Macro Dev

Macroeconomics & development

SEPTEMBER 2021 | No. 36

SEMESTRIAL PANORAMA 2021

Hard Times for Developing Countries : Africa's Financing Needs in Question

Coordinated by Sylvain Bellefontaine (AFD)

Translated by Cadenza Academic Translations

AFD éditions
AGENCE FRANÇAISE DE DÉVELOPPEMENT

MacroDev - Semestrial Panorama

Semestrial Panoramas are special issues of the MacroDev series written by AFD analysts; They present a synthesis of macronomic et socioeconomic analyses of emerging and developing countries. In addition to short, country-focused articles, a thematic section sheds light on broader economic and structural issues affecting these countries.

List of authors: Sylvain Bellefontaine, Cécile Duquesnay, Marion Hémar, Benoît Jonveaux, Laura Marie, Emmanuelle Monat, Jules Porte, Meghann Puloc'h, Bertrand Savoye, Maxime Terrieux, Cécile Valadier

Acknowledgements: the authors wish to thank the AFD publishing team for their enthusiastic support and in particular Etienne Charrière for carefully editing the manuscript.

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Editorial

A tale of two worlds

Cécile Valadier—valadierc@afd.fr

The divergence between the trajectories of advanced economies and those of emerging and developing countries (EDCs), which had already begun at the end of 2020, is becoming even more marked, with the latter showing all the symptoms of long COVID. The prospects for a vigorous recovery in advanced economies (+5.6% in 2021, according to the latest projections by the IMF) should, however, be good news. The sustained rise in commodity prices since the summer of 2020, as well as the rebound in the international trade in goods, has improved the external environment for many exporting EDCs, although rising food prices are a concern, particularly in low-income countries. While nearly 35% of the population in advanced economies had been vaccinated by the end of June 2021, this proportion was only 10% in emerging countries and less than 2% in low-income countries. A lack of access to immunization casts a shadow over all economic activities that are impacted by social distancing. Restrictions on international mobility are also expected to have lasting effects on economies that depend on the tourismsector. In addition, there are strong constraints on the ability of EDCs to adoptimplement sustainable countercyclical monetary and fiscal policies. Inflationary pressures generated by the depreciation of some emerging currencies against the dollar or by a faster-than-expected tightening of US monetary policy are likely to leave little room for maneuver for central banks in emerging countries to support a recovery that is slow to materialize. In this case, by increasing the burden of interest on the public debt, the steepening of the yield curve on local- or hard-currency bonds would increase the burden of public debt interest and increase thus the pressure on a fiscal space that is already constrained by the expenditures that the crisis has required. In a context of high indebtedness, and with the risks of refinancing far from over, the way out of the crisis for EDCs is fraught with pitfalls, and that means that renewed support from the international community will be required. In line with the immediate response to the crisis via the increase in financing from official creditors and the launch of the Debt Service Suspension Initiative (DSSI), the general special drawing rights (SDR) allocation approved by members of the IMF should help strengthen the liquidity of these economies (with USD 275 billion of the USD 650 billion total allocation going to EDCs). Similarly, the Common Framework for Debt Treatments aims to restore the solvency of the countries that will benefit from it. In view of the challenges facing the global economy and the interdependence between advanced economies and EDCs, the extension of existing mechanisms and innovation in international governance remain priorities.

This semi-annual publication aims to shed light on the economic trajectories of the countries in which the Agence française de développement (AFD, French Development Agency) operates. These analyses are based on close monitoring over a long period and are rooted in a detailed knowledge of local contexts. Cyclical developments, which are often highlighted in the news, are systematically examined in the light of long-term trends in these economies. Finally, special emphasis is placed on developing countries for which macroeconomic analyses are rare or occasional, in order to complement existing publications on the latest global economic developments, which tend to concentrate on advanced economies and large emerging countries. This first issue thus focuses largely on African economies, in a context of rapid transformation across the continent, at a time when the impact of the COVID-19 crisis threatens to undermine the progress that has been made over the last decade. A thematic contribution on external balances at the continental level looks at the differentiated vulnerabilities of African economies in terms of external financing and access to liquidity during the crisis, as well as at their resilience factors. The issue also includes four analyses of African countries: Côte d'Ivoire, Chad, Zambia, and Madagascar. These are accompanied by country focuses on Georgia, Uzbekistan, Sri Lanka, Myanmar, and Ecuador, and by a regional analysis of the impact of the crisis on Overseas France.

Thematic section:

The African external balance shock

Meghann Puloc'h - pulochm@afd.fr

The May 2021 Summit on the Financing of African Economies (SFEA) in Paris highlighted the magnitude of the continent's needs, and in particular its dependence on international financing. The fact is, the COVID-19 crisis has left its mark on the external balances of African countries, creating or exacerbating pressures on foreign currency liquidity and even the external solvency of countries.

On one hand, in the short term, the pandemic has not significantly affected the continent's gross external financing needs (GEFN). These are mainly the result of imbalances in each African country's current trade in goods, services, and capital with the rest of the world. Yet, these current imbalances stabilized in 2020. The fall in imports associated with the economic slowdown and the closure of borders offset the volatility of commodity prices and the collapse of tourism revenues. In addition, countries must honor the amortization of their external debt—that is, the repayment of the principal.[1] This represents 40% of the continent's GEFN. The impact of the additional debt that has been taken on in order to address the consequences of the pandemic will not be visible in the immediate future, given the maturity of the loans granted.

On the other hand, the crisis has dried up the inflow of external financing required to cover these needs: a drop in foreign direct investments (FDI), net outflows of the most volatile capital, prohibitive financing conditions on the international bond markets for some countries that had access to them before the health crisis, and so on. In 2020, African countries could count on the support of the international community, whether multilateral or bilateral donors, to fill the financing gap—that is, the difference between the need and the coverage of that need. After the initial shock, the problem will persist in the years to come insofar as emergency funding—although increased and extended—is not intended to be permanent. This observation has led the international community to make new foreign exchange resources available to all countries.

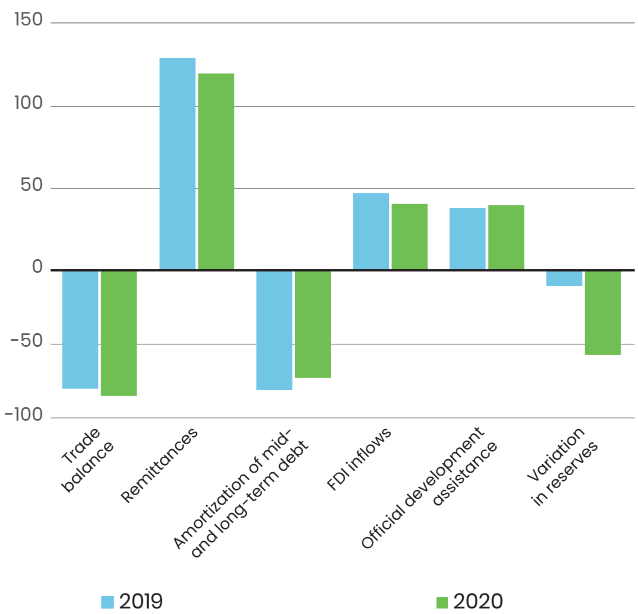
African countries were not evenly equipped to face the shock of the COVID-19 crisis. The pressures on external balances that have been generated or exacerbated by the crisis should be examined in the light of the exposure and vulnerability of African economies to such shocks—that is, according to their capacity to absorb them, particularly through foreign exchange reserves or the adjustment of exchange rates. The economic impact of such a crisis thus depends on these structural characteristics.

1. The African current account in 2020: Zero-sum games

Contrary to the first projections made by the International Monetary Fund (IMF) in the spring of 2020, which were based on an increase in the current account deficit, the pandemic has not had a negative impact on the continent's current account. Sub-Saharan Africa (SSA) recorded a deficit of -3.7% of GDP in 2020, which was stable in relation to 2019. Similar deficits are forecast for 2021 and 2022. In North Africa, the current account balance has remained stable since 2018 (-5.6% of GDP in 2020) and is expected to narrow temporarily in 2021 (-5.2% of GDP), according to the IMF.

The main channels through which the crisis has impacted the trade balance have been exports of goods for commodity-producing countries, and services for tourism countries. With a few exceptions, private remittances showed some resilience in 2020, but there is still some caution around the measurement of these flows and whether they will be sustained in 2021.

Graph 1 - Main African external flows (in USD billion)



Sources: IMF (WEO, AFRREO), World Bank, OECD, UNCTAD

1 Interest payments on external debt are included in the current account.

Africa's extractive sector is recovering quicker than its tourism sector

While oil prices fell by an average of 33% in 2020, the continent's 13 oil-producing countries recorded a drop in export value of 14% on average. Libya (82% drop in crude oil exports value), Nigeria (-44%), Algeria (-36%), and Angola (-33%) were particularly exposed, because the sector generates more than 90% of these countries' total exports. Meanwhile, gold-exporting countries, mainly Sudan and some West African countries (Ghana, Mali, etc.), have benefited from the record prices of precious metals, which are regarded as safe havens. For other metals and minerals, the fall in prices in the first half of 2020, followed by a rebound, had impacts that differed by country (positive for the year in Zambia and Liberia, neutral in Rwanda, and negative in Sierra Leone). The general recovery in prices should brighten the short-term outlook for these countries. A 57% rebound in oil prices is expected for 2021, while base metals (+32% expected for 2021) are benefiting from the Chinese and Western recoveries, and the price of gold remains high (+30% in 2020, +6% in 2021).

The tourism industry ground to a halt as a result of the closure of borders and the lockdowns that have been imposed on populations. This has particularly impacted 17 African tourist destinations, to varying degrees depending on how important this sector is to their economies. Tourist destinations in North Africa, whose economies are relatively diversified, have been moderately exposed, with tourism accounting for less than a quarter of exports in goods and services for Morocco and Egypt, and around 10% for Tunisia (compared to 46% for Ethiopia). Conversely, the vulnerability of small island economies has been underlined once again. The fall in tourism, which generates two-thirds of the foreign exchange earnings of the Seychelles, caused the current account deficit to rise to -29% of GDP in 2020. The successive waves of the pandemic, particularly in the advanced countries that send tourists, will severely limit the sector's recovery in 2021, and that recovery will be very gradual.

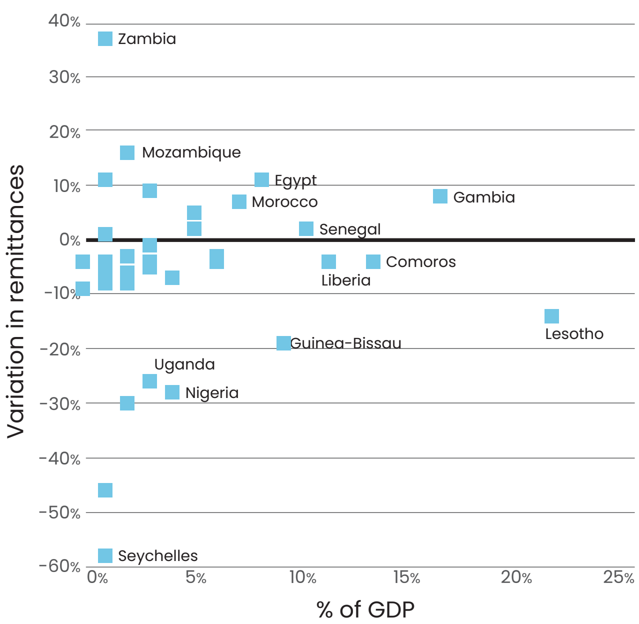
Conversely, a relatively widespread decline in the volume of imports of goods and services across the continent (-5.8% in volume on average in 2020) has limited the deterioration of the trade balance. Several factors contributed to this: the closure of borders in the first half of 2020, lower consumption and investment because of restrictive measures and economic uncertainty, and a reduction in the energy bill of oil-importing countries.

The diaspora: A sustainable support for African economies?

The resilience of remittances has also helped to limit the deterioration of the current account. According to the World Bank (2021d), remittances to Africa amounted to USD 119 billion in 2020 (down 7.4% on the year before), or 4.6% of the GDP of the continent as a whole.

