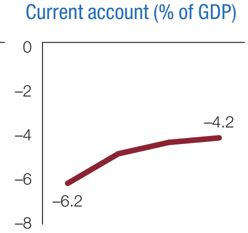
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Burkina Faso

Recent macroeconomic and financial developments

Despite the security crisis, the growth rate rebounded to 3.6% in 2023, still below the 6.0% recorded over 2010–19. The economy is driven by services and agriculture. Extractive activities continue to be affected by the security context. On the demand side, rising final consumption supported growth. Inflation slowed from 14.1% in 2022 to 0.7% in 2023, due to improved food supplies and a restrictive monetary policy.

The budget deficit improved from 10.4% of GDP in 2022 to 6.9% in 2023 thanks to higher tax revenue (17.8% of GDP in 2023 versus 17.0% in 2022). The reform program agreed in September 2023 between Burkina Faso and the International Monetary Fund has strengthened fiscal discipline and economic governance. But security-related spending remains high, affecting budget margins. Risk of debt distress remains moderate, though public debt, estimated at 60.8% of GDP in 2023, has risen with the increased issuance of government securities. The current account deficit deteriorated to 8.2% of GDP in 2023 following a decline in the value of cotton exports. The banking sector's portfolio deterioration rate dropped from 7.5% in 2021 to 5.7% in 2022, while the solvency ratio rose from 13.4% in 2021 to 14.2% in 2022, against a minimum standard of 11.25%.

The security context, humanitarian crisis, and climatic shocks have had a deteriorating impact on social conditions. Poverty rose from 41.4% in 2018 to 43.2% in 2021, and the precariousness of youth employment remains a major challenge.

Outlook and risks

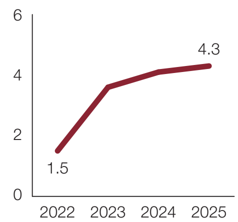
The economic outlook is favorable, with growth projected at 4.1% in 2024 and 4.3% in 2025, underpinned by rising extractive and agricultural production. But these sectors remain dependent on the domestic security and sociopolitical climates and on the dynamics with the Economic Community of West African States (ECOWAS). Inflation is projected to rise to 2.1% in 2024 and to 2.2% in 2025 due to higher food prices. The budget deficit is expected to narrow to 6.0% of GDP in 2024 and to 5.4% in 2025, in line with higher tax revenues. Debt is projected to remain sustainable, rising to 65% of GDP in 2024–25, driven by increased issuance of public securities to cover the financing gap. The current account deficit is projected to improve to 6.5% of GDP in 2024 and to 5.4% in 2025 thanks to higher gold and cotton exports. Downside risks to this outlook include a deterioration in the security situation and budgetary slippage and external risks linked to climatic shocks, falling prices of exported raw materials (gold and cotton), and the terms of the country's exit from ECOWAS.

Reform of the global financial architecture

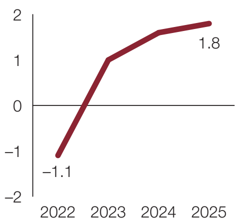
Structural transformation has been slow, with agriculture still the main sector of the economy. Between 2000 and 2022, manufacturing's share of GDP fell from 16.2% to 9.9%, agriculture's share fell from 26.4% to 21.7%, and services' share rose from 48.8% to 50.5%. The share of extractive industries rose from 1.9% to 14.5%. Over the same period, industry's share of employment rose from 4.2% to 7.0%, services' share rose from 10.4% to 18.8%, while agriculture's share fell from 85.4% to 74.2%.

Accelerating structural transformation will require returning to security and institutional stability, developing promising agro-pastoral and industrial value chains, adopting an adequate energy mix, opening the country to trade, improving the business climate, and developing the private sector. Strengthening the macroeconomic and financial framework and increasing the mobilization of domestic resources will also be necessary. Developing innovative financial vehicles (diaspora bonds and the like) will also be useful. In addition, in the short term, the country will need the support of international financial institutions to access more concessional resources and technical assistance to better manage its mining sector. In the medium term, access to nonconcessional windows could be explored on a case-by-case basis for structuring projects with long maturities at reduced costs and the use of partial guarantee and credit instruments.

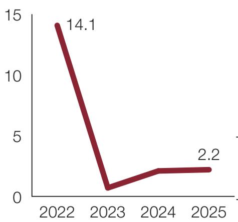
Real GDP growth (%)



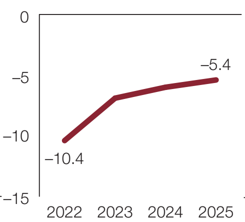
Real GDP per capita growth (%)



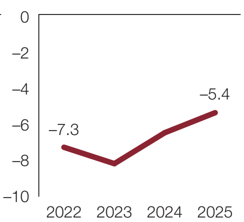
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Cabo Verde

Recent macroeconomic and financial developments

Cabo Verde's GDP growth remains volatile due to its dependence on tourism-intensive activities and its vulnerability to climate-related shocks. On the demand side, private consumption bolstered growth, amid falling inflation as food and energy prices declined.

In 2023, monetary policy was tightened to narrow the interest rate differential and preserve the peg to the euro. Policy reforms to streamline arrears in collection of the value added tax and the use of electronic invoicing boosted tax revenue from 18.1% of GDP in 2022 to 18.9% in 2023, and the fiscal deficit shrank from 4.6% of GDP to 4.4%. The current account deficit deteriorated from 5.8% of GDP in 2022 to 6.1% in 2023, driven by high import bills and lower exports. International reserves increased from €626 million in 2022 to €728 million in 2023 (about 6.7 months of imports cover), boosted by the disbursement of $21.2 million under the International Monetary Fund's Extended Credit Facility. Cabo Verde's external debt risk is moderate, and its public debt-to-GDP ratio declined from 127.1% in 2022 to 119.9% in 2023 due to higher nominal GDP growth and fiscal overperformance. The financial sector appears sound, with a capital adequacy ratio of 21.4%, well above the 12% minimum regulatory requirement. Nonperforming loans increased from 7.8% in 2022 to 8.7% in June-2023, following the unwinding of Covid-19 credit moratoriums.

Although Cabo Verde performs well on social indicators, poverty and unemployment remain challenges. Poverty increased from 26% in 2019 to 31.1% in 2022 exacerbated by Covid-19. Unemployment was at 14.5%.

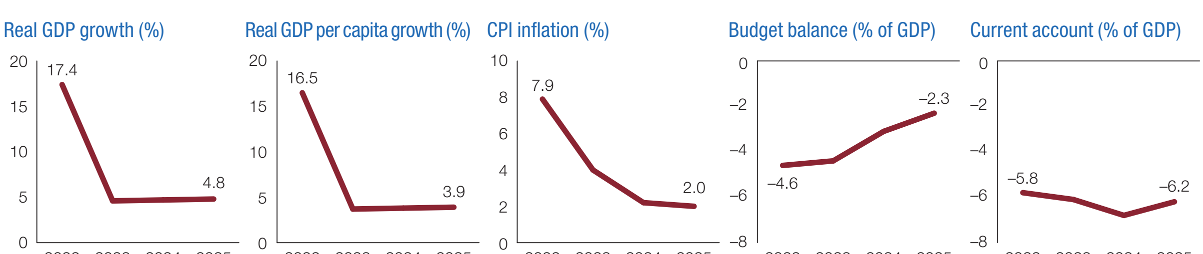
Outlook and risks

Economic growth is projected at 5.2% in 2024 and 5.4% in 2025, boosted by agriculture, energy, the digital economy, and private consumption. The outlook is premised on a stable global environment and vibrant tourism. Inflation is projected to average 2.1% over 2024–2025 on the back of weaker demand and declining food and energy prices. The fiscal deficit is expected to narrow to 3.0% of GDP in 2024 and 2.1% in 2025 owing to fiscal consolidation measures, higher tax revenues, and privatization of state-owned enterprises. The current account deficit is projected to narrow to 5.2% of GDP in 2024 and 4.4% in 2025, supported by tourism receipts and remittances. Risks to the growth outlook include an economic slowdown in Europe, disruptions in oil supply chains, limited progress in state enterprise reform, and impacts of climate change. Actions to reduce fiscal risks from state enterprises and address infrastructure gaps are fundamental for sustainable growth.

Reform of the global financial architecture

Structural transformation of Cabo Verde's economy has been slow over the past two decades, with limited economic diversification. Agriculture's share of GDP dropped from 9.7% in 2000 to 7.8% in 2021, while the shares increased for industry (19.7% to 21.8%) and services (57% to 65%). Employment shares declined in low-productivity agriculture (23% to 10.6%), with excess labor being absorbed by high-productivity industry (20.5% to 21.8%) and services sectors (55.9% to 67.6%) between 2000 and 2021. Investments in skills, technological innovation, and modernization of ports and airports are vital to expand the economy and take advantage of the Africa Continental Free Trade Area.