Although Sub-Saharan Africa is the region that has recorded the largest drop in remittances in the world (-12.5% in 2020 to USD 42 billion, as against -1.6% globally), this is explained almost entirely by the fall in remittances to Nigeria (-28%, to USD 17 billion, or 40% of SSA flows), in the context of a substantial gap between the official exchange rate (which was nevertheless devalued by 20% in 2020) and the parallel exchange rate, as well as restrictive measures on the convert-

Graph 2 - Importance of remittances in 2020



Source: World Bank

ibility of remittances into naira. In the rest of SSA, remittances rose by 2.3% in 2020, with particularly strong increases in Zambia (+37%) and Mozambique (+16%). Conversely, remittances to Southern African countries (Lesotho -14%, Botswana -14%, Malawi -13%, Namibia -8%, Eswatini -5%) were affected by South Africa's economic difficulties and the closure of its land borders, with outflows from the country falling by 12% in 2020. It should be noted that these remittances constitute essential foreign exchange inflows for small African economies such as Lesotho (21% of GDP), Gambia (16% of GDP), or the Comoros and Cape Verde (13% of GDP each).

These flows are also relatively important for, and remained resilient in, North Africa. Egypt, the world's fifth-largest recipient of remittances in 2020, recorded an increase in these flows of 11% (USD 30 billion, or 8% of GDP), and thus continued an upward trajectory that began in 2016 with the flexibilization of the exchange rate regime.

The economic recovery in developed countries is expected to support an increase in remittances to the African continent (+2.6% in 2021 and +1.6% in 2022 for SSA, according to the World Bank), with disparities depending on the source of the flows and their sensitivity to the economic situation of the sending countries. In 2020, the resilience of flows to Kenya (+9%) was largely thanks to the resilience of remittances from the United States, which is home to a quarter of the Kenyan diaspora. The strong rebound that is expected in US economic growth (+7.0% in 2021 according to the World Economic Outlook (WEO) of July 2021) is a reassuring factor here. The countries of North and West Africa will have to cope with a more modest recovery in the euro area (+4.6%). The difficulties migrant workers face in gaining employment in the Gulf countries, which were at the bottom of the oil price cycle in 2020, are also something to watch out for.

However, two reservations expressed by the World Bank temper the positive tone of this picture. On the one hand, the closure of borders led to a greater recourse to formal channels and thus to an easier identification of these flows in the balance of payments statistics.[2] It is therefore not impossible that some countries actually experienced a decline in these foreign exchange inflows. On the other hand, the return of some migrant workers to their countries of origin could significantly affect the sustainability of the flows.

2. Amortization of external debt increases the financing need

The amortization of medium- and long-term external debt significantly increases Africa's financing needs: USD 73 billion in 2020 and USD 65 billion in 2021. Three-quarters of these amounts concern developing countries in SSA[3]. Egypt accounts for half of the maturities in North Africa,[4] compared to 29% for Morocco. However, beyond these amounts, the typology of this debt and the nature of the creditors entail rather different methods of managing these maturities, depending on whether we are talking about developing countries that are mainly indebted to official creditors, or about countries that have access to private financing, particularly through the international bond markets.

Debt service relief initiatives: Welcome but not lifesaving

Public or guaranteed debt represents on average 61% of the outstanding obligations of African developing countries over the period from 2020 to 2022. Official creditors, primarily bilateral donors, are the main recipients of these repayment flows (41% of the amortization of public debt in 2020).

However, bilateral debt accounts for only 21% of the long-term external debt service (interest and principal) that was due in 2020 by the 41 African countries eligible for the G20 creditors' Debt Service Suspension Initiative (DSSI) for poor countries over the period from May 2020 to December 2021 (in three tranches). This explains why the DSSI does not significantly reduce their financing needs. It is true that the first postponements of payments had already helped to address the liquidity problems of 24 African countries in December 2020. But, at USD 830 million (plus USD 465 million in the first half of 2021), the debt service that was suspended seemed low in view of a cumulative external debt service for these 24 countries of USD 29 billion.

2 These informal flows were recorded before the onset of the pandemic but were included in the errors and omissions category.

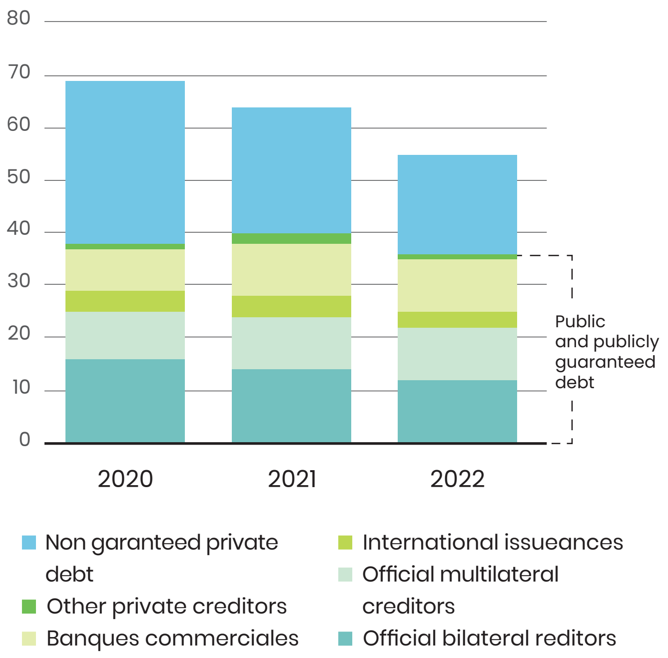
3 This scope corresponds to that of the World Bank's International Debt Statistics (IDS) database. It does not include the following countries from the subregion: Equatorial Guinea, Mauritius, Namibia, the Seychelles, South Sudan.

4 Algeria, Djibouti, Egypt, Morocco, and Tunisia according to the IDS classification.

At the same time, in order to limit the pressure on the balance of payments of the 29 most vulnerable members of the IMF, the latter provided grants for debt relief on debt service payments. Between the onset of the pandemic and the end of May 2021, the Catastrophe Containment and Relief Trust (CCRT) provided USD 603 million in relief to the 23 African countries that were eligible for it.

For countries facing intractable debt situations, the Common Framework for Debt Treatments (G20/PC) should provide a broader response, bringing all creditors to the negotiating table. Chad will be the first country to benefit (see the Chad country focus). Ethiopia and Zambia will follow, at which point there will be the additional challenge of involving Eurobond holders in debt restructuring.

Graph 3 - Breakdown of the amortization of the long-term external debt of African EDCs (in USD billion)



Sources: World Bank (IDS May 2021), EIU
Note: Libya, Equatorial Guinea, Mauritius, Namibia, the Seychelles, and South Sudan are not included

The roll-over of Eurobonds: A major challenge

Across the continent, 21 countries have had access to international bond markets in recent years. According to the Institute of International Finance (IIF 2021), the overall outstanding amount of African Eurobonds reach USD 147 billion in February 2021 (60% of it in SSA). As the largest issuer in Africa, Egypt has an outstanding balance of nearly USD 40 billion, equivalent to 10% of its GDP, including the February 2021 bond issues. The refinancing of USD 35 billion in Eurobonds will be required for the African continent between 2021 and 2025 (including USD 20 billion in 2024–2025). The inherent pitfall of any bond issue is that, when past issues mature, they have to be refinanced, without countries having any control over current market conditions, leading to the risk of an increase in their external debt service. Indeed, future repayments may constitute a considerable burden, absorbing at least 1.8% of GDP in Kenya in 2024, 2% in Ghana in 2023, 2.3% in Angola in 2025, 3% in Rwanda in 2023, and as much as 7.9% in Gabon in 2024 (AFD 2021). Zambia, which already defaulted on a Eurobond coupon payment in November 2020, will have to restructure the equivalent of 16% of its 2020 GDP in bonds that were issued between 2012 and 2015 and that will mature starting next year (see the Zambia country focus).

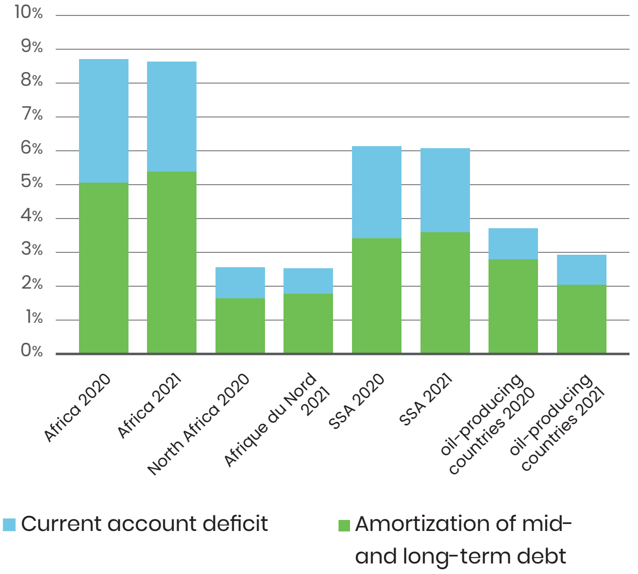
High financing needs in 2021 and 2022

Setting aside short-term debt repayment flows[5], the expected GEFN of African countries comes to more than USD 170 billion per year between 2020 and 2022—that is, annual flows equivalent to an average of 6.8% of continental GDP, of which about 60% is related to current account deficits and 40% to external debt repayments. The magnitude of the GEFN is comparable on both sides of the Sahara, in relation to the GDPs of these two subregions.

Tunisia stands out within North Africa for having a significantly higher GEFN than Egypt (6% of GDP in 2020–2021), Morocco (7% of GDP in 2020), and Algeria (9% of GDP in 2020). The increase in the amortization of external debt (8% of GDP in 2021, as against an average of 6% from 2017 to 2020) brings Tunisia's GEFN to 17% of GDP in 2021 (as against 13% in 2020). It is expected to remain high in the coming years, with a forecast of 14% of GDP on average between 2022 and 2025.

5 Short-term debt accounted for 11% of the total debt stock of low- and middle-income countries in SSA in 2019: USD 68 billion. A broader scope would include in the GEFN the short-term debt contracted in year n-1 and assumed to mature in year n.

Graph 4 - External financing need of the African continent (as a % of GDP)



Sources: IMF (WEO April 2021), World Bank (IDS May 2021), EIU

The GEFN of the oil-producing countries, which was high in 2020 (10% of GDP on average, not counting Mozambique), should benefit from the rebound in prices and come down to 6% of GDP in 2021 and 2022. The scale of the impact of the COVID-19 crisis on economic activity and current account deficits in island countries has increased the weight of their GEFN: +15 percentage points of GDP in 2020 in Cabo Verde (to 18% of GDP in 2020) and +13 percentage points in the Seychelles (to 34% of GDP in 2020).

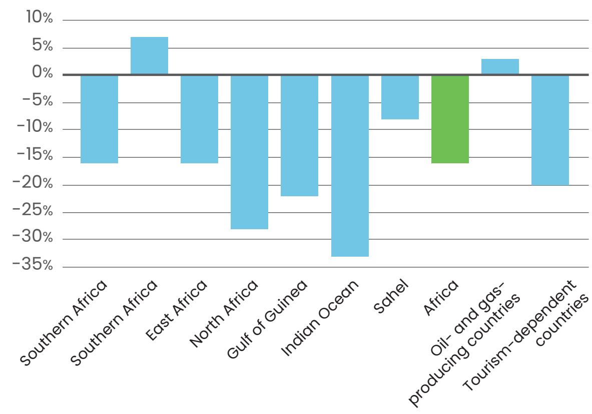
3. The inadequate covering of financing needs

Before the crisis, private capital flows covered two-thirds of the GEFN for SSA. The uncertainties surrounding how dynamic the return of capital to Africa will be, coupled with rising needs, point to a financing gap that the IMF estimated in October 2020 at USD 345 billion between 2020 and 2023 for the continent. Low-income countries with access to the IMF's Poverty Reduction and Growth Facility (PRGF) account for 40% of this amount.

FDI: A source of sustainable financing that still largely eludes the continent

FDI is a privileged source of external financing that has two advantages. Firstly, it constitutes long-term flows that are potentially more resilient to shocks than portfolio flows and other short-term flows. Secondly, it does not generate debt for the recipient countries[6]. In 2020, African countries accounted for 4% of global FDI inflows, which were unevenly distributed across the continent. By virtue of their size, Egypt and South Africa account for a quarter of the inflows into Africa. Having built their economic development partly around financial openness, African island economies, and in particular Mauritius, typically have the highest ratios of FDI flows to GDP in Africa. Some commodity-producing countries also receive large FDI flows in relation to the size of their economies, but these flows remain vulnerable to fluctuations in commodity prices or even to a deterioration in the security or business environment. Mozambique has been the most prominent illustration of this since the discovery of the twelfth-largest gas reserves in the world, with net flows of around 25% of GDP on average since 2011 (17% of GDP in 2020), which have financed large current account deficits related to capital goods imports. That being said, on average, net FDI flows represented only 2% of SSA's GDP over the last decade.

Graph 5 - Change in net FDI flows in 2020



Source: UNCTAD

6 Unless through intra-group financing between foreign parent companies and local subsidiaries.

In 2020, according to the United Nations Conference on Trade and Development (UNCTAD 2021), global FDI flows contracted by 35%—to a level 20% lower than that recorded during the 2008–2009 financial crisis—and are expected to reach a low point in 2021. Although this drop primarily concerns developed countries (-58%), African countries nevertheless recorded a 16% contraction in inflows (to USD 40 billion), twice as high as the average for EDCs.

The 35% contraction of net investments in Egypt (USD 6 billion in 2020) brought in its wake the contraction of net investments in North Africa as a whole (-28%). Only Morocco maintained its capital inflows (+3%), thanks to the diversity of its investment sectors. FDI flows to SSA were more resilient (-12%), despite the 39% drop in investment in South Africa. In contrast to the general trend, some countries recorded an increase in investments, often associated with the energy sector. This is notably the case in Senegal (+39% against -8% in the Sahel), the Democratic Republic of the Congo (+19%), and Mozambique (+6%), while disinvestments (repatriation of capital that has been invested for several years in the context of weak growth in the oil and non-oil sectors) have slowed in Angola.

UNCTAD warns that the number of new projects in Africa has fallen by 62% (compared to an average of -42% for EDCs), in particular for large infrastructure projects (-74%), which does not bode well for investment flows in the coming years. UNCTAD nevertheless forecasts a slight rebound of 5% in FDI on the continent in 2021, driven by the extractive sector. According to the IMF (2021c), after slowing down to +1.3% of GDP in 2020, net FDI flows to SSA should recover to +1.7% of GDP in 2021.

Successful first returnsto international markets, but a high risk of refinancing

After the initial shock of the crisis, some African countries were able to re-enter the international bond markets. In the first half of 2020, the sharp increase in spreads made sovereign issuance prohibitive before market conditions eased.

The USD 5.9 billion in (gross) issuance by SSA countries in 2020 represents a 70% drop from the number in 2019 (World Bank 2021a). Only Gabon (1 billion) and Ghana (3 billion) had managed to finance themselves on the markets before the crisis broke. Since then, Côte d'Ivoire (see country focus),Benin, Ghana, Kenya, and South Africa have been among the SSA countries that have carried out successful issues. In particular, in January 2021, Benin completed a USD 300 million, 31-year bond issue—a record maturity for the country—at a rate of 6.875%. Issuance volumes in SSA are expected to recover this year, and could reach USD 15 billion according to the IMF (2021c).

The situation in North Africa is mixed. Unlike Egypt and Morocco, which have already managed to issue bonds after the crisis and are expected to return to the markets in 2021 and 2022, Tunisia has found itself in a more delicate position, given concerns about the sustainability of its external public debt. As two Eurobond issues of USD 500 million each matured this summer, the country had to draw on foreign exchange reserves pending IMF financing.

This option remains costly for African economies: issues with maturities of between 10 and 15 years made between 2018 and 2020 had a coupon of over 7.5% on average (AFD 2021). In 2021, although spreads are tending to return to pre-crisis levels, they are still high, despite a favorable global interest rate and liquidity environment, reflecting the markets' appreciation of risk. Zambia's and Ethiopia's astronomical spreads are the exception to the rule: their debt restructurings under the G20 Common Framework should lead to the restructuring of their Eurobond issuances.

Emerging economies in Africa have not been spared by the wave of capital outflows

Africa has few developed financial centers. These domestic markets (bonds and equities) allow emerging African countries to attract capital thanks to high rates of return that contrast with a low-rate global environment. They have benefited greatly from the high global liquidity of recent years. But this capital is highly volatile and does not stand up well to crises. In 2020, African financial markets did not escape portfolio investment (PI) outflows. In Egypt, portfolio outflows in the second quarter of 2020 (amounting to more than USD 15 billion from March to May) put pressure on the balance of payments, but economic stability in the second half of the year and high real returns helped reverse the trend. Nigeria recorded net outflows of PIs over the year (USD -3.6 billion, of which 90% was associated with the bond market). In Angola, capital outflows represented 8.6% of GDP.

The stakes are all the higher for countries whose short-term capital flows are a significant way of meeting their GEFN. South Africa is particularly vulnerable to changes in investor confidence. Its GEFN is high (4% of GDP in 2020, but over 15% of GDP including short-term debt) and 43% of it was covered by portfolio flows between 2016 and 2019. Since the beginning of the pandemic, net capital outflows have reached about 4.6% of GDP.

Beyond emergency financing, official creditors will be called upon to contribute

For the least developed countries that have difficulty attracting FDI and that lack access to international capital markets, the main source of external financing is concessional debt from donors. In response to the crisis, donors responded strongly, so that, at the global level, official development assistance (ODA) reached unprecedented levels in 2020. According to the first estimates by the OECD (April 2021), net bilateral ODA[7] to Africa stood at USD 39 billion in 2020 (of which 80% went to SSA), an increase of 4% in real terms compared to 2019.

In the context of the COVID-19 crisis, the continent benefited greatly from IMF support in the form of exceptional financing to ease pressure on the balance of payments. By the end of May 2021, the fund had provided USD 28.8 billion in financial assistance to Africa, two-thirds of which went to SSA. The continent thus accounts for nearly two-thirds of the financing disbursed by the IMF since the start of the COVID-19 crisis. It is expected that the IMF's emergency financing will be replaced by a new wave of agreements on programs that are themselves expected to catalyze financing from other multilateral and bilateral donors. It is anticipated that this financing will amount to USD 4 to 5 billion in 2021 (IMF 2021c). At the same time, the World Bank's cumulative support mechanisms in response to the pandemic represent an overall package of USD 160 billion made available to developing countries up until June 2021. The 19th replenishment of the World Bank's International Development Association (IDA) concessional window is expected to provide USD 53 billion to Africa (out of a total commitment of USD 82 billion) between July 2020 and June 2023.

4. Drawing on foreign exchange reserves to buffer adverse external shocks

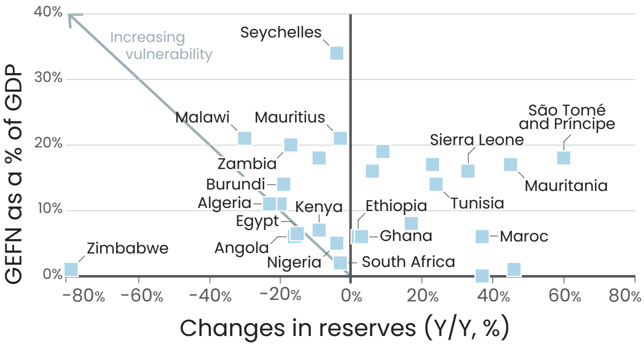
The capacity of African countries to absorb the external balance shock is uneven.

It depends primarily on the size of the GEFN. The higher it is, the more financing is needed—preferably stable, long-term financing. Any decline in this financing then exposes the country to a contraction in the availability of foreign exchange. And countries are all the more vulnerable if their level of foreign exchange reserves is insufficient to face this shock.

Many African countries were forced to draw on their foreign exchange reserves to make up the financing gap in 2020, so that reserves held by SSA countries (minus gold) fell by USD 16.9 billion (IMF 2021c). In North Africa, the pandemic has amplified a pre-crisis contraction in reserves, to the tune of USD -34.4 billion in 2020, a loss equivalent to 16% of 2019 reserves. Economies that depend on tourism (-16% in Egypt, -9% in Cape Verde) and some oil-producing countries (-31% in Libya, -23% in Algeria, -17% in Angola) recorded significant declines, even as they came into the crisis with reserves already affected by the 2014 price collapse. Conversely, lower import bills and financing from the international community significantly strengthened the external liquidity of around ten countries (+23% in Rwanda, +37% in Morocco, +46% in the Comoros). However, this increase in foreign exchange reserves can be deceptive, since it generates debt and/or is associated with a temporary drop in domestic demand. Moreover, a replenishment of reserves does not mean that the reserves in question are adequate. In Tunisia, a net accumulation of reserves that began in 2019 (+21% in 2020), and that was enabled by the appreciation of the exchange rate and the support of donors, has brought reserves to a historically high level, which is nevertheless still insufficient to cover all of the country's short-term obligations.

7 Based on cash flow basis, not grant equivalent basis, to allow for historical comparison.

Graph 6 - External balances of African countries in 2020



Sources: IMF (IFS, WEO), World Bank (IDS)

Reserves must also be assessed according to the type of exchange rate regime:

for the same level of reserves, the shock-absorption capacity is less strong for a country with a fixed exchange rate regime than for a country with a floating one. In this respect, the absorption of the shock by currency depreciations (-33% for the Zambian kwacha, -27% for the Angolan kwanza, -16% for the Ethiopian birr) made it possible to preserve some of these countries' reserves. On the other hand, Nigeria, which has a relatively moderate GEFN (5% of GDP in 2020), has a relatively fragile external liquidity position. Supported by disbursements from donors and restrictive remittance and convertibility measures, foreign exchange reserves declined by only 4% in 2020, remaining at an adequate level of 5.2 months of goods and services imports forecast for 2021. However, reserves are expected to decline by 2023, depending in part on the flexibility of the exchange rate regime.

The question of foreign currency liquidity will remain a major concern in the years to come.

According to IMF projections (IMF 2021b), the contraction of reserves is expected to continue at a slower pace in North Africa (USD -3.5 billion in 2021 and USD -7 billion in 2022), and even recover in Egypt. Reserves would tend, rather, to stagnate in SSA (USD +458 million USD in 2021, and USD -689 million in 2022).

As for the main African monetary unions, whose member countries pool their reserves, the West African Economic and Monetary Union (WAEMU) maintained an adequate level of liquidity at the end of 2020, in line with IMF recommendations (5.4 months of goods and services imports forecast for 2021). On the other hand, the foreign exchange reserves of the countries of the Central African Economic and Monetary Community (CEMAC) have suffered from the cumulative effect of the fall in oil prices since 2014 and then of the health crisis, as the oil sector accounts for two-thirds of the zone's total exports. They are not expected to reach the target of 5 months of imports before 2025.

What are SDRs?

The special drawing right (SDR) is an international reserve asset created in 1969 by the IMF to supplement the official foreign exchange reserves of its member countries. Its value is based on a basket of five reference currencies (since 2016: USD, EUR, GBP, JPY, and CNY) against which SDRs can be exchanged. To date, SDR 204 billion (about USD 293 billion) has been allocated to member countries. In response to the additional financing needs caused by the COVID-19 crisis, a new allocation of SDR 456 billion, equivalent to USD 650 billion, was announced. This amount is well above the SDR 183 billion allocated in 2009 during the global financial crisis.

These amounts are allocated in proportion to the countries' quota shares, which are determined by their relative position in the world economy. A member country's quota share determines the amount of financial assistance it can get from the IMF. The G7 members will receive the equivalent of USD 283 billion under this new SDR allocation, and all high-income countries are allocated USD 438 billion. These countries will be able to voluntarily channel their allocations to a new "Resilience and Sustainability Trust". It is expected that these additional resources will be directed primarily to the 69 low-income countries that are eligible for the Poverty Reduction and Growth Trust, including 38 countries in sub-Saharan Africa.

Sources: IMF, UNDP

The general SDR allocation agreed in the summer of 2021 is a welcome source of additional financing for the continent's foreign exchange liquidity (USD 33 billion, or 5% of the allocation). The top six African recipients, namely South Africa, Nigeria, Egypt, Algeria, Libya, and the Democratic Republic of the Congo, account for half of these amounts. The 29 African low-income countries (LICs) would receive only USD 8.5 billion, just over a quarter of the funds that would go to Africa. These amounts appear insufficient in view of the needs, particularly when it comes to honoring the external debt service of the most vulnerable countries, as the United Nations Development Programme (UNDP 2021) points out. This may require a new push for international solidarity.