Cabo Verde could learn from the experiences of Seychelles, in harnessing the blue economy through blue bonds and debt swaps, and Maldives in diversifying the economy beyond tourism by upgrading the fishery value chains. Reform of the global financial architecture could leverage additional funds on more advantageous terms. To ensure access to and optimal use of financing for development, crucial reforms in the short term include establishing a blue grants fund and blue investment fund, deepening capital markets, and enhancing macroeconomic stability. In the medium to long term, strengthening infrastructure financing, notably in inter-island transportation, is imperative for commercial viability and competitiveness.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Côte d'Ivoire

Recent macroeconomic and financial developments

Economic activity was vigorous in 2023, with real GDP growth estimated at 6.5%, up from 6.2% in 2022, driven by investment (public and private) and domestic consumption. Despite a 22.7% drop in cocoa production, economic growth was sustained by the dynamism of food-producing agriculture, construction and public works, manufacturing and extractive industries, trade, and transport. Inflation decelerated from 5.2% in 2022 to 4.4% in 2023 responding to restrictive monetary policy by the Central Bank of West African States, as well as government measures to combat the high cost of living.

Continued reforms to increase domestic revenue and improve budget management helped reduce the budget deficit from 6.8% of GDP in 2022 to 5.2% in 2023, enabling the debt ratio to stabilize at 56.8% of GDP in 2023 (compared with 56.7% in 2022). The current account deficit widened from 7.7% of GDP in 2022 to 8.2% in 2023 due to deficits in services and income. Financial sector performance remains satisfactory, with credit to the economy up 16.2% between 2022 and 2023 and nonperforming loans down 7.2% between December 2022 and June 2023.

According to the second Harmonized Survey of Household Living Conditions, the poverty rate fell from 39.4% in 2018 to 37.5% in 2021. Although the youth (ages 15–24) unemployment rate declined from 5.4% in 2020 to 4.9% in 2023, it remains a major challenge to social cohesion. Strengthening the inclusiveness of growth and enabling the creation of more jobs for young people are at the heart of the government's 2022–24 social program and 2023–25 youth program.

Outlook and risks

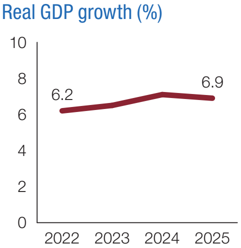
The economic outlook remains favorable, with real GDP growth projected to average 7% in 2024–25, driven by increased cocoa production in response to higher cocoa prices, investment in infrastructure, the development of agro-industrial value chains, and the exploitation of the Baleine field, whose potential is estimated at 2.5 billion barrels of oil and 3,300 cubic feet of natural gas. Inflation is projected to fall below the West African Economic and Monetary Union target of 3% in 2025 thanks to an increase in the local supply of food products. Fiscal consolidation is projected to contain the budget deficit at 4.2% of GDP in 2024 and 3% in 2025. The current account deficit is projected to narrow to 6.9% of GDP in 2024 and 6.1% in 2025, supported by improvements in the terms of trade. However, this outlook could be jeopardized by a deterioration of the security situation in the north, worsened by high youth unemployment; the impact of Russia's invasion of Ukraine; tighter international financial conditions; and climate hazards. Strengthening macroeconomic stability, the inclusiveness and sustainability of growth, and security and institutional stability should make it possible to contain these risks.

Reform of the global financial architecture

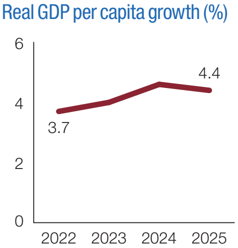
The structural transformation of the economy is proceeding slowly. The industrial sector's share of GDP rose from 16.4% in 2000 to 22% in 2022, while agriculture's share declined from 18.7% to 16.8% and services' share fell from 59.6% to 53.9%. Agriculture's share of employment contracted from 51.1% in 2000 to 40.2% in 2019, while services' share expanded from 36.2% to 47%, and industry's share remained virtually unchanged at 12.6% in 2000 and 12.9% in 2019. Improved agricultural productivity, more complex export products, and investments in infrastructure, technological innovation, and human capital, combined with reforms to increase domestic resources, improve the business climate, and ensure active management of public debt, will accelerate structural transformation.

Since 2014, Côte d'Ivoire has had regular access to international bond markets, with its latest eurobond issue in January 2024 raising $2.6 billion at an average yield of 6.61%. In addition, it has also benefited from a €400 million partial credit guarantee from the African Development Bank, which raised €533 million in sustainable financing on favorable terms. Reforming the global financial architecture should enable the country to benefit from more guarantees, with a view to mobilizing more innovative financing (green funds, sustainable bonds, thematic bonds) on advantageous terms and increase private investment.

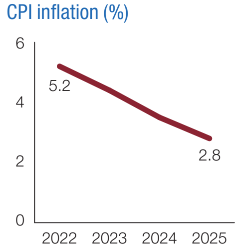
Real GDP growth (%)



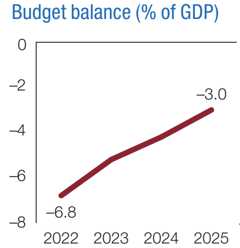
Real GDP per capita growth (%)



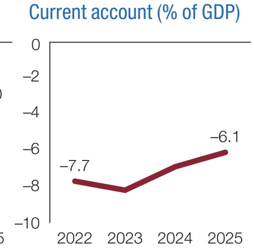
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

The Gambia

Recent macroeconomic and financial developments

Economic activity was resilient in 2023. Real GDP growth improved from 4.9% in 2022 (2.4% in per capita terms) to 5.6% (3.1% per capita). Growth was underpinned by improvements in tourism, construction, and industry on the supply side and by private investment and public spending on the demand side. Inflation accelerated, reflecting higher food and energy prices and a 9.9% exchange rate depreciation. In response, the monetary policy rate was tightened from 10% in March 2022 to 17% in September 2023.

The fiscal deficit narrowed from 4.9% of GDP in 2022 to 3.5% in 2023, due to expenditure restraint and improved customs revenues, but tax revenue remains low at 9.8% of GDP. The public debt-to-GDP ratio improved substantially, from 82.8% of GDP in 2022 to 71.8% of GDP in 2023, on strong nominal GDP growth. The current account deficit deteriorated from 6.1% of GDP in 2022 to 7.6% in 2023, driven by low agricultural exports and higher commodity import prices. International reserves dropped from $454.7 million (5.3 months of import cover) in 2022 to $416.4 million (4.4 months) in 2023 due to higher imports. The financial sector remained resilient, with nonperforming loans down from 4.6% of gross loans in 2022 to 3.5% in 2023, below the prudential requirement. The capital adequacy ratio of 24.6% exceeded the regulatory requirement of 10%.

The cost of living crisis worsened, eroding household incomes and pushing poverty rates from 45.8% in 2019 to 53.4% in 2021. Aggregate unemployment was an estimated 31.6% in 2023.

Outlook and risks

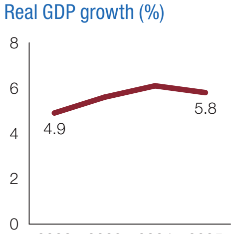
Economic growth is projected at 6.1% in 2024, driven by agriculture, services, and construction and by strong public infrastructure development. The ongoing $25 million threshold program will bolster growth, but vulnerability to extreme weather events could decelerate growth to 5.8% in 2025. Benefiting from strong growth in 2024, the fiscal deficit should narrow to 2.7% of GDP and the current account deficit to 7.2%. Public debt should drop to 65.2% of GDP in 2024 and stabilize at 60.8% in 2025 owing to fiscal consolidation. Inflation could decrease to 12.5% in 2024 and 11% in 2025 in response to restrictive monetary policies and declining global food and energy prices. Risks to growth includer potential disruptions in global supply chains for oil and fertilizers, the impacts of climate change, and a shortfall in budget support disbursements. Fiscal consolidation, improved debt management, and economic diversification are critical for sustained growth.

Reform of the global financial architecture

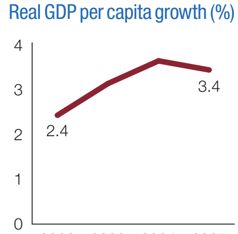
The Gambian economy has experienced dynamic changes in the past decade, with agriculture's share in GDP value added dropping from 35% in 2010 to 23% in 2021, industry's share rising from 9% to 14%, and services' share up from 54% to 62%. Nonetheless, structural transformation has been slow. Labor has exited low-productivity agriculture (down from 30% share in 2010 to 25% in 2021), but it has moved directly into services (up from 52% to 59%), bypassing the high-productivity industry sector (down from 16% in 2010 to 14% in 2021). Investments in infrastructure, technological innovation, and access to finance are critical to bridge the $2.8 billion financing gap essential to fast-track structural transformation.

The Gambia signed a shareholder agreement with Africa50 to govern management of the Senegambia bridge under the Asset Recycling Program. This will unlock capital for further investment in infrastructure. The Gambia also secured $4.14 million in 2020 under the G20 Debt Service Suspension Initiative and $129 million in deferred payments from official bilateral creditors between 2020 and 2024. To benefit from the reform in the global financial architecture, the government should strengthen debt sustainability by prioritizing highly concessional loans. Furthermore, promoting cross-border trade and infrastructure development is crucial to enable The Gambia to benefit from the Africa Continental Free Trade Area.