The problem of liquidity and short-term external refinancing makes the major structural challenge facing Africa all the more pressing and complex: that of financing (the return to) dynamic and sustainable growth in order to accelerate the continent's development and economic convergence. Beyond the necessary extension of health and economic measures, this colossal undertaking requires vast investments that would cost USD 425 billion overall for SSA between 2021 and 2025, including USD 245 billion for low-income countries (IMF 2020).

To achieve this, Africa will have to increase its attractiveness to private investors (FDI) if it is to limit its use of debt. The deteriorating trend in the debt situation of African states (AFD 2021) is already making access to financing more difficult, whether in terms of access to the market or to support from the international community. This is the conundrum that the continent will have to solve in the next decade.

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Country focus

Côte d'Ivoire
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Côte d'ivoire: a relatively resilient economy

Emmanuelle Monat—mansartmonate@afd.fr

Côte d'Ivoire avoided a recession in 2020, despite the health crisis and a busy election year. Recovery is expected in 2021, but it will be important to quickly resume the process of fiscal consolidation needed in order to maintain a sustainable debt ratio while the country pursues its reform agenda, which aims to foster a sustainable and more inclusive economic recovery.

Described as "Francophone West Africa's economic hub" by the World Bank,[8] in 2011 Côte d'Ivoire was aiming for economic emergence by 2020. Political tensions and difficulties in implementing reforms have led to a less ambitious reformulation of this objective: the "path to emergence."[9] The country's positive economic momentum was interrupted by the COVID-19 crisis, thus highlighting the development challenges it faces.

Sociopolitical and macroeconomic stabilization since 2012

Since the 1980s, Côte d'Ivoire has had a chaotic growth regime that has depended on cocoa exports and been disrupted by episodes of pronounced violence during election periods. Between 1980 and 2010, real GDP per capita was cut in half. The return to stability since 2012 has led to stronger growth, averaging 8%, supported by a recovery in household consumption and public investment, while the diversification of the services sector has improved the resilience of economic activity to the fall in cocoa prices.

After reaching the completion point under the Highly Indebted Poor Countries (HIPC) Initiative in 2012, Côte d'Ivoire benefited from debt cancellations, which led to a significant reduction in its debt ratio (33% of GDP in 2012 compared to 50% in 2011). This created new fiscal space that allowed the authorities to implement a major public investment program. While implementation of the budget was constrained in 2017 and 2018 by the fall in cocoa prices (15% of tax revenues), the budget deficit has since narrowed to below the 3% of GDP mark set as a target by the West African Economic and Monetary Union (WAEMU).

A recession-free 2020 despite the health crisis and a chaotic presidential election

Côte d'Ivoire avoided recession in 2020 despite the COVID-19 crisis, recording a 2.3% GDP growth. This strong performance can be put down to the resilience of the agricultural sector, the economic support programs introduced by both the Central Bank of West African States (BCEAO) and the government, and a lower dependence on tourism and remittances than in comparable countries such as Senegal or Benin.

The re-election of the incumbent president Alassane Ouattara for a third term in October 2020 reignited political tensions, but the resumption of dialog with opposition parties allowed the March 2021 legislative elections to proceed peacefully. The ruling party won a majority, suggesting a continuity of economic policy and a relaxation of tensions in the political environment. As things clear up in the aftermath of the election, the challenge for the government will be to set in motion a process of reconciliation in order to avoid a resurgence of tensions and to allow for robust economic growth.

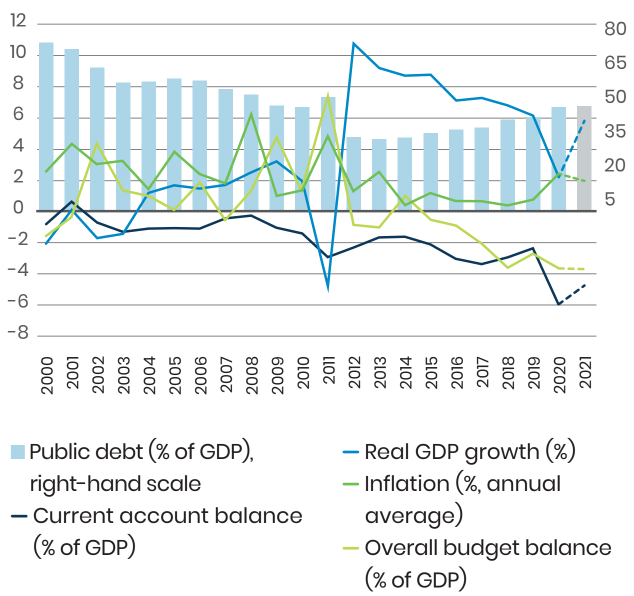
8 https://www.worldbank.org/en/country/cotedivoire/overview.

9 https://www.lepoint.fr/afrique/la-cote-d-ivoire-a-l-heure-du-bilan-economique-26-10-2020-2398049_3826.php.

A rebound expected in 2021 and a fiscal consolidation to be relaunched...

Economic growth is expected to rebound to 6% in 2021, driven by a combination of a recovery in exports and domestic demand, supported by public investment. A minor fiscal consolidation is expected from 2021. After -5.9% of GDP in 2020, the budget deficit is forecasted to be 4.6% of GDP this year, in particular due to the lifting of the suspensions of taxes that were put in place during the crisis. Its financing should be facilitated by the issuance of Eurobonds on the international markets, with two new issues in November 2020 and February 2021 for EUR 1 billion and 850 million, respectively, at historically low rates of 4.8% and 4.3% (10-year maturities). The country also participates in the DSSI (0.4% and 0.1% of GDP in 2020 and 2021, respectively), and it would like to negotiate a new IMF program. Although public debt is on the rise again (45.7% of GDP in 2020), as is the average cost of debt because of Eurobond issued at market rates, public debt remains sustainable. The average maturity of external public debt has been extended from 10.4 years in 2015 to 14.4 years in 2020, and the peg to the euro limits the foreign exchange risk associated with foreign currency debt, which is mainly in euros. The country faces a moderate risk of debt distress, even though its capacity to absorb shocks has been reduced by the crisis, according to the IMF's Debt Sustainability Analysis (DSA) of December 2020.

Graph 7 - Main macroeconomic aggregates



Source: IMF (WEO April 2021)

... but uncertainties remain about the medium-term macroeconomic outlook

The expected rebound in 2021 is conditional on a recovery in exports, which are largely based on cocoa and oil, which account for 39% and 10% of export earnings, respectively. The current account deficit grew in 2020 to 3.6% of GDP, but it is expected to stabilize in 2021. The GEFN will be met this year thanks to financing on international markets, as illustrated by the recent Eurobond issues. But uncertainties remain in the medium term, as access to international markets remains dependent on investors appetite and could be impacted by any new global financial shock that would undermine Côte d'Ivoire's attractiveness. At the same time, the availability of international donors financing, which played an important role in 2020 in meeting the GEFN, may be more limited. Financing in the WAEMU regional market will also be more complex, as other countries in the zone also have high public financing needs.

Furthermore, following the deterioration of public finances in 2020, fiscal consolidation could be complicated by (i) the social context, which has been weakened by the health crisis and the elections; (ii) the increased reliance on public investment to sustain growth; and (iii) the low level of public revenues, which have stagnated at around 13% of GDP for the last two decades. To reduce the deficit, the government is counting on a recovery in budgetary revenues, which is contingent on the recovery of economic activity as well as on tax reforms.

Moreover, while the banking sector seems to have weathered the crisis well, the risk that contingent liabilities will materialize in state-owned enterprises will need monitoring, especially with the lifting of the moratorium on bank debt repayments that was introduced during the crisis. The ability of the economy to remain on a solid growth path (potential growth estimated at 6.5%) will be closely linked to the reform agenda and to sustainable poverty reduction. The various workstreams will be highlighted in the new National Development Plan 2021–2025, which aims to make economic growth more inclusive.

Chad: The challenges of political transition and the success of the common framework

Laura Marie—mariel@afd.fr

The sudden death of President Idriss Déby in April 2021 has caused a major disruption to the functioning of the country, which is facing a significant debt issue. Chad will be the first country to benefit from the Common Framework for Debt Treatments (G20/Paris Club), whose negotiations with bilateral creditors are progressing rapidly, while those with Glencore, the country's main private creditor, seem to be more delicate. The forthcoming signing of a new IMF program and the peaceful resolution of the political and security situation in the country and the region will be crucial to Chad's medium-term economic prospects.

A landlocked country in Central Africa and a major player in the G5 Sahel, Chad is facing a double security and public-debt crisis, with deep macro- and socioeconomic imbalances and high vulnerability to climate hazards. Since its independence in 1960, the country has experienced a series of conflicts (war against rebel movements and against Libya, and interethnic conflicts), which have greatly slowed its development: it ranks 187th on the Human Development Index (HDI) with a GDP per capita of USD 654, 42% of the population live below the poverty line, and it is the seventh-most fragile state in the world, according to the Fragile States Index. The fall in oil prices from 2014 to 2016 and again in 2020 revealed the deep vulnerabilities of the Chadian growth model, characterized by a mono-export economy, a glaring governance deficit, and a profound lock-in of the regime by former president Idriss Déby, who had been in power for three decades.

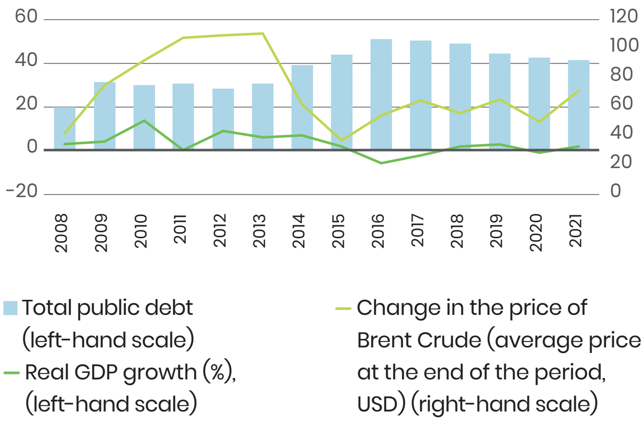
An unexpected political transition for this key player in political cooperation within the G5 Sahel framework

Idriss Déby, who had just won the April 2021 presidential election, earning him his sixth term, was killed during clashes with the rebel political-military group Front for Change and Concord in Chad (FACT), which was threatening the capital N'Djamena. A transitional military council headed by his son, Mahamat I. Déby, immediately took the reins of power, suspended the Constitution, and dissolved the legislative bodies. This government has committed itself to holding "free and democratic" elections at the end of a renewable 18-month transition period. The Chadian army, the most powerful and most active in the region, is the key local player in the fight against terrorism. Combined with the death of Idriss Déby, true pillar of the Chadian army's cohesion, constitutes a source of uncertainty regarding the stability of the country and the region.

An economic model dependent on oil

The discovery of oil deposits in 2003 and the sharp rise in oil prices fueled the growth of the Chadian economy up to 2014 (8.5% average growth over the period). In 2019, oil production represented 80% of exports, 20% of GDP, and 35% of public revenues. This dependence on oil, for both fiscal sustainability and external solvency, constitutes a major vulnerability in the absence of diversification of the production model and of countercyclical mechanisms. On the other hand, the state has taken a predominant place in the country's economy, stifling the development of the private sector, which is also hampered by extensive corruption (Chad ranks 160th on Transparency International's Corruption Perceptions Index) and by the extremely poor quality of infrastructures. Public investment is low (5.3% of GDP before the COVID-19 crisis). The pandemic and major floods in August 2020 caused the Chadian economy to contract by -0.9%. It should rebound moderately in 2021, to +1.7%, according to the IMF.

Graph 8 - Increase in debt against a backdrop of weak growth since 2014



Sources: World Bank (Brent), IMF (WEO)

A country "in debt distress"

Despite some progress under the Extended Credit Facility (ECF) program agreed with the IMF in 2017, and a budget surplus that had recovered as of 2018 (+1.8%), Chad suffers from a very narrow tax base, which constrains spending on social protection and public investmenst: from 2017 to 2020, non-oil revenues accounted for only 7% of GDP (15.7% oil included). Public-sector debt was 48.9% of GDP in 2020, to which is added the equivalent of 9.5% of GDP in contingent liabilities (Société Nationale d'Électricité and Société Nationale de Ciment). Public debt is mostly external (USD 3 billion, or 25.3% of GDP). This debt is held by multilateral donors on concessional terms (37% of the total) and by private creditors (also 37%), mainly Glencore, with the remainder held by bilateral donors (26%).

In the absence of access to international capital markets, in 2014 the Chadian government took out a USD 1.4 billion loan (8.6% of GDP) from Glencore, the company that is exploiting the country's oil resources. Falling oil prices in the period from 2014 to 2016 led to the accumulation of external arrears (~1% of GDP) and an inability to service debt to Glencore, resulting in two debt restructurings, in 2015 and 2018. The decline in oil prices in 2020 put further pressure on the country's liquidity, which was temporarily relieved by the participation of Chad's bilateral creditors in the DSSI. From 2021 to 2024, 69% of the debt service will be owed to Glencore.

Despite the continued rise in Brent crude oil prices since the end of 2020 and the size of the public gross financing needs (PGFN), which amount to about 10% of GDP per year on average between 2021 and 2026, Chad is "in debt distress," according to the IMF. The country thus became the first beneficiary of the Common Framework for Debt Treatment and will be granted, in parallel, a new ECF. Nevertheless, Glencore's active participation will be decisive: the effort of bilateral donors alone would be insufficient to put Chad's public debt on a sustainable path (USD 852 million has to be restructured over the period from 2021 to 2028).

Finally, the banking sector continues to bear the scars of the exogenous shock of 2014–2016 and of the government's massive accumulation of domestic arrears. The sector suffers from a lack of liquidity, deteriorating balance sheets, and a lack of depth: total assets represent only 27% of GDP. Moreover, the banking sector's exposure to sovereign risk has increased: the holding of sovereign assets by domestic and regional banks has risen (12% of non-oil GDP), the profitability of banks has declined, and their refinancing with the Bank of Central African States (BEAC) has been made more difficult by the deterioration of collateral.

Zambia: Economic recovery on hold until debt restructuring

Meghann Puloc'h—pulochm@afd.fr

In November 2020, Zambia became the first country to default on its sovereign debt since the COVID-19 crisis began. In reality, the pandemic has only exacerbated macroeconomic imbalances that were already evident before the onset of the health crisis, in the form of low economic growth, high foreign currency liquidity pressures, and unsustainable public debt.

A landlocked country in Southern Africa, Zambia has built its development model on abundant mineral resources, which have made it Africa's second-largest copper producer and one of the world's top ten. This exploitation, in the upswing of the cycle, has contributed significantly to improving the standard of living among the population, despite strong demographic pressure (+3% per year on average over a very long period). Conversely, price collapses have had a direct negative impact on growth and external balances. While the veracity of the images of the dry Victoria Falls that went viral in December 2019 may have been questioned, the drying up of foreign exchange reserves is undeniable. But the disruption of the extractive sector alone does not explain the economic difficulties of recent years.

Dependence on copper, a source of volatility

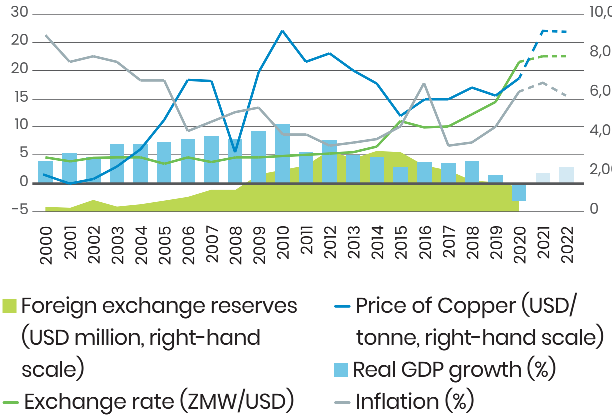
Mining still generates 70% of Zambia's export earnings and 10% of its GDP. As a result, although the Zambian economy is now largely based on the tertiary sector, it remains vulnerable to fluctuations in global prices. Between 2015 and 2019, their volatility accentuated the country's economic difficulties, with growth averaging +3.1%, compared to +5.7% between 2011 and 2014.

After sluggish growth in GDP in 2019 (+1.4%) as a result of low copper production, power cuts, and drought, Zambia recorded a 3.0% recession in 2020. The recovery in copper prices that began in the second half of the year partially offset the impact of the pandemic. Record price levels are helping to restore the country's external balances. The current account balance, which was in deficit between 2013 and 2018 (-1.3% of GDP on average), is expected to be in surplus in 2020 and 2021 (+1.5% and +6.5% of GDP, respectively).

In the short term, prices are expected to remain at a high level against a backdrop of strong demand from the Chinese market, the recovery of the manufacturing industry in OECD countries, and production difficulties in Chile, the world's leading exporter of copper. In the medium term, investment in green forms of energy, which consume a lot of copper, should support prices. To take full advantage of this dynamic, the country will have to remove the obstacles that are holding back its production and foreign investment (the supply of electricity and water, and the business environment). While net FDI flows stood at an average of 5% of GDP between 2013 and 2018, Zambia recorded net capital outflows in 2019, with -0.6% of GDP for FDI and -0.2% for PIs, and small net inflows in 2020 (+0.5% and +0.9% of GDP, respectively).

However, the dynamism of the mining sector will remain insufficient to allow a significant rebound of the economy: the forecast is +1.8%, according to the World Bank (June 2021).

Graph 9 - A rebound in copper prices that is insufficient for a recovery in growth



Sources: IMF (IFS, WEO), World Bank, Macrobond, Oxford Economics

From fiscal imbalances to default

With the slowdown in growth, public finances have become strained. Expenditures have increased and then been maintained at a high level, despite stable revenues, thus generating large public deficits: -7.6% of GDP on average between 2013 and 2019, and -14% of GDP in 2020. At the same time, the state has accumulated significant internal payment arrears (9% of GDP at the end of March 2020). Financing difficulties initially forced the authorities to concentrate spending on wage bill (41% of revenue in 2019) and interest payments on debt (a quarter of revenue).

The rise in external public debt service is being exacerbated by the depreciation of the kwacha (-52% cumulatively against the USD in 2018–2020), while these payments contributed to the erosion of the country's foreign exchange reserves to the point where these became insufficient to meet external commitments (USD 1.2 billion at the end of 2020, compared to USD 3 billion at the end of 2015). In 2020, the amounts to be repaid reached USD 1.1 billion, an increase of 19% year on year, and the moratorium secured in August 2020 from the Paris Club (PC), worth as much as USD 165 million, did not significantly reduce the burden. With the sharp rise in sovereign spreads—already very high—ruling out any refinancing on the international markets, the country defaulted on USD 42.5 million in interest payments on a Eurobond issuance in November 2020, and has since been accumulating external arrears.

Zambia's public debt has risen sharply over the decade (120% of GDP in 2020, as against 21% in 2011), and its composition is unfavorable (two-thirds of it is in foreign currencies and it is mostly on market terms). Returning to a sustainable path will be complex, as the USD 3 billion in Eurobonds issued between 2012 and 2015—an amount equivalent to 16% of 2020 GDP—mature as early as next year, with a first repayment of USD 750 million. For the time being, negotiations are proving difficult with Eurobond holders (a quarter of external debt) and tricky with China (a third of external debt), and Zambia has requested debt treatment under the G20 Common Framework. This restructuring is a prerequisite for any financial support from the IMF.

Difficult access to financing for the private sector

The depreciation of the kwacha and the 46% increase in the money supply in 2020, coupled with domestic financing of the public deficit, fueled inflation (above 20% in the first half of 2021), which had already been well above the 6–8% target since mid-2019. The Bank of Zambia has been forced to end the accommodative monetary policy that was designed to support the economy (-350 base points in 2020) by raising its key rate by 50 base points in February 2021 to 8.5%.

The slowdown in economic activity and the accumulation by the state of domestic arrears have tended to deteriorate the quality of bank assets. The economic shock associated with the COVID-19 crisis has increased pressure on banks and limited their financing capacity. The country may not have defaulted on its domestic debt, but commercial banks are exposed to sovereign risk, as they hold more than two-thirds of the country's treasury bills.

The government's recourse to domestic financing (+37% of credits in 2020) is crowding-out credit to the private sector (+8.5%) and keeps rates for borrowing from commercial banks at high levels (6% in real terms in 2020, compared with 16% in 2019). These deleterious effects slow down local private investment, which is essential for a sustainable revival of economic growth.

Madagascar: Deep-rooted fragilities

Cécile Duquesnay - duquesnayc@afd.fr

The human and economic impact of the COVID-19 crisis in Madagascar has been severe, undermining recent improvements in growth and development. Disbursements from the Rapid Credit Facility (RCF) in 2020 have helped to fill short-term financing gaps and to catalyze budget support from donors, which has become more critical than ever. The challenges for the future are the development of a fiscal policy strategy and continued efforts at transparency, the idea being to create a fiscal space to ensure an adequate level of social spending to meet the country's considerable needs.

Since its independence, Madagascar's trajectory has been marked by a spectacular monetary impoverishment. It is one of only eight countries whose real per-capita income is lower today than it was in 1960[10] and the only one of these countries not to have been affected by armed conflicts or wars during this period. With a nominal GDP per capita of just over USD 500 in 2020, and with three-quarters of the population living on less than USD 1.90 per day at purchasing power parity, Madagascar is the tenth-poorest country in the world.

Recurrent major crises alternating with periods of insufficient growth

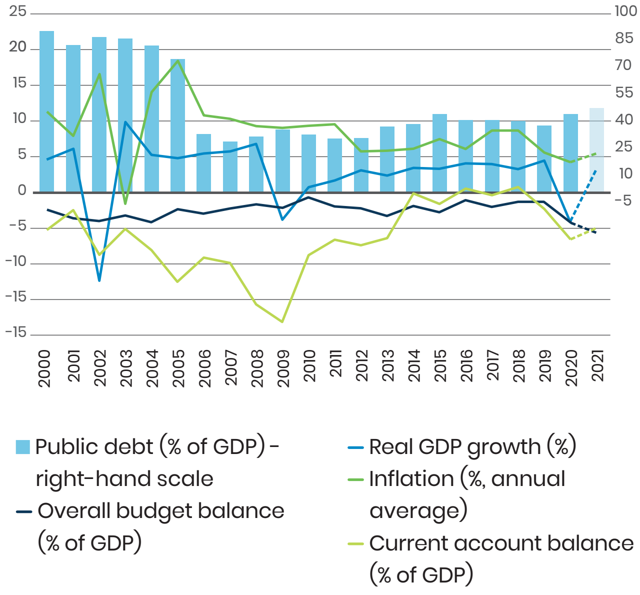
Because of the island's exposure to natural disasters and political instability, Madagascar's economic growth has remained weak and volatile in recent decades, marked by recurrent sharp contractions in GDP. The average annual growth rate (AAGR) was less than 2% between 1980 and 2016. With an average of three cyclones per year and several episodes of drought and flooding, Madagascar is among the countries most affected by extreme weather events in Africa. It is estimated that natural disasters and other exogenous shocks cost the economy about 1% of GDP per year on average.

From 2016, growth accelerated at an average rate of 4.3% per year, driven by the mining sector (one-fifth of growth in the period from 2015 to 2018). At the end of 2018, after three decades of successive political crises, Madagascar experienced a democratic and peaceful political transition with the return to power of Andry Rajoelina. This new stability has reinforced the rebound in growth and, above all, the re-engagement of the international community.

But the COVID-19 pandemic has hit Madagascar hard, reversing recent gains in per-capita income and poverty reduction, with job losses in key manufacturing and service sectors, as well as income losses for informal workers who have been affected by the lockdowns in large cities. GDP contracted by 4.2% in 2020, down from +4.4% in 2019. The global slowdown has affected tourism, manufacturing, and textile exports, although exports from free-trade areas have shown some resilience. A rebound of 3.2% is expected in 2021, but there remain significant uncertainties around the exit from the crisis. Supported by public and private investments and the recovery of exports, growth should recover and accelerate in the medium term (+5% by 2026 according to the IMF).

10 Per-capita income in 2019 was 56% of its 1971 level, in constant (2010) dollars.

Graph 10 - Main macroeconomic aggregates



Source: IMF (WEO April 2021)

Vital support from donors in the short term...