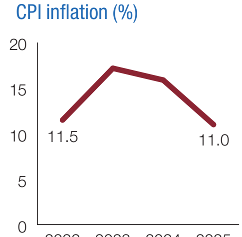
Real GDP growth (%)



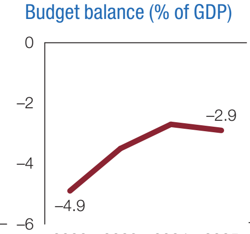
Real GDP per capita growth (%)



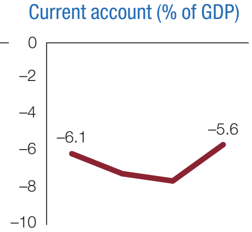
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Ghana

Recent macroeconomic and financial developments

Ghana's real GDP growth decelerated from 3.8% in 2022 to 2.9% in 2023, reflecting spillover effects from Russia's invasion of Ukraine, tight global financial conditions, and macroeconomic challenges. Growth was led by industry on the supply side and by private consumption on the demand side. Inflation worsened from 31.5% in 2022 to 40.3% in 2023, driven mainly by food prices and currency depreciation.

The pace of exchange rate depreciation slowed from 60% in 2022 to 17% in 2023, responding to adjustments in macroeconomic policies. The fiscal deficit narrowed from 11.8% of GDP in 2022to 4.5% in 2023 due to fiscal consolidation and improved revenue performance. Public debt dropped from 92.4% of GDP in 2022 to 84.9% in 2023, reflecting the benefits of the Domestic Debt Exchange Program. The current account deficit narrowed from 2.1% of GDP in 2022 to 1.7% in 2023 on improved export performance. Gross international reserves shrank from $6.3 billion at the end of 2022 (2.7 months of import cover) to $5.0 billion (2.3 months) in November 2023. The financial sector remained sound, with a capital adequacy ratio above the 10% threshold but declining (from 18.22% in 2022 to 13.96% in 2023).

Multidimensional poverty worsened slightly, from 46% in 2017 to 46.7% in 2022, due to the impacts of the Covid-19 pandemic. Youth unemployment remains high at 7.16%, particularly among youths ages 15–24, especially women (36.7% compared with 29.3% among men).

Outlook and risks

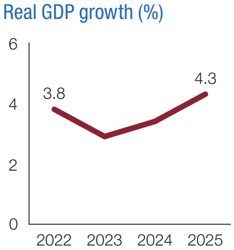
The medium-term growth outlook is positive. GDP growth is projected to rise to 3.4% in 2024 and 4.3% in 2025, led by industry and services on the supply side and private consumption and investment on the demand side. Inflation is expected to remain outside the Bank of Ghana bound of 8±2 at 20.9% in 2024 and 11.1% in 2025. The fiscal deficit is projected to widen slightly to 4.9% in 2024 before narrowing to 4.2% in 2025 as fiscal consolidation efforts continue. The current account deficit is projected to widen to 1.9% in 2024 and 2.3% in 2025. The outlook is clouded by several factors, including the impact of fiscal consolidation under the Post-Covid Program for Economic Growth, the lingering effects of Russia's invasion of Ukraine, limited access to finance and foreign exchange, and global macroeconomic shocks. Prudent macroeconomic management policies could mitigate the risks.

Reform of the global financial architecture

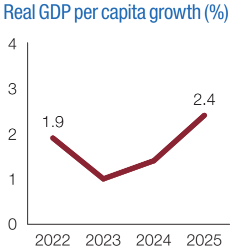
Ghana's structural transformation needs reinforcement. Productivity has stagnated in services, the dominant employment sector, and is rising only slowly in industry and agriculture. Agriculture's employment share declined from 53.9% in 2007 to 29.8% in 2019, while industry's share rose from 14.1% to 21.0% and services' share rose from 31.9% to 49.2% over the same period. To fast-track structural transformation, Ghana must enhance its competitiveness by easing infrastructure bottlenecks; accelerate agro-industrialization by strengthening skills development, value addition, and private sector development; and create a policy framework for technology adoption and innovation.

Financing structural transformation in Ghana requires selective investments in value-added activities that can drive the desired transformation. It also requires building resilience against global shocks, including measures to enhance macroeconomic management and domestic resource mobilization. Key reforms should include improving the coordination and sequencing of public sector development initiatives in line with the country's fiscal position; fast tracking the ongoing debt restructuring, enhancing the scope for concessional finance, and deepening financial markets to increase access to affordable credit; and strengthening stakeholder engagement and coordination of development assistance to maximize synergies and impact.

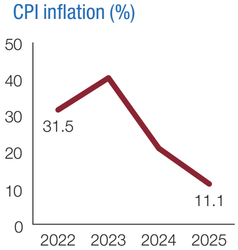
Real GDP growth (%)



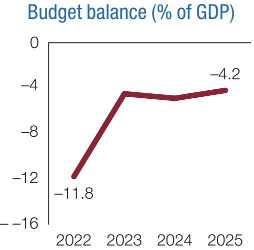
Real GDP per capita growth (%)



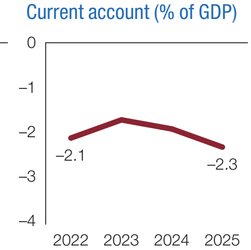
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Guinea

Recent macroeconomic and financial developments

The Guinean economy is one of the most resilient in West Africa. Driven by agriculture and mining, GDP grew an estimated 5.7% in 2023, up from 4% in 2022. Inflation fell from 10.5% in 2022 to 7.8% in 2023. The near stability of the exchange rate against the US dollar has offset imported inflation.

The budget deficit rose from 0.8% of GDP in 2022 to 1.6% in 2023, reflecting the impact of electricity and fuel subsidies, but remains one of the lowest in the Economic Community of West African States (ECOWAS). The budget deficit was financed by bond issues. Public debt fell from 40.1% of GDP in 2022 to 35.2% in 2023. The risk of external debt distress is moderate, but capacity to absorb shocks is limited. The budget deficit and public debt are in line with ECOWAS convergence criteria. The current account deficit remained stable at 8.6% of GDP in both 2022 and 2023, financed by foreign direct investment in the Simandou iron ore mine. Foreign exchange reserves declined from 3.4 of import cover in 2022 to 2.5 months in 2023. The banking sector remains adequately capitalized, but nonperforming loans rose slightly from 8.77% of gross loans in 2022 to 8.95% in 2023.

According to the National Institute of Statistics, Guinea's poverty rate was 43.7% in 2019, down from 55.2% in 2012. The economy is dominated by the informal sector, which in 2023 generated 42% of GDP and 96% of employment (generally not decent jobs). However, GNI per capita rose from $1,010 in 2021 to $1,180 in 2023, moving Guinea from low-income to lower-middle-income status.

Outlook and risks

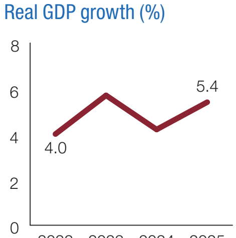
GDP growth is projected at 4.2% in 2024, driven by mining production and investment in the Simandou iron ore mine. The growth deceleration from 2023 is attributable to fuel shortages following the oil depot explosion in December 2023 and a reduction in hydroelectric power supply. Growth is projected to recover to 5.4% in 2025, as electricity supply improves. Inflation is projected to rise above 10% in 2024 and 2025, due to exchange rate depreciation and higher freight costs linked to Russia's invasion of Ukraine. The budget deficit is projected to widen to under 3% of GDP in 2024 and 2025, due to the resumption of infrastructure investment, higher energy subsidies, and election spending. In 2024 and 2025, imports of capital equipment for Simandou are expected to raise the current account deficit above 2023 levels. The generally favorable outlook could be impaired by sociopolitical tensions and by declining foreign direct investment due to geopolitical tensions. Prudent political management and the signing of a program with the International Monetary Fund (IMF) could mitigate risks.

Reform of the global financial architecture

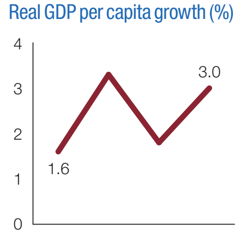
Though dominated by low-productivity services, the economy is diversifying toward industry. Industry's share of GDP rose from 32.1% over 1990–99 to 39.4% over 2010–19, while the share of agriculture, which is undiversified and capital intensive, grew from 19.6% over 2010–19 to 25.6% over 2020–21, with the introduction of improved seeds and fertilizers. These dynamics benefit from investment incentives; greater hydropower supply, which needs to be consolidated; connectivity infrastructure to regional markets; and the import substitution strategy promoted through the National Economic and Social Development Plan 2016–2020 and the Interim Transition Reference Program 2022–2025.

The Interim Transition Reference Program has an annual financing gap of $1.125 billion, in addition to the $1.39 billion a year required over 2020–30 for climate resilience. To bridge this gap, Guinea needs to strengthen its macroeconomic framework, improve the business environment, increase domestic resource mobilization, stimulate dormant private financing (stock market, pension funds, green finance), and attract more foreign direct investment. Signing a program with the IMF would also be a helpful signal for mobilizing the approximately $7 billion in financing from the Dubai Round Table on UN Principles for Responsible Investment. In the short term, multilateral development banks should let Guinea benefit from more Special Drawing Rights and partial risk and credit guarantees. In the medium and long terms, graduation to nonconcessional windows and financing would be useful.