The sharp decline in tourism revenues (-81%) and exports of goods (-27%) caused the current account deficit, excluding grants, to grow in 2020 (-9.6% of GDP compared to -5.3% in 2019). The two IMF RCF disbursements in 2020 (USD 338 million, or 2.4% of GDP) helped to bridge short-term financing gaps, supported COVID-19-related crisis-mitigation measures, and helped catalyze budget support from donors. A new 40-month ECF arrangement with the IMF worth USD 312 million (1% of GDP) was agreed in April 2021. Exports are expected to recover gradually, as are imports. That would allow the current account deficit (including grants) to drop to -5% of GDP in 2021, as against -6.5% in 2020.

As a result of multiple disbursements and delays in government spending, foreign currency reserves reached 5.9 months of imports in early 2021, thus exceeding the traditional three-month threshold, as well as the IMF's Assessing Reserve Adequacy (ARA) upper limit of 5.7 months for economies whose credit is constrained. Total external debt increased to 73.3% of GDP in 2020 (an increase of eight percentage points).

...but reducing fiscal risks remains essential for long-term growth

Before the COVID-19 crisis, Madagascar's debt situation was under control, with a stable debt level and a budget deficit that had been contained (respectively 38.4% and -1.4% of GDP in 2019). The health crisis and the ensuing drop in public revenues[11] have resulted in an increase in the budget deficit (-4.2% of GDP in 2020) and in the level of public debt (43.6% of GDP). According to IMF estimates, debt could reach about 49% of GDP in 2025, but the DSA of March 2021 still assesses Madagascar at moderate risk of external and overall public debt distress, with some space to absorb shocks.

However, efficiency in public spending suffers from a long tradition of porosity between the management of state-owned enterprises and that of the state budget, resulting in significant transfers, which have amounted to nearly 20% of public spending over the last five years. The reduction of these transfers is one of the objectives of the new IMF program. In particular, the financial difficulties of Jiro sy Rano Malagasy (JIRAMA), the state-owned water and electricity company (estimated debt of 2.1% of GDP), Air Madagascar (estimated debt of 0.4% of GDP), and other state-owned enterprises (estimated debt of 2.3% of GDP) point to significant risks that contingent liabilities will materialize. For JIRAMA, the authorities have committed to clearly identifying the amount of transfers for 2021 in the revised budget law and to taking corrective measures to ensure that the total amount of these transfers remains limited. For Air Madagascar, a business plan is being prepared by external auditors to assess the short-term financial viability of the group and to define a medium-term recovery plan. The authorities have pledged to avoid any further public financing until the plan is finalized.

11 At just 13.5% of GDP in 2019, they fell to 10.9%, one of the lowest levels in the world, as a result of the crisis.

Overseas France: Economic impacts contained, at the cost of greater imbalances

Bertrand Savoye—savoyeb@afd.fr

Until recently, the economies of the Overseas France had been less affected by the first lockdown than was metropolitan France. With the exception of Martinique, they also escaped the second lockdown that was imposed on metropolitan France at the end of 2020. However, the public health situation is evolving fast. Economic conditions remain uncertain and a complete assessment will only be possible once the impact of both the particularly strong ongoing epidemic wave and the end of business support schemes are known.

When the COVID-19 health crisis struck the overseas territories of France, it encountered very different socioeconomic contexts depending on the territory. While the growth rate in overseas territories has been the same as in metropolitan France since 2015 (around 1.5% per year in volume), this moderate average growth in fact conceals sharply contrasting situations. While Mayotte enjoyed much faster growth than metropolitan France, New Caledonia and Martinique experienced virtual stagnation.

As the activity- and employment-support measures taken in the Overseas Departments and Regions (DROMs) are the same as those taken in metropolitan France, while those taken in the Overseas Collectivities (COMs) and the *sui generis* Collectivity of New Caledonia are broadly similar, the economic shock of the first wave of the pandemic is essentially linked to three factors:

- the sectoral orientation of economies, with some sectors being sheltered from the effects of the crisis while others have been particularly exposed (air transport, hotels and restaurants, and so on). In overseas territories, this sectoral orientation has generally had a much more protective effect than in metropolitan France, thanks to the much greater size of the general government sector (except in New Caledonia). This factor largely explains the lower decrease in activity in the DROMs during the lockdown (-18% in Mayotte, -20% in the French West Indies, -25% in French Guiana, and -28% in Réunion) compared to metropolitan France (-33%);

- the specific circumstances of each territory, in particular its remoteness. Thus, in a relatively homogeneous sector such as construction and public works, the drop in activity ranges from -25% in Guadeloupe to -90% in Mayotte (compared with -79% in metropolitan France);

- the duration of local lockdowns, as determined by the spread of the virus. This duration was shorter in the Pacific territories (27 days in New Caledonia and 40 days in French Polynesia) than in metropolitan France and the DROMs (55 days).

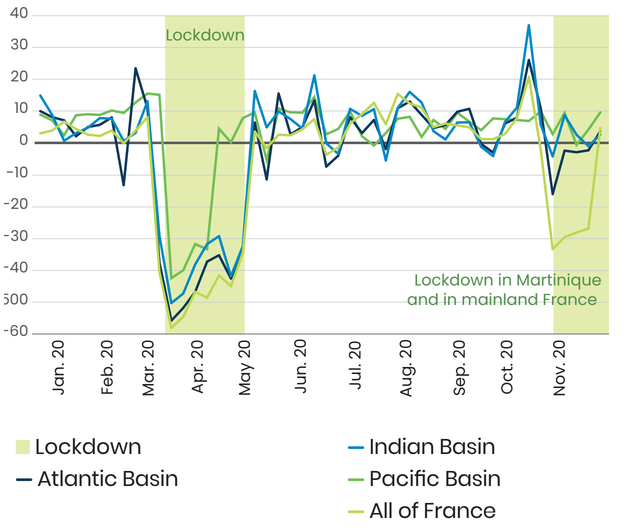
In the end, if we consider the whole period over which the first lockdown was imposed, its impact can be estimated, *stricto sensu*, at around 3 percentage points of annual GDP in the French West Indies, Mayotte, and New Caledonia, 4 points in French Guiana, Réunion, and French Polynesia, and 5 points in metropolitan France.

From the second half of 2020 onward, the comparative analysis of the impacts of the health crisis between the different overseas territories and metropolitan France is more difficult to carry out due to the disparity between the new lockdowns imposed in response to the successive waves of the pandemic.

In the fourth quarter of 2020, only metropolitan France and Martinique imposed a new lockdown, from the end of October to mid-December, although other territories did impose curfews. The effect of this second lockdown can be seen in the banking transactions trends (see chart): while all the territories experienced a marked decline during the first lockdown and then a clear recovery in the third quarter, only metropolitan France and Martinique experienced a further decline at the end of the year.

In the first half of 2021, the situation in terms of policies implemented to control the pandemic was even more varied. Metropolitan France and most of the Overseas France were forced to impose new lockdowns, but with timetables and measures specific to each territory.

Graph 11 - Bank transactions
(in % relative to 2019)



Year-on-year change (%) in the weekly amount of CB bank card transactions in 2020 compared to the corresponding week in 2019.

Source: CB bank cards

While the health toll was more positive in June 2021 in overseas territories than in mainland France in terms of the number of deaths per capita, conditions have, since then, taken a sharp turn for the worse in a number of territories. The available statistics do not yet allow us to assess the economic toll. As in the first wave, the economic impact is expected to be less marked than in mainland France, for the same reasons: more favorable sectoral orientations and shorter lockdowns.

However, other factors may come into play and affect, in particular, how long it takes for activities to resume following each lockdown.

Thus, the early estimate of economic activity in 2020 produced in French Polynesia as part of the Comptes économiques rapides pour l'Outre-mer (CEROM, Rapid Economic Accounts for Overseas France) project calls for caution. While the loss of annual GDP percentage points during the first lockdown was less than in mainland France (-3.7 points as against -5 points), and while French Polynesia did not have a second lockdown in 2020, the drop in GDP in 2020 was higher than in France (-10% as against -9%). This pronounced drop in activity, which extended over the four quarters of the year, can be explained by the fall in tourism, in other export sectors, and in transport, which was impacted, as it was in New Caledonia, by measures to control entry into the territory.

On the other hand, it can be assumed that the drop in activity over the course of 2020 and the first half of 2021 was less pronounced overall in Réunion than it was in mainland France, because Réunion's economy does not depend that much on tourism and has a relatively significant network of companies focused on the domestic market. But in the other overseas territories, the extent of the economic impact compared to what has been observed in mainland France is still partly unclear.

In the second half of 2021, most of the economies of Overseas France are at risk of being strongly impacted by the new epidemic wave resulting from the spread of the Delta variant and which led to the implementation of a new temporary lockdown in Guadeloupe, Martinique and parts of French Polynesia. The full impact of this crisis can be assessed only after the epidemic is under control and when we are able to observe the consequences of the withdrawal of support measures for economic activity and employment, both in mainland France and in overseas territories.

Government intervention has thus far made it possible, to contain the economic impacts of the crisis and, in particular, to limit corporate insolvency. However, this action is further accentuating the imbalances in the overseas economies:[12] the relative weight of the administrative sector and of remittances from mainland France will increase, and the foreign trade deficit will grow.

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12 In the first half of 2021, the number of corporate insolvencies has decreased, cumulatively for one year, in both the overseas territories and mainland France by -23% and -40% respectively.

Georgia: A country at a crossroads

Maxime Terrieux - terrieuxm@afd.fr

Despite having a relatively robust institutional and macroeconomic framework, Georgia approached the COVID-19 crisis aware of its fragility in the face of such an external shock. The health and economic response of the authorities has been adequate, although the financial support of donors, which had always been forthcoming in Georgia's short history, was still necessary. To turn the corner after three decades of progress, Georgia must now remove the structural locks on its economy, while ensuring that it preserves some of the institutional fundamentals that have contributed to its development.

"Our foreign policy is European and Euro-Atlantic integration." This sentence from Bidzina Ivanishvili, the current strongman of Georgia and the founding oligarch of Georgian Dream (GD), which has been the ruling party since 2012, could have been attributed to his predecessors on all sides. It reflects a strong consensus in Georgian society regarding the pro-Western aspirations of this small country in the South Caucasus, which has made openness a key element of its development for three decades.

Openness, democracy, liberalism, and remarkable structural transformations

Georgia has experienced several political upheavals since its independence in 1991, in particular the Civil War of 1991–1994, the Rose Revolution in 2003, and the war against Russia in the summer of 2008. Despite this turbulent context, Georgia has managed to build the relatively robust institutions that are necessary for the establishment of a democracy. At the same time, and more particularly since the mid-2000s, it has put in place a liberal economic framework, thanks to numerous reforms that have created a favorable climate for business and foreign investment. Democracy and a liberal economic system are the two pillars of a country that has openly displayed its Western aspirations since the 1990s and has thus continuously benefited from foreign aid, catalyzed by numerous IMF programs since 1994. This combination of domestic progress and external assistance has enabled Georgia to make significant progress over the last three decades.

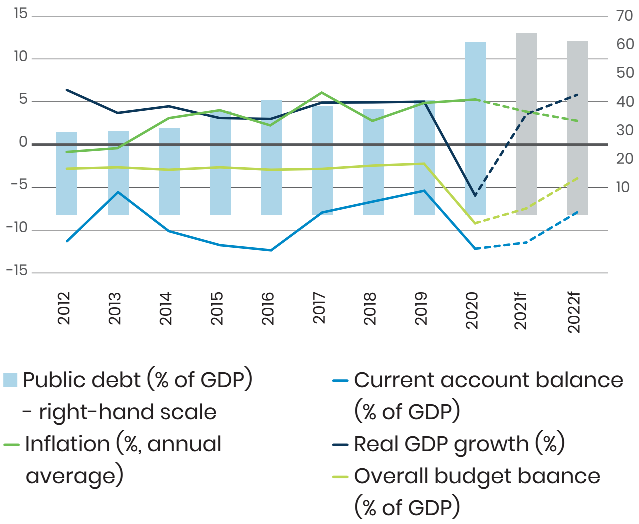
A small and very open economy, Georgia has enjoyed solid growth, averaging 6% in the 2000s. Major reforms (liberalization, institutional reforms, anti-corruption, tax reform) have made the country one of the most attractive investment destinations in the world in just a few years: the country was ranked seventh in the Ease of Doing Business index in 2020. The economy is now tertiary, with more than two-thirds of the value-added being produced by services, driven in particular by trade and tourism. Growth continued in the 2010s, though at a slower pace than in the preceding decade: the AAGR was 4.8%, very close to potential growth (5%). It is notable that the country's progress has been consistently supported by successive IMF programs, and this has paved the way for the recurrent involvement of other donors such as the World Bank and the European Bank for Reconstruction and Development (EBRD).