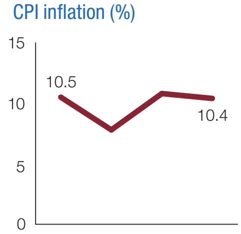
Real GDP growth (%)



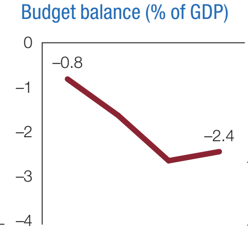
Real GDP per capita growth (%)



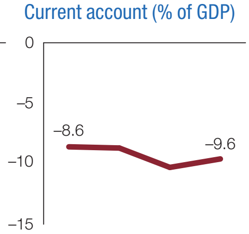
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Guinea Bissau

Recent macroeconomic and financial developments

Despite the difficult economic and political context in Guinea-Bissau, GDP grew 4.3% in 2023, up from 4.2% in 2022, driven by renewed dynamism in agriculture thanks to strong rice production. On the demand side, growth was driven by investment. Higher food prices and higher international rice prices pushed inflation to 7.2% in 2023 from 6.9% in 2022.

Budgetary management was marked by a drop in revenue mobilization, due to tax subsidies on basic necessities and higher spending linked to legislative elections. The budget deficit deteriorated from 6.5% of GDP in 2022 to 7.3% in 2023. It was financed by grants, loans, and public securities, bringing public debt to over 80% of GDP, creating a high risk of debt distress. The current account deficit widened from 8.2% of GDP in 2022 to 8.6% in 2023, impacted by a deterioration in the terms of trade and a drop in sales of cashew nuts, the main export product. Except for one undercapitalized systemically important bank, the financial sector's situation was adequate, marked by a decrease in nonperforming loans from 19.4% of gross loans in 2021 to 10.4% in 2022.

According to World Bank data, the poverty rate (at $3.65 a day in 2017 purchasing power parity terms) rose from 59.9% in 2022 to 60.4% in 2023, reflecting the low yields in cashew nut production, the main source of income for poor households. The youth unemployment rate was an estimated 3.9% in 2023.

Outlook and risks

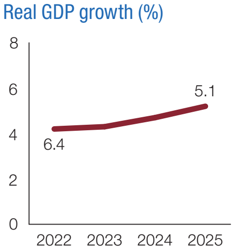
Economic growth is set to consolidate at 4.7% in 2024 and 5.2% in 2025, reflecting continued investment, governance reforms to improve the business environment, and normalization of cashew nut exports. Inflation is projected to fall to 5.4% in 2024 and to 3.1% in 2025, in response to the continued tightening of monetary policy by the Central Bank of West African States. The budget deficit is projected to fall to 3.6% of GDP in 2024 and to 3.2% in 2025 thanks to the government's commitment to accelerate measures to control the wage bill and increase tax revenue. The current account deficit is projected to narrow to 5.2% of GDP in 2024 and to 3.3% in 2025 as cashew nut exports recover. The main downside risks to the outlook include political instability, which could slow fiscal consolidation; uncertainties about cashew nut production; lower demand for raw materials; unfavorable weather conditions; and tighter regional financial conditions, which could limit the issuance of government securities. Mobilizing additional grants and concessional loans from development partners would help the country to cope with persistent external shocks.

Reform of the global financial architecture

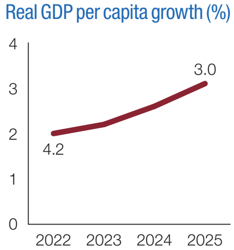
The economy remains dependent on agriculture, which accounted for around 45% of GDP over 2000–20. Industrial production has been low, and its contribution to GDP is estimated at 14%, while services account for 41%. Progress in structural transformation and productivity has been very slow, due to inadequate physical and human capital accumulation. Agriculture's share of employment fell from 61% in 2020 to 50.9% in 2020, while services' share rose from 29% to 39%. Intersectoral productivity is virtually nonexistent, and labor productivity has been low, particularly in agriculture. Investment in manufacturing industries, development of local value chains (agriculture, fishing), capacity building, and access to infrastructure would help boost productivity.

Guinea-Bissau has undertaken reforms and projects that should advance the structural transformation of its economy. However, given the country's high debt, achieving momentum for structural transformation requires substantial concessional external financial support. To take advantage of the global financial architecture, the authorities will need to ensure political and institutional stability, accelerate reforms aimed at transparent governance and mobilization of domestic resources, and improve debt management to reduce the risk of debt distress. International financial institutions could mobilize trust fund resources, simplify access to financing through country risk guarantees, and encourage innovative regional financing (such as green bonds).

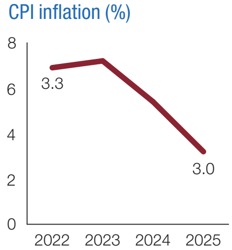
Real GDP growth (%)



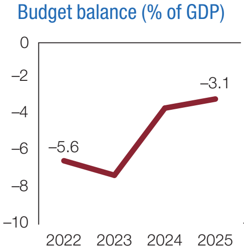
Real GDP per capita growth (%)



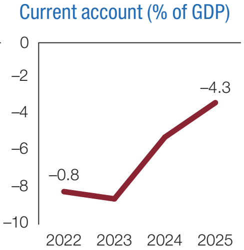
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Liberia

Recent macroeconomic and financial developments

GDP growth is estimated to have declined from 4.8% in 2022 to 4.5% in 2023, driven largely by growth in mining and construction on the supply side and public spending on the demand side. Despite restrictive monetary policy, inflation rose from 7.6% in 2022 to 10.5% in 2023, led mainly by rising domestic food prices and global fuel prices.

The exchange rate depreciated by 22.6% year on year from December 2022 to December 2023 due to increased demand for imports. The fiscal deficit narrowed from 6.5% of GDP in 2022 to 3.0% in 2023 as public spending was cut by 2.9 percentage points of GDP compared with 2022. As of October 2023, public debt stood at 52.6% of GDP, down from 53.4% in 2022, reflecting faster growth in GDP than in debt. The current account deficit narrowed from 23.9% of GDP in 2022 to 22.4% in 2023 due to reductions in the trade deficit. International reserves stood at $478 million in October 2023 (3.8 months of import cover), down from $691 million in 2022 (4.5 months of imports) largely because of depreciation. The financial sector remained sound, with a capital adequacy ratio of 18.2% in October 2023 against a 10% threshold, although the nonperforming loan ratio remained high at 18.2% of gross loans against a 10% threshold.

The poverty rate ($2.15 per person per day) declined from 35.4% in 2022 to 34.2% in 2023. Unemployment is estimated at 3.7% in 2023, unchanged from 2022.

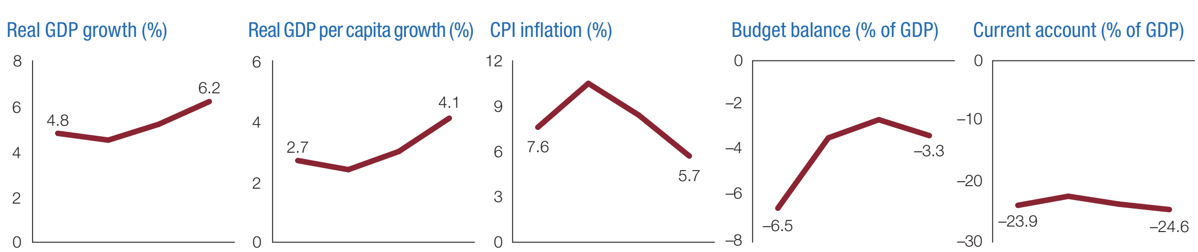
Outlook and risks

Growth is forecast at 5.2% in 2024 and 6.2% in 2025, driven by the expansion of services and agriculture and existing mining projects. Inflation is projected to decline to 8.4% in 2024 and 5.7% in 2025 due to anticipated stability in the exchange rate and tighter monetary policy. The fiscal deficit is forecast to edge from 3.4% of GDP to 4.2% in 2024 and deteriorate further to 4.5% in 2025 on projected increases in government expenditure. The current account deficit is forecast to increase to 23.7% of GDP in 2024 and to 24.6% in 2025, due to projected increases in imports. The exchange rate and financial market are projected to remain stable. Downside risks include Russia's continuing invasion of Ukraine and deterioration of the terms of trade for gold and rubber. Tailwinds include increased demand for Liberia's exports. Mitigation measures could include fiscal consolidation and improved governance.

Reform of the global financial architecture

Structural transformation has been slow. Agriculture's share in value added declined from 66% in 2002 to 29.5% in 2023, while services' share rose from 30% to 51% and industry's from 3.8% to 19.5%. Agriculture's share of total employment declined from 51% in 2002 to 42% in 2023 and industry's from 22% to 10%, while services' share increased from 37% to 48%. Government should promote productivity in natural resources through greater value addition and invest in human capital and infrastructure, particularly roads and energy.

Adequately financing structural transformation in Liberia requires improving revenue collection, reducing public expenditure, managing natural resources, leveraging international support, promoting sustainable debt financing, and strengthening institutions. Liberia needs to establish a Green Bank and to capitalize on its carbon sink services in the carbon market. However, carbon trading should be informed by a robust strategic vision and policy framework. The International Monetary Fund's global financial safety net needs to increase its liquidity provision for Liberia. In the short term, the government should mobilize domestic financial resources and manage its international aid more effectively, focusing on grants and concessional loans that do not raise debt levels. In the medium term, the government should encourage foreign direct investment by improving the business environment.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team. Data on the budget balance correspond to Liberia's fiscal year, which runs from July 1 to June 30.

Mali

Recent macroeconomic and financial developments

Mali's economic recovery from the impacts of the Covid-19 pandemic continues, with growth of 4.3% in 2023, up from 3.7% in 2022. This performance was driven on the supply side by higher production of cotton (up 10.8%) and gold (up 3.02%) and on the demand side by a revival of investment (up 41.8%) and household consumption (up 0.7%). Inflation fell from 9.7% in 2022 to 2.2% in 2023, in response to the combined effects of restrictive monetary policy by the Central Bank of West African States, uninterrupted supply of products to local markets, and the government's 25% customs duty exemption in return for setting ceiling prices on sugar.

The budget deficit improved from 4.9% of GDP in 2022 to 3.8% in 2023, reflecting good mobilization of public resources (98.5% of forecasts) and tight control of spending (92.8% execution rate). Tax revenue mobilization improved from 13.5% of GDP in 2022 to 14.7% in 2023, due to tax reforms. The current account deficit widened from 8% of GDP in 2022 to 8.7% in 2023, due to higher imports of machinery and vehicles (up 55.5%), food products (up 23.2%), and textiles and leather (up 15.1%) and lower exports of cotton (down 13.5%) and gold (down 4.6%). The net deterioration rate of the banking portfolio rose from 4.2% in December 2022 to 5.7% in 2023.

Social conditions improved slightly. The poverty rate fell from 45.5% in 2022 to 45.3% in 2023, as the unemployment rate improved from 7.7% to 6.7%.

Outlook and risks

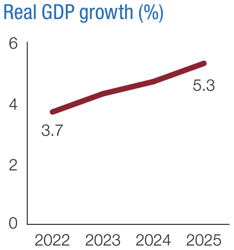
The upturn in economic activity is projected to continue, with growth of 4.7% in 2024 and 5.3% in 2025. Growth will be driven by extractive activities, with the start of lithium production in 2024, the revival of the textiles sector, and development of wheat production and processing potential. Linked to the continuing restrictive monetary policy, inflation is expected to continue to fall to 2% in 2024 and 1.8% in 2025. The budget deficit is projected to worsen to 4.3% of GDP in 2024 and then improve to 3.4% in 2025. The current account deficit is projected to improve to 6.4% of GDP in 2024 and to 5.9% in 2025, due to higher cotton exports in 2024 and higher gold exports in 2024 and 2025, combined with the start of lithium exports in 2024. The main downside risks to the outlook include the postponement of the presidential election, which had been scheduled for February 2024; the energy crisis; the country's withdrawal from the Economic Community of West African States; climate shocks; and insecurity. Mitigation measures include continuing political and institutional reforms, support for the energy sector, and the ongoing fight against terrorism.

Reform of the global financial architecture

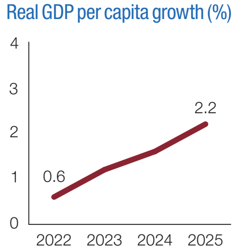
Structural transformation has been slow, with agriculture's share of employment falling from 69.3% in 1991 to 67.7% in 2021, and industry's share rising only slightly, from 8% in 1991 to 10% in 2021. Accelerating structural transformation requires urgent measures to mitigate the electricity deficit, strengthen transport infrastructure to increase internal trade and external trade at the regional level, reinforce the agricultural growth pole program, improve the business climate, and accelerate development of human capital.

Insecurity and political instability reduced Mali's access to the international financial market in 2022. Reforming the global financial architecture should enable the country to increase external financing. Priority should be given to political and institutional reforms and to strengthening security. As a backup, other reforms should aim to reduce risks that increase the cost of debt and prepare for a securities issue on the international financial market, following unsuccessful attempts at a eurobond issue in 2019. In addition, Mali should diversify its financing sources and consider issuing government bonds targeting its large diaspora, to channel their resources toward restructuring investments and green bonds. Reforming the global financial architecture should promote access to more grants (only 60.7% of which were implemented in 2023) and concessional financing, including budget support (suspended since 2022 due to political instability) and the granting of partial risk, credit, and trade guarantees.

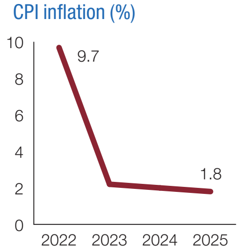
Real GDP growth (%)



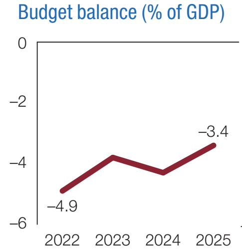
Real GDP per capita growth (%)



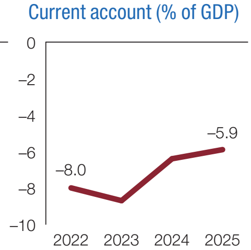
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Niger

Recent macroeconomic and financial developments

Economic activity slowed to 2.5% in 2023, as the political regime changed in July, economic and financial sanctions were imposed by the Economic Community of West African States (ECOWAS) and the West African Economic and Monetary Union (WAEMU), and external funding was frozen by the country's main technical and financial partners. The limited economic growth was due mainly to higher oil production and agriculture on the supply side and to increased final consumption on the demand side. Inflation fell from 4.2% in 2022 to 3.7% in 2023, due to a good agricultural season.

The budget deficit improved to 5% of GDP in 2023, linked to reduced investment spending because of a freeze on external financing. Despite accumulated debt servicing arrears, debt stabilized at approximately 50% of GDP in 2023. The current account deficit narrowed from 16.1% of GDP in 2022 to 12.8% in 2023, due mainly to a large sanction-linked drop in imports from 27.2% of GDP in 2022 to 23.5%. The economic and financial sanctions also slowed banking activity, depreciated the quality of bank receivables (for example, the gross portfolio deterioration rate rose from 15.9% in the second quarter to 21.5% in the third quarter of 2023, well above the WAEMU average), and reduced foreign exchange reserves to 4.6 months of import cover. The rate of nonperforming loans was 18.2% of gross loans.

Sanctions increased the estimated incidence of poverty by 1.9 percentage points to 43.9% at the end of 2023, according to the National Institute of Statistics. Food insecurity and the precarious health situation prior to the political change also worsened.

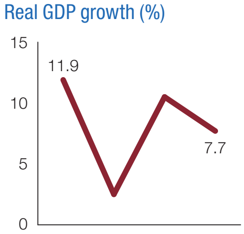
Outlook and risks

The economic outlook for 2024 and 2025 is favorable. Growth is expected to be driven mainly by hydrocarbons—with a five-fold increase in crude oil production to approximately 100,000 barrels a day, up from 20,000—and by the resilience of the agricultural sector. Economic activity is projected to also benefit from the lifting of ECOWAS economic and financial sanctions and the resumption of external financing by the main technical and financial partners. Economic growth is projected to reach 10.4% in 2024 then to slow to 7.4% in 2025. Inflation in 2024 and 2025 should be contained by agricultural sector performance. A substantial increase in tax revenue with the resumption of commercial activities and oil revenue is expected to result in budget consolidation in 2024 and 2025. But the budget deficit is projected to remain above the WAEMU convergence criterion (3% of GDP). The current account balance is projected to improve greatly, benefiting from the surge in oil production. Downside risks to these favorable economic prospects are linked to climate change, insecurity, and the negative effects of the country's announced exit from ECOWAS.

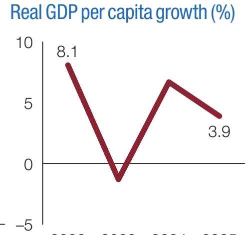
Reform of the global financial architecture

The structure of the economy has changed little over the past two decades. From 1991–2000 to 2011–2020, agriculture's share of GDP rose from 33% to 34.9%,industry's share rose from 21.3% to 22.4%, and services' share rose from 36.9% to 38.7% The main obstacles to structural transformation in Niger are linked to low factor productivity, which hinders economic diversification. The infrastructure deficit is a major impediment to competitiveness and structural transformation. The financial sector remains underdeveloped for mobilizing and allocating savings to development needs. Despite recent progress driven by the financial inclusion strategy, Niger's financial sector represents only 4.1% of WAEMU's market share. The credit-to-GDP ratio is barely 13%, compared with a WAEMU average of above 25%. Before the change in the political regime in July 2023, the country had substantially increased the concessional resources mobilized from bilateral and multilateral development institutions (including the African Development Bank, the World Bank, and the International Monetary Fund), mainly by implementing economic reforms. To continue to benefit from the global financial architecture and concessional resources, Niger must first return to institutional stability and pursue economic and financial reforms. In the medium to long term, it needs more effective strategies for developing the financial sector and mobilizing revenue from exploitation of its natural resources.