This progress allowed Georgia, which had been a low-income country (LIC) in the early 2000s, to move two steps up and become an upper-middle-income country (UMIC) in 2019. The extreme poverty rate (threshold of USD 1.90/day at purchasing power parity) has fallen from 19.2% of the population in 2000 to 3.6% in 2019, thanks in particular to this economic progress and the social policies in place.

Inspired by EU rules (maximum fiscal deficit of -3% of GDP, debt capped at 60% of GDP), the framework for the management of public finances is robust. The public deficit thus averaged -2.8% of GDP in the period from 2011 to 2019, while public debt, which is sustainable, remained below 45% of GDP at the end of 2019.

The financial system, dominated by two banks (Bank of Georgia and TBC Bank), is generally sound, with high capitalization and profitability, as well as high-quality assets. Although it is well regulated, the system remains too dollarized. The central bank's monetary policy is generally effective, particularly at controlling inflation.

Graph 12 - Main macroeconomic aggregates



Source : FMI (WEO April 2021; EFF 8th review, April 2021)

A model facing its own limitations

Georgia's external position is its main source of vulnerability, regularly putting its foreign exchange reserves under pressure. Having opted for openness, the economy is exposed to the international economic situation, particularly that of its neighbors (Russia in particular), and its GEFN is structurally very high: more than 30% of GDP, linked to a current account deficit that is regularly close to -10% of GDP and to an external debt that reached 104% of GDP at the end of 2020. The COVID-19 crisis has exacerbated these fragilities, in particular through the collapse of tourism (-83% in 2020), which accounted for 30% of foreign exchange inflows in 2019. To reduce pressure on the balance of payments, Georgia continued to benefit from donor support in 2020, which fully covered its external financing gap of USD 1.2 billion. Foreign exchange reserves, equal to 5.2 months of imports as at December 2020, are not threatened at this stage, but the crisis is a reminder of how dependent the country still is on external aid.

In addition, despite real progress, the Georgian growth model is struggling to find new growth drives, suffering in particular from deficiencies in its infrastructure and its education system. Reforms are in progress to address this, but they may be slowed by the health crisis. In 2020, the recession reached -6.1%, and the rebound in 2021 is expected to be rather timid, with an expected growth in GDP of 3.5%.

Moreover, the influence of Russian foreign policy, and more generally of the external context, is inseparable from internal political life. Today, the geopolitical risks linked to the tensions with the two separatist regions in Georgia (South Ossetia and Abkhazia) and with neighboring Russia remain significant. At the same time, under the ruling government, democracy does not seem to have been strengthened (the judicial system remains fragile, and corruption, electoral fraud, and a lack of transparency persist) and may even have suffered setbacks. The legislative elections at the end of 2020, which were deemed fraudulent by the opposition, the imprisonment of the main leader of the opposition, and the resignation of the prime minister, thus reflect a form of chronic political instability. This could be fueled in the coming months by the concomitant rise in unemployment and poverty (+0.5 and +2.8 percentage points, respectively, in 2020) in the wake of the COVID-19 crisis.

Lastly, public finances will have to be monitored: public debt, nearly 80% of which is denominated in foreign currency, remains very vulnerable to a depreciation of the lari. The crisis and the fall in the lari (-12.5% against the USD) pushed up the public debt ratio by 20 percentage points in 2020, to 60% of GDP. The debt also remains vulnerable to the contingent liabilities of state-owned enterprises (15% of GDP). Despite this, in April 2021, Georgia easily refinanced its single USD 500 million Eurobond issue on attractive terms (2.750% at five years).

Uzbekistan: A new frontier market

Sylvain Bellefontaine—bellefontaines@afd.fr

Relatively sound macroeconomic fundamentals before the onset of the COVID-19 crisis, combined with government measures and financial support from donors, allowed Uzbekistan to withstand the shock and avoid recession in 2020. The country is rapidly changing: the authorities embarked on a formal post-Soviet transition starting in only 2017, and are pursuing the transformation from a planned to a market economy. The challenges for the coming years are to avoid overheating and to find the right pace at which to open up and reform in order to ensure socioeconomic development without causing major macroeconomic imbalances and while controlling the spiral of external debt.

Samarkand, crossroad of cultures: this proclamation by UNESCO in 2001 makes sense in view of the thousands-year-old history of the city, in the heart of Eurasia. But it has a certain irony for the contemporary observer of an economy that was until very recently quasi-autarkic. The opportunities and pitfalls of the ongoing transition are likely to have a profound influence on Uzbekistan's medium- to long-term trajectory.

An opening up that is a source of optimism and opportunity…

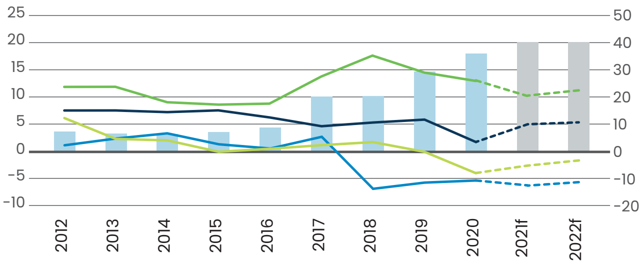
The coming to power of Shavkat Mirziyoyev in late 2016 marked a shift toward an open foreign policy and a less authoritarian domestic policy. President Mirziyoyev, who is fairly popular, is preparing to run for re-election in October 2021. This will be the first major test of democracy after Islam Karimov's years in power, from 1989 to 2016. The goal of more than doubling GDP per capita to USD 4,000 (the UMIC threshold) by 2030 is ambitious but achievable.

Without denying its historical ties with Russia and its commercial ties with China—the main trading partner of Uzbekistan, which stands to benefit from the Belt and Road Initiative—, the objective of courting Western investment could support the reform program. Under the aegis of donors (the IMF, the World Bank, and the Asian Development Bank), who provide financial support and technical assistance, the reforms are aimed primarily at improving governance and transparency, as well as at economic and financial liberalization.

GDP growth has been dynamic over the last 15 years, with an AAGR of +7.1%. The loss of momentum in income from commodity exports (especially gold, natural gas, and cotton) in connection with the end of the super-cycle (2003–2014) has been offset by the acceleration of public investment since 2017 (investment stands at 40% of GDP). Countercyclical fiscal and monetary measures, the country's control over the spread of the virus, and the rise in gold prices have cushioned the shock of the COVID-19 crisis, with a GDP growth rate of +1.6% in 2020, supported by agriculture and the construction boom. The rebound is expected to reach +5% in 2021 in the prices of sustained notably by the upward trend in the rates of commodity exports..

In the medium term, potential growth could exceed in the prices of IMF projections (+5.5% by 2026), assuming strong capital accumulation (public investment and FDI) and successful integration into world trade. This will require developing a competitive industrial export base around the country's comparative advantages, such as its mining and textile industries, and even tourism.

Graph 13 - Main macroeconomic aggregates



Source: IMF (WEO and Fiscal Monitor, April 2021)

... but that also involves risks

As a result of demographic pressure and the insufficient creation of formal jobs (45% of jobs are in the public sector), emigration has been a social valve and an economic driver (remittances were equivalent to 7% of GDP on average in the period from 2014 to 2020). But the socioeconomic impacts of the massive return of the diaspora (~1.1 million people in 2020, out of 2 million who had settled in Russia) in connection with the COVID-19 crisis will have to be monitored should it turn out that these migration flows are irreversible.

Despite the public savings cushion, which is equivalent to a quarter of GDP through the Fund for Reconstruction and Development (FRD), the surge in public debt, which quadrupled in the space of four years to 38% of GDP in 2020, must be controlled. Public debt (including State guarantees), which is mostly external, remains sustainable but suffered even before the COVID-19 crisis from a significant exchange rate effect since 2017, following the partial flexibilization of the exchange rate regime. The public deficit, which the IMF estimates was -4.4% of GDP in 2020, has been capped at -5.5% of GDP in the 2021 Finance Act, against a backdrop of continued efforts in terms of social spending, health spending, and support for households and businesses. The government aims to reduce the deficit to -2% of GDP and to establish a medium-term fiscal framework. It has also committed itself to reducing its off-budget spending, in particular loans to state-owned enterprises (4% of GDP).

Pending fiscal consolidation, short-term liquidity risk remains contained. The country has applied for emergency financing from the IMF (the Rapid Financing Instrument (RFI) and the Rapid Credit Facility (RCF)) but not from the G20/Paris Club's DSSI. The GPFN is expected to remain moderate in the coming years. However, its coverage by recourse to donors and international markets, with a second Eurobond issued in November 2020, will have to be complemented by recourse to the shallow and expensive local market.

The crucial development of the local bond market and the fall in domestic interest rates will depend on the ability of the central bank to curb inflationary pressures (15% year on year on average since 2017 for a target rate of 5% by 2023), fueled by the credit boom (which has to be monitored), the depreciation of the so'm (70% against the USD since 2017, of which 10% in 2020), and the liberalization of some controlled prices. The transmission channels of monetary policy on the economy via the banking sector remains ineffective, with 58% of credit being at controlled rates and 57% in foreign currency. Dominated by public banks, which hold 86% of assets, the banking sector maintained satisfactory balance sheet ratios in 2020, and a privatization plan is under consideration.

The country's ability to diversify a competitive export base in order to 1) avoid the pitfalls of a strong appreciation of the real effective exchange rate through the Balassa-Samuelson effect or Dutch disease, 2) anticipate the low-carbon energy transition, and 3) attract foreign investors (net FDI: 2.1% of GDP since 2014, -26% in 2020) will be essential to preserving the sustainability of the balance of payments in the medium term. While commodity prices are trending upward, the end of the super-cycle in 2014 and rising imports following gradual trade liberalization have eroded the current account surplus (-6.1% of GDP on average in the period from 2018 to 2020).

The amount of external debt increased by 38% in 2020 to reach 58% of GDP, but the GEFN is expected to remain manageable in the medium term, even with a current account deficit of around 5% of GDP. Uzbekistan is still a net foreign creditor (+34% of GDP at the end of 2020), notably through the assets of the FRD, and the level of foreign exchange reserves is comfortable (equivalent to more than 8 months of imports).

Sri Lanka: Exacerbated structural vulnerabilities

Jules Porte—portej@afd.fr

Sri Lanka entered the COVID-19 crisis with a slowing economy and deteriorating public finances, and these vulnerabilities were exacerbated in 2020. The extent of the economic growth rebound in 2021 remains uncertain at this stage. The sustainability of public finances is now at risk, while the country's solvency could be jeopardized by the impossibility of resorting to international markets and by weak and declining foreign exchange reserves.

Sri Lanka has made considerable progress in terms of social indicators. In particular, the percentage of the country's population living in poverty has declined from 23% in 2002 to 4% in 2016 at the national poverty line. The growth model, which is based on specialization in sectors such as tea and textiles, is nevertheless struggling to move toward value-added activities such as tourism, logistics, and business services.

Stiffening of power and economic slowdown

The stability that Sri Lanka has enjoyed since the end of the armed conflict in 2009 has been threatened to some degree in recent years. Indeed, a serious political crisis in 2018 led to an institutional deadlock that lasted for several months. In 2019, attacks targeting hotels and churches raised fears of renewed inter-religious tensions and led to a decline in tourism. That same year, Gotabaya Rajapaksa (Sri Lanka Podujana Peramuna - SLPP) was elected president and appointed his brother, Mahinda Rajapakṣa, as prime minister. In August 2020, the SLPP won the parliamentary elections, leaving the opposition divided and flailing. The adoption of the twentieth amendment to the Constitution by Parliament in October 2020 has resulted in a concentration of power in the hands of the president, while significantly reducing that of the prime minister and Parliament and paving the way for the politicization of many institutions.