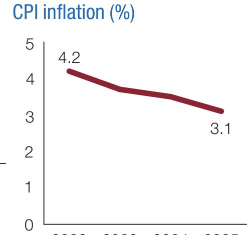
Real GDP growth (%)



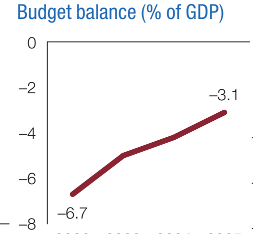
Real GDP per capita growth (%)



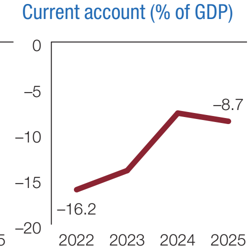
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Nigeria

Recent macroeconomic and financial developments

Economic growth in Nigeria slowed from 3.3% in 2022 to 2.9% in 2023 due to high inflation and sluggish growth in the global economy, which declined from 3.5% in 2022 to 3.2% in 2023. Growth was driven by services and agriculture on the supply side and by consumption and investment on the demand side. Inflation rose from 18.8% in 2022 to 24.5% in 2023, due to rising fuel costs and a depreciating naira. Petrol prices increased 167%, from naira 254 per liter in May 2023 to naira 671 in December 2023.

The exchange rate depreciated by 95.6% in 2023, resulting from the floating of the naira in June 2023. Monetary policy was tightened to control inflation, with the policy rate increased from 17.5% in January 2023 to 18.75% in December 2023. The fiscal deficit narrowed from 5.4% of GDP in 2022 to 5.1%, as general government revenues improved from 6.7% of GDP in 2022 to 7.6% in 2023, although remaining low. The deficit was financed mainly by domestic borrowing, including from the Central Bank's Ways and Means. Public debt remained low at 40% of GDP in 2023, but the federal government debt service to revenue ratio was high, at 111%, due to weak revenues. The current account surplus improved from 0.2% of GDP in 2022 to 0.9% in 2023, driven by higher oil prices and exports. International reserves remained robust but dropped from 6.6 months of import cover in 2022 to 5 months in 2023, reflecting tight global financing conditions.

The poverty level remains high, with multidimensional poverty at 63% and income poverty at 40%. Income inequality is lower than in many middle-income countries, with a Gini coefficient of 0.35.

Outlook and risks

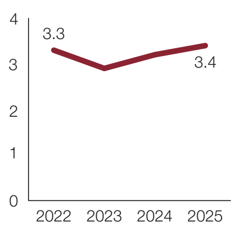
Economic growth is projected to increase to 3.2% in 2024 and 3.4% in 2025, due to improved security, higher oil production, and stronger consumer demand. Inflation is expected to rise to 31.6% in 2024, driven by higher food prices and continued depreciation of the naira, before moderating to 20.7% in 2025 as inflationary pressures abate. The fiscal deficit, financed by domestic borrowing, is projected to narrow to 4.3% of GDP in 2024 and 4.1% in 2025 as both oil and non-oil revenues improve. The current account surplus is expected to improve to 3.0% of GDP in 2024 and 3.6% in 2025 due to higher oil exports. Headwinds include insecurity, lower oil production, rising fuel and food prices, and further exchange rate depreciation. Tailwinds include new oil production from the Dangote refinery, which is expected to lower energy prices as it starts supplying the local market.

Reform of the global financial architecture

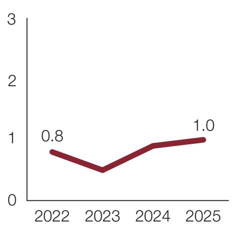
Despite some evidence of structural transformation, reflected in agriculture employment's falling share in total employment from 49.3% in 2000 to 35.2% in 2021, the pace of transformation is not sufficient to propel industrial take-off. Labor has relocated to the services sector, whose share of employment rose from 39.4% in 2000 to 52.1% in 2021. However, industry's share of employment has increased only marginally over the past 20 years, from 11.3% to 12.7%, reflecting slow industrialization. Furthermore, wage employment is low, at 11.8%, reflecting low-quality jobs and characterized by high informality, at 92.6%.

To finance structural transformation, Nigeria needs to accelerate domestic resource mobilization, especially by reforming tax administration. The African Development Bank is supporting the introduction of an integrated unique identification system aimed at improving tax compliance. Nigeria also faces exorbitant financing costs in global financial markets, with its 30-year bond trading at a double-digit yield of 11.11% in January 2023 (and 10.58% in April 2024) compared with 8.25% at issue in 2021. Consequently, Nigeria was unable to mobilize financing from the eurobond market in 2023. As part of the reform of the global financial architecture, establishing an African Financial Stability Mechanism could help Nigeria access liquidity at a lower cost. Furthermore, multilateral development banks can reform their risk capital models to allow additional lending capacity to regional member countries, including through risk transfer and balance sheet optimization instruments.

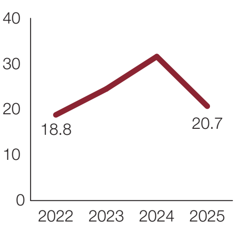
Real GDP growth (%)



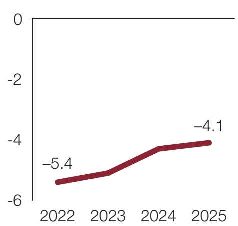
Real GDP per capita growth (%)



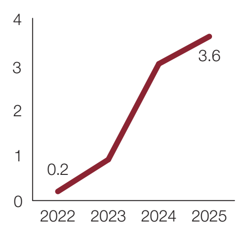
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Senegal

Recent macroeconomic and financial developments

The real GDP growth rate rose from 3.8% in 2022 to 4.3% in 2023, driven by the resilience of the agricultural sector. While services experienced a downturn (from 6.7% growth in 2022 to 3.9% in 2023), due to restrictive measures on the Internet and transport, GDP growth was sustained by agriculture and industry. Inflation fell from 9.7% in 2022 to 5.9% in 2023, responding to government efforts and tighter monetary policy by the Central Bank of West African States, which raised the minimum liquidity injection rate from 2% in 2022 to 3.25%.

Due to increased revenue and rationalized subsidies, the budget deficit narrowed from 6.5% of GDP in 2022 to 4.9% in 2023. The fiscal deficit buildup led to an increase in debt from 76% of GDP in 2022 to 80% in 2023. The current account deficit narrowed from 20% of GDP in 2022 to 15.2% in 2023 due to reduced oil investment. The financial sector performed well, with equity rising 13.4% in 2023 and nonperforming loans falling from 11.3% of gross loans in 2022 to 9.9% in 2023. Credit to the private sector increased by 20.8% in 2023 against 22.2% in 2022.

According to the National Agency for Statistics and Demography, the poverty rate fell from 38% in 2011 to 32.9% in 2019, due to rising agricultural income, higher public investment, and stronger social services. However, according to the World Bank, that trend has been reversed by recent shocks, and the poverty rate was projected to rise from 35.9% in 2021 to 36.3% in 2022. Extended unemployment fell from 24.1% in 2021 to 19.5% in 2023 and affects women (32%) more than men (10%).

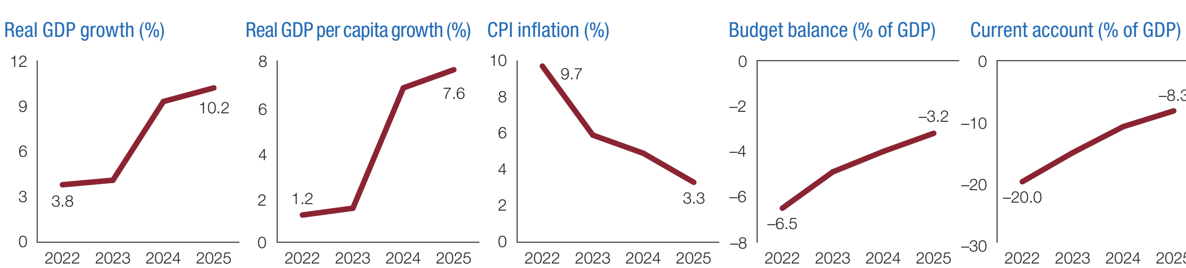
Outlook and risks

Projected oil production for 2024 makes the macroeconomic outlook very favorable. Economic growth is projected to reach 9.3% in 2024 and 10.2% in 2025. The fiscal deficit is projected to narrow further to 4% of GDP in 2024, with the implementation of measures to reduce energy subsidies from 3% of GDP in 2023 to 1% in 2024. These efforts and the robust growth prospects are expected to reverse the upward trend in debt. The external position is expected to further improve with the start of hydrocarbon production in 2024. But this outlook faces major risks if there is a lack of consensus on the review process for oil and mining contracts. Other risks to the macroeconomic outlook include structural vulnerability linked to climate change, delay in oil production, Russia's invasion of Ukraine, the war in the Middle East, deterioration in terms of trade, and tightening financial conditions. Greater macroeconomic stability and economic diversification are key to mitigating these risks.

Reform of the global financial architecture

Over time, the structure of the economy has shifted to services. As the agricultural sector's share of employment declined from 50% in 2000 to 20% in 2022, the services sector's share rose from 38% to 56%. The services sector has made the greatest contribution to productivity through intersectoral growth, facilitating the flow of labor from the low-productivity agricultural sector. The government's Plan for an Emerging Senegal has identified flagship projects (the Train Express Regional, highways, renewable energy) to boost productivity. Structural transformation could be accelerated through implementation of the new industrial policy, the private sector development strategy, and agricultural growth poles.

To accelerate structural transformation, Senegal will need to mobilize more resources on international capital markets. Senegal raised $5.3 billion in eurobonds between 2009 and 2021, reflecting the country's stability and solid institutions. Reforming the global financial architecture should enable the country to mobilize additional financing on more favorable terms. But to take full advantage of these financing options, the government needs to maintain macroeconomic stability to bolster the confidence of international investors, focus on public securities in local currency, deepen the regional market with the introduction of green bonds, and prioritize external financing on concessional terms. Support from international financial institutions will also be needed, with guarantees for borrowing on competitive terms.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Sierra Leone

Recent macroeconomic and financial developments

Sierra Leone's economic growth slowed from 3.5% in 2022 to 2.6% in 2023 as Russia's invasion of Ukraine triggered rapid increases in commodity prices. Growth was driven by higher mining and agribusiness exports on the demand side and by iron ore production and recoveries in agriculture, manufacturing, and tourism sectors on the supply side. Inflation accelerated from 27% in 2022 to 46.6% in 2023 driven by food and fuel prices, depreciation of the leone, and supply-side constraints. The Bank of Sierra Leone tightened monetary policy, raising the policy rate from 18% in 2022 to 22.25% in December 2023.

The fiscal deficit narrowed from 9.6% of GDP in 2022 to 5.8% in 2023. The public debt-to-GDP ratio declined from 98.8% in 2022 to 90.5% in 2023 due to the lower primary deficit. The current account deficit narrowed from 8.3% of GDP in 2022 to 6.1% in 2023, reflecting increases in exports and grants. The current account deficit was financed from the financial account. Gross foreign reserves stood at $432.9 million in October 2023 (3 months of import cover). The depreciation of the leone moderated from 39.1% in 2022 to 17.2% in 2023 as administrative barriers were lifted in the foreign exchange market. Nonperforming loans fell from 14.8% of gross loans in 2021 to 11.6% in 2022 against a regulatory limit of 10%. The capital adequacy ratio declined from 39.8% in 2021 to 35% in 2022.

The poverty headcount ratio was 56.8% in 2018, and the extreme poverty rate was 25% in 2023. Youth unemployment was 10% in 2022, but underemployment is much higher.

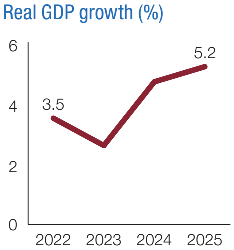
Outlook and risks

Growth is projected to improve to 4.7% in 2024 and 5.2% in 2025, driven by the mining sector and recovery in agriculture, manufacturing, construction, and tourism. Inflation is projected to decline to 33.6% in 2024 and 20.2% in 2025, as external shocks subside. The fiscal deficit is projected to narrow to 2.8% of GDP in 2024 and 2.4% in 2025, due to higher tax revenue. The current account deficit is expected to narrow to 4.2% of GDP in 2024 and 2.1% in 2025, as official and private grants increase. Downside risks to the outlook include the possibility of a global economic recession, the continuation of Russia's invasion of Ukraine, and declining international financial assistance. Risk mitigation measures could include boosting domestic revenue mobilization, reprioritizing spending to create fiscal space, and accelerating reforms to improve economic diversification, accelerate structural transformation, and increase resilience to recurring external shocks.

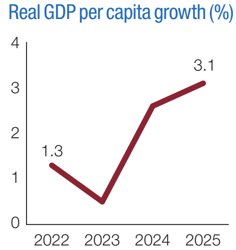
ReReform of the global financial architecture

Sierra Leone has not made progress in structural transformation. Agriculture grew from 47% of GDP in 2003 to 60% in 2022, while its employment share dropped from 66.5% to 43%. Industry declined from 10% of GDP in 2003 to 7% in 2022, while its employment share rose from 6.2% to 12%. Services contracted from 37.6% of GDP in 2003 to 29% in 2022, while its employment share expanded from 27% to 45%. The country needs more investment in infrastructure and human capital to foster industrialization and structural transformation. The government has ramped up investments in power, nearly doubling the installed electricity generation capacity to 253 megawatts in the past five years. To finance structural transformation, Sierra Leone needs to focus on domestic resource mobilization and governance of its natural resources. It also needs to leverage international development assistance through reform of the global financial system. To reduce debt vulnerabilities in the short term, the government should prioritize grants and concessional loans and improve the business regulatory environment to attract foreign direct investment. In the long term, the government needs to develop domestic capital markets, enhance trade, and deepen regional integration.

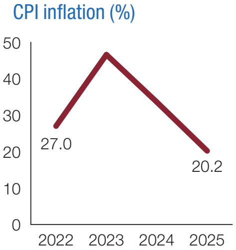
Real GDP growth (%)



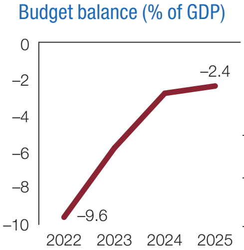
Real GDP per capita growth (%)



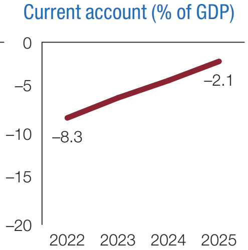
CPI inflation (%)



Budget balance (% of GDP)



Current account (% of GDP)



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

Togo

Recent macroeconomic and financial developments

Economic activity remains sluggish, with real GDP growth falling from 5.8% in 2022 to 5.6% in 2023, driven by developments in agriculture (contributing 1 percentage point to GDP growth), industry (2 percentage points), and services (2.6 percentage points). Inflation fell from 7.6% in 2022 to an estimated 5.3% in 2023, driven by lower food prices and subsidies on fuel and electricity prices.

The budget deficit narrowed from 8.3% of GDP in 2022 to 6.9% in 2023, responding to fiscal consolidation and public finance management reforms. The current account balance remained structurally in slight deficit, worsening from 2.8% of GDP in 2022 to 3.2% in 2023, due to rising prices for imported goods. Credit to the economy, in particular to the private sector to boost economic activity, increased 4.5% in 2023, from CFAF 1.663 trillion in 2022 to CFAF 1.739 trillion. The gross deterioration rate in banks' loan portfolios fell from 11% in March 2022 to 9% in 2023 due to recovery in overdue loans, which boosted the financing capacity of the banking system. The risk of debt distress is moderate. Outstanding public debt, at 67.2% of GDP in 2023 compared with 67.2% in 2022, was below the West African Economic and Monetary Union ratio of 70%.

Poverty and inequality remain high. According to the latest Harmonized Household Living Conditions Survey (2018), poverty incidence was an estimated 45.5% in 2019, down from 53.5% in 2017. Inequality persists, with the Gini coefficient rising from 0.393 in 2011 to 0.427 in 2017.

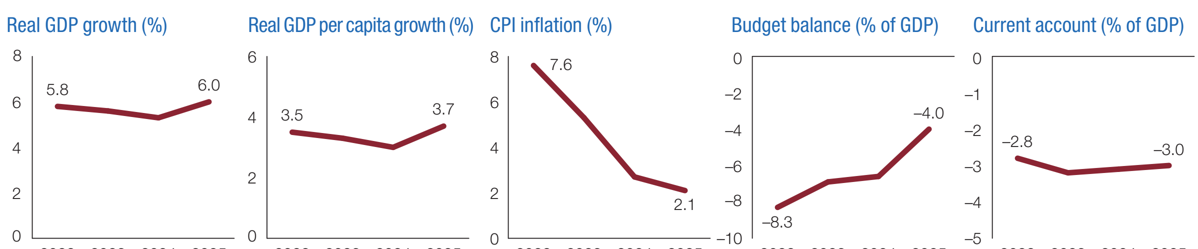
Outlook and risks

The economic outlook is favorable, benefiting from structural reforms and key investment projects. Real GDP is projected to grow 5.3% in 2024 and 6.0% in 2025, driven by the dynamism of agriculture and private investment. The inflation rate is expected to continue its downward trend to 2.7% in 2024 and 2.1% in 2025, as energy price subsidies continue. The budget deficit is projected to improve to 6.6% of GDP in 2024 and to 4% in 2025, attributable to public finance management reforms. However, energy subsidies could keep the budget in deficit over the long term. The current account deficit is projected to narrow to 3.1% of GDP in 2024 and 3% in 2025, due to lower prices for imported goods, including petroleum products. The main risks to the economic outlook are a potential escalation of terrorist violence in parts of the country, lower agricultural yields, and volatility in world phosphate prices. In addition, economic activities are likely to be hampered as the new constitution goes into effect. But these risks can be mitigated through effective coordination of fiscal policies, continued structural reforms, political dialogue, and social calm.

Reform of the global financial architecture

Foreign trade accounts for 58% of Togo's GDP, and phosphates are one of the country's main foreign currency–earning exports. Togo's transport infrastructure makes it a regional hub for hinterland countries such as Burkina Faso, Mali, and Niger. Structural transformation of the economy is in its early stages, and momentum needs to be consolidated. The agricultural sector's share of value added GDP declined from 32.8% in 2001–2010 to 27.7% in 2011–2020, while services' share rose from 48.9% to 51.9% and industry's share rose from 18.2% to 20.4%. The Togo 2025 Roadmap, which targets structural transformation and sustainable, inclusive growth, needs to be accelerated.

Accelerating structural transformation requires modernizing agriculture and increasing productivity, improving access to energy, consolidating the industrial fabric by developing agro-industrial processing zones, and creating a business climate that can attract lower cost financing. In addition, reforming the global financial architecture should make it possible to optimize the benefits of international capital flows, giving Togo privileged access to substantial concessional resources to meet its growing development needs. In the medium term, obtaining technical assistance to access nonconcessional resources—in particular, partial guarantees (risk, credit, and trade) for public-private partnerships—and strengthening the macroeconomic framework should be explored.



Source: Data are as of April 2024 and are from domestic authorities; figures for 2023 are estimates and figures for 2024 and 2025 are projections by the African Economic Outlook team.

ABBREVIATIONS

ACMI	African Carbon Markets Initiative
ACRA	African Credit Rating Agency
ADF	African Development Fund
AEO	African Economic Outlook
AfCFTA	African Continental Free Trade Area
AfDB	African Development Bank Group
AFMI	African Financial Markets Initiative
AFSM	African Financial Stability Mechanism
AGBI	African Green Bank Initiative
AIF	Africa Investment Forum
ANS	Adjusted Net Savings
ASUT	Africa Supply and Use Tables
AU	African Union
ATAF	African Tax Administration Forum
BEER	Behavioral Equilibrium Exchange Rate
BEPS	Base Erosion and Profit Shifting
BMA	Bayesian Model Averaging
bps	Basis points
BRICS	Brazil, Russia, India, China, and South Africa
CAF	Capital Adequacy Framework
CAW	Climate Action Window
CEMAC	Central African Economic and Monetary Community
CFA	Communauté Financière Africaine/ Coopération Financière en Afrique
CI	Confidence Interval
CIA	Central Intelligence Agency
CO2	Carbon dioxide
COP27	Conference of the Parties, 27th session
COP28	Conference of the Parties, 28th session
COVID-19	Coronavirus disease
CPI	Consumer Price Index
DAC	Development Assistance Committee
DFI	Development Financial Institution
DRC	Democratic Republic of Congo
DRM	Domestic Resource Mobilization
DSA	Debt Sustainability Analysis
DSF	Debt Sustainability Framework
ECA	United Nations Economic Commission for Africa
ECB	European Central Bank
ECCAS	Economic Community of Central African States
ECCE	Country Economics Department
ECF	Extended Credit Facility
ECI	Economic Complexity Index
ECMR	Macroeconomic Policy, Forecasting, and Research Department
ECNR	African Natural Resources Management and Investment Center
ECST	Statistics Department
ECVP	Economic Governance and Knowledge Management Vice-Presidency
EIA	US Energy Information Administration
EIB	European Investment Bank
EITI	Extractive Industries Transparency Initiative
EMBI	Emerging Markets Bond Index
ESG	Environmental, Social, and Governance
ETD	Economic Transformation Database
EU	European Union
FDI	Foreign Direct Investment
FEER	Fundamental Equilibrium Exchange Rate
G20	Group of 20
G7	Group of 7
GCA	Global Center on Adaptation
GCI	Generalized/General Capital increase
GDP	Gross domestic product
GERD	Gross Domestic Expenditure on Research and Development
GFA	Global Financial Architecture
GFF	Green Finance Facility
GFI	Global Financial Institution
GLS	Generalized Least Squares
GMM	Generalized Method of Moments
GNI	Gross National Income
HIC	High-Income Country
HIPC	Heavily Indebted Poor Countries Initiative
HIV	Human immunodeficiency virus
IBM	International Business Machines Corporation
IBRD	International Bank for Reconstruction and Development
ICT	Information and communication technologies
IT	Information Technology
IDA	International Development Association
IDS	International Debt Statistics
IEA	International Energy Agency

IFI	International Financial Institution
IIP	Integrated Industrial Platforms
ILO	International Labor Organization
IMF	International Monetary Fund
IMFC	International Monetary and Financial Committee
IPCC	Intergovernmental Panel on Climate Change
IRENA	International Renewable Energy Agency
ITMO	Internationally Transferred Mitigation Outcome
ITU	International Telecommunication Union
IV	Instrumental Variable
KtCO2e	Kiloton of carbon dioxide equivalent
kWh	kilowatt-hour
LCOE	Levelized Cost Of Electricity
LIC	Low-Income Country
LMIC	Lower Middle-Income Country
LSDV	Least Squares Dummy Variable
LTE	Long Term Evolution
MDB	Multilateral Development Bank
MEO	Macroeconomic Performance and Outlook
MPA	Multipronged Approach to Address Debt Vulnerabilities
MtCO2e	Million tons of carbon dioxide equivalent
NASA	National Aeronautics and Space Administration
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OLS	Ordinary Least Squares
OPEC	Organization of the Petroleum Exporting Countries
O&M	Operation and Maintenance
PAISD	Program for Solidarity Initiatives for Development
PASS	Pan-African Payment and Settlement System
PFM	Public Finance Management
PFMA	Public Finance Management Academy
PMI	Purchasing Managers' Index
PPG	Public and Publicly Guaranteed
PPP	Private Public Partnership
PRGT	Poverty Reduction and Growth Trust
PV	Photovoltaics
REDD+	Reducing Emissions from Deforestation and Forest Degradation
RST	Resilience and Sustainability Trust
R&D	Research and Development
SACU	Southern African Customs Union
SAPZ	Special Agro-Industrial Processing Zone
SCDI	State-Contingent Debt Instrument
SDG	Sustainable Development Goals
SDR	Special Drawing Rights
SEGA	Strategy for Economic Governance in Africa
SME	Small and Medium-sized Enterprise
STEM	Science, Technology, Engineering, and Mathematics
S&P	Standard & Poor's
TA	Technical Assistance
UK	United Kingdom
UN	United Nations
UNCTAD	United Nations Trade and Development
UNDP	United Nations Development Programme
UNECA	United Nations Economic Commission for Africa
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNIDO	United Nations Industrial Development Organization
UMIC	Upper Middle-Income Country
US	United States
USAID	The United States Agency for International Development
VAT	Value Added Tax
VIX	Chicago Board Options Exchange's CBOE Volatility Index
VTA	Voluntary Trading Arrangement
WAEMU	West African Economic and Monetary Union
WAMU	West African Monetary Union
WDI	World Development Indicators
WEO	World Economic Outlook
ZIG	Zimbabwe gold
ZWL	Zimbabwe dollar

Amid multiple successive headwinds, Africa's average real GDP growth of 3.1 percent in 2023 was second only to that of developing Asia (4.7 percent). This growth outturn for Africa was, however, lower than the previous year's 4.1 percent due to persistently high inflation, weak global demand for the continent's exports, heightened exchange rate depreciations, impacts of climate change, and pockets of political instability in some countries. The outlook for the medium term appears more favorable, as global, regional, and domestic economic conditions gradually improve. Average real GDP growth is projected at 3.7 percent in 2024 and could strengthen further to reach 4.3 percent in 2025. At the projected growth rate, Africa is poised to retain its position as the second fastest growing region after developing Asia in 2024. Importantly, growth in 17 African economies is projected to exceed 5 percent in 2024 and 10 of them could join the world's top 20 fastest growing economies.

The positive outlook is subject to several caveats, however. Domestic inflationary pressures remain entrenched, and with continued strengthening of the United States dollar, domestic currencies in Africa could stay pressured. High food prices will also complicate deploying traditional monetary policy tools to lower inflation to single digits in a majority of countries. The gridlock in trade and investment, protracted by rising geopolitical tensions, may offset any gains from domestic policy interventions. Regional conflicts and political instability as well as climate shocks should also be closely watched to avoid weakening growth.

Africa's average growth had been sustained at about 4 percent for four decades before the outbreak of COVID-19. However, Africa's real GDP per capita growth has not grown fast enough—and has been consistently one of the lowest in the world since the 1980s—and thus unable to engender rapid socioeconomic transformations and improve people's living conditions. A major factor for this asymmetry is that the structure of most African economies has remained relatively unchanged, with traditional sectors—mainly agriculture, travel, transport, and other low-skilled services—continuing to drive Africa's growth and employment. For instance, the agriculture sector alone accounts for 42 percent of the continent's workforce, yet it is 60 percent less productive than the economywide productivity rate.

Accelerating the pace of Africa's structural transformation is essential to engendering inclusive growth, but it will require substantial resources to invest in critical sectors that add value to the continent's vast natural resources. The Bank estimates that closing an annual financing gap of about $402 billion by 2030 and prioritizing investment in education, energy, productivity, and infrastructure—coupled with effective and consistent implementation of domestic endogenous programs—could unlock the continent's transformation potential. Africa should also capitalize on the emerging high value services sector and leveraging its main features—smaller firms, high productivity, and greater labor intensity—to develop a services-led growth model. That model should include the promotion of tradable and nontradable services such as tourism, business, finance, and ICTs, with significant potential to generate foreign exchange to finance Africa's structural transformation. Domestic efforts to promote manufacturing led-industrialization would ensure that the continent catches up with high-performing developing countries from other regions.

The scale of resources to support Africa's structural transformation cannot be generated solely from domestic sources, even with significant improvement in revenue collection. External resources—both public and private—should be explored to complement domestic resources. However, this calls for radical reforms of the global financial architecture to make it inclusive, nimble, and fit for purpose to mobilize resources at scale and affordable terms. The growing momentum of international calls for reforms present an opportunity for Africa to ensure that the reformed global financial system is responsive to its needs, particularly to finance structural transformation and the SDGs as well as climate action and other global public goods.

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