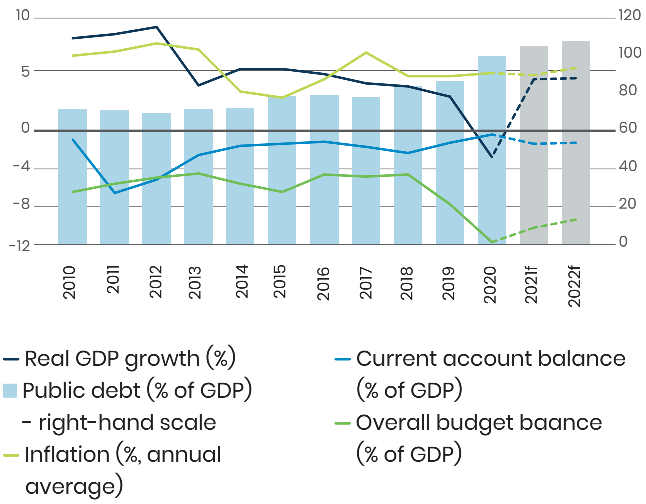
At the same time, the pace of economic growth has slowed. While GDP growth rate was above 8% in the period from 2010 to 2012, supported by post-conflict reconstruction, it started to slow down in 2013. This slowdown has become more pronounced in recent years as a result of internal and external shocks. Thus, in 2018, the growth rate stood at 3.3%, dropping to 2.3% in 2019. The fallout from the COVID-19 crisis, including border closures, a halt in the tourism sector, and a slowdown in world trade, led to a recession of 3.6% in 2020. The extent of the rebound in 2021, which the IMF expects to be 4%, remains uncertain at this point because of a strong wave of COVID-19 that has been hitting the country since April, the turbulence suffered by neighboring India, and uncertainty about the recovery of global tourism.

From unsustainable public finances to insolvency?

The Sri Lankan economy is heavily burdened by an imbalance in public finances, and this has led to a structurally high fiscal deficit that has averaged 6.7% of GDP over the last decade. Low public revenues, at around 12% of GDP, and the burden of interest on the public debt, at around 7% of GDP, are weighing on the budget and limiting the resources available for social spending and investment. The public deficit rose to 11.9% of GDP in 2020 and is expected to remain high in the coming years. As a result, the public debt increased significantly from 86.9% to 100.1% of GDP between 2019 and 2020. The high risk of debt distress highlighted by the IMF's DSA in 2019, particularly if the large public deficit is not absorbed or if growth does not accelerate, is therefore more acute today.

The matter of the sustainability of public finances will be complicated, in 2021 and in the years that follow, by increased pressure on the country's solvency. While the current account deficit narrowed in 2020 to 1.4% of GDP, mainly because of the contraction of domestic demand, it is expected to rise again in 2021, while external debt repayments will remain high (6% of GDP). As a result, the GEFN is expected to increase in 2021 to USD 7 billion (about 8% of GDP) and remain at that level until 2023. However, the GEFN is not covered by the structurally weak capital inflows, and foreign exchange reserves are dwindling. These reserves

Graph 14 - Main macroeconomic aggregates



Source: IMF (WEO April 2021)

amounted to only USD 3.6 billion at the end of May 2021, or about 2 months of goods and services imports. The room for maneuver is therefore particularly narrow: the country has not had access to international markets since the beginning of 2020 because of excessively high spreads, and all the rating agencies now give the country a CCC rating. The support of China, with which Sri Lanka signed a USD 1.5 billion swap agreement in March 2021, therefore appears to be decisive, while discussions with the IMF seem to be blocked by the authorities' reluctance and by doubts about the sustainability of Sri Lanka's public finances.

Domestic financing of public debt poses new risks

In response to the COVID-19 crisis, the Central Bank of Sri Lanka lowered the main policy rate four times, for a total of 200 base points, and it is now at an all-time low of 5.5%. At the same time, since it is excluded from international markets, the country was forced to resort to internal debt to finance itself, through purchases of securities by the central bank on the primary market and by commercial banks. The combination of a strong need for financing coming from the public sector and a low-interest-rate environment led to less financing for the private sector, a phenomenon reinforced by the slowdown in economic activity.

As a result, commercial banks' lending to the public sector jumped by 51.2% for the government and by 22.5% for state-owned enterprises. By contrast, the growth in credit to the private sector slowed to +6.4% in 2020. The public sector thus accounted for 80% of the credit granted by the banking sector in 2020. The money supply grew by 13 percentage points of GDP in 2020, a rise that corresponds to the increase that took place between 2012 and 2019.

New risks are thus emerging. On the one hand, the rapid increase in the money supply could have an inflationary effect and contribute to the depreciation of the Sri Lankan rupee, thus automatically increasing the foreign currency debt burden and worsening sovereign risk. On the other hand, the massive financing of the public sector by the banks could, if it continues, generate a crowding-out effect to the detriment of the private sector and hinder Sri Lanka's potential economic growth in the medium term.

Myanmar: A catching-up process stalled by the health and political crises

Marion Hémar—hemarm@afd.fr

The military coup of February 1, 2021, put an end to the democratic transition that had been underway for more than five years. The population remains mobilized, with many public and private services being hit by strikes. The proliferation of acts of repression poses a particularly high risk of sociopolitical destabilization in the short term. Economic activity had been buoyant over the preceding decade, but it slowed dramatically in 2020 and is expected to contract significantly in 2021. Myanmar's ability to implement policies to support the economy and act as a social buffer is limited, given its fiscal and institutional weaknesses. Thus, the health and political crises are already causing a deterioration in the living conditions of the population, a quarter of whom live below the national poverty line.

Since gaining independence from the United Kingdom in 1948, Myanmar has undergone a succession of military dictatorships, resulting in an autarkic withdrawal of the country and a privileged relationship with China based on a security-business diptych. After more than half a century of isolation, in March 2016 Myanmar underwent a democratic transition with the installation of a civilian government controlled by the National League for Democracy (NLD) and led de facto by Aung San Suu Kyi. The November 2020 parliamentary elections had consolidated the NLD's power, but the military seized power in February 2021 and declared a year-long state of emergency. Aung San Suu Kyi and other Burmese leaders were arrested. Demonstrations denouncing the coup have been brutally repressed by the junta, and this has left several hundred people dead since February. The central state's relations with minorities remain conflictual, and the prospects for improvement seem slim in the current context.

Over the last decade, the opening up of the country has allowed sustained growth, which came to an abrupt halt with the COVID-19 crisis and the coup d'état

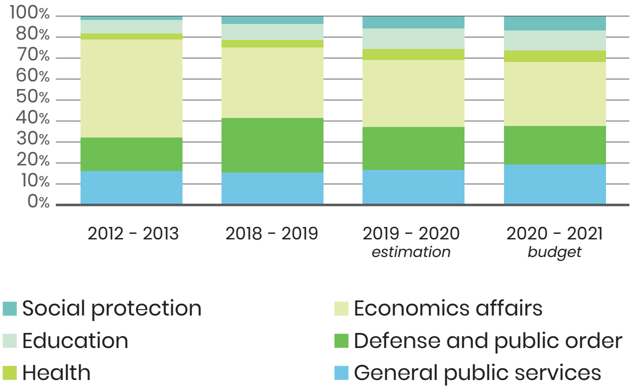
After a decade of crisis in the 1980s that lasted until 1991, Myanmar entered a period of sustained growth from 1992 to 2007 (membership of ASEAN in 1997, and the creation ex nihilo of the capital, Nay Pyi Taw). The social crisis of 2007 and Cyclone Nargis in 2008, which struck one of the countries most exposed to climate change, broke this momentum and led the regime to embark on a gradual process of economic opening up that resulted in a steady acceleration of the growth rate to a high point of 8.2% in 2014. The economy of Myanmar is marked by a certain opacity, resulting both from the involvement of the military in various sectors and from the need to bring institutions up to standard. It has been going through fundamental reforms since 2010 and has opened up considerably, even if its economic relations are primarily with other Asian countries, allowing it to achieve an AAGR of close to 7% between 2011 and 2019. In 2020, it was 3.2%, against the backdrop of the health crisis, which led to declines in exports, tourism, and remittances, as well as to a contraction in domestic demand. In 2021, there could be a sharp reversal in economic growth (-8.9% according to the IMF, -10% according to the World Bank, and -20% according to Fitch) with the recent rise of COVID-19 cases in the country and the sociopolitical turbulence following the coup.

Poor fiscal depth and political turmoil limit social and countercyclical policies

The structure of public revenues has changed significantly in recent years with the rise in tax revenues (7% of GDP since FY2015,[13] as against 3% of GDP in FY2010), which, nevertheless, is still among the lowest in the world. In terms of

13 The Burmese fiscal year runs from October 1 to September 30.

Graph 15 - Changes in budgetary expenditure (%)



Source: RCF/RFI January 2021

(the "Economic affairs" item includes infrastructure spending and SOE operations).

budgetary expenditure, the proportion related to social expenditure is low and is not increasing much in relation to the population's needs. On the other hand, in a region marked by strong geostrategic competition among countries, defense spending is particularly high: it accounted for 29% of total spending in FY2019, which is more than double the combined budgetary spending on education and health.

The budget deficit has been growing for the past five years and reached 6% of GDP in FY2020. Against the backdrop of the global health crisis, it is estimated that the budget deficit will be 6.4% of GDP in FY2021.

Its political and economic opening up helped the country benefit from the restructuring or cancellation of part of its external public debt, and that in turn allowed it to reduce its level of public debt in foreign currency from 40% of GDP in 2008 to less than 15% of GDP in 2014. In FY2020, public debt remained under control at 38.2% of GDP. Monetary financing by the central bank amounted to 3.6% of foreign exchange reserves, with the IMF recommending a maximum of 5%. The domestic financing of the fiscal deficit resulted in two-thirds of the public debt being denominated in local currency in FY2020. As the deficit increases, total public debt could rise to 42.9% of GDP in FY2021.

The external sector remains vulnerable

Given the country's recent opening up, the current account balance is structurally in deficit, but it has been narrowing in recent years (to 2.6% of GDP in FY2019). The current account deficit is financed primarily by FDI flows (down sharply in FY2020 to 2.5% of GDP from 5.8% in FY2016), mainly from countries in the region (infrastructure and energy production projects, and mining). The country's economic relations are largely with other Asian countries: more than half of its trade is with China and Thailand. The IMF estimates that there was a slight widening of the deficit (to -3.5% of GDP) in FY2020 due to the decline in tourism revenues. Foreign exchange reserves increased in 2020 to USD 6.7 billion (from USD 5.7 billion at the end of 2019), or 4.7 months of goods and services imports, with the IMF considering the appropriate level to be between 5 and 6 months. The GEFN is expected to be USD 4.3 billion in FY2021 (about 5.1% of GDP). The financing gap (1.1% of GDP) is expected to be filled in part through debt service relief through the DSSI at the end of 2020 (0.4% of GDP) and through IMF financing (RFI and RCF) of USD 357 million in January 2021 (0.4% of GDP). The country will have to rely more on international donors or draw on its reserves to plug the remaining financing gap. Given the sociopolitical context, gaining access to funding from Western donors may prove difficult.

Ecuador: A narrow path out of the crisis

Benoît Jonveaux—jonveauxb@afd.fr

While the selective default announced by Ecuador in the spring of 2020 was resolved through a successful restructuring of its external public debt with its private creditors, the country's main macroeconomic challenges persist. They have to do in particular with the large-scale fiscal adjustments needed to stabilize public debt and preserve external balances, and with the development of a new growth model. The room for maneuver available to the team of President Guillermo Lasso, who was elected in April 2021, is very narrow, however, as both the international community and private creditors already made a substantial effort in 2020 to support the country.

Recovering the drivers of economic growth

Ecuador experienced a relatively high growth rate (3.9% between 2000 and 2010, then 5.5% until 2014), driven by rising oil prices (the country has produced an average of 515,000 barrels per day since the early 2000s) and by an increase in the contribution of the public sector to growth. The oil shock that struck in 2015 strongly impacted the economy because of limited countercyclical economic policy options (no autonomous monetary policy, and constrained fiscal means). The fiscal adjustment carried out from 2017 onward also had an impact on activity, and the average growth rate from 2015 to 2019 was under 0.5%. As a result of the COVID-19 crisis, the country went through a 7.5% recession in 2020, and the IMF does not foresee a recovery higher than 2% in 2021.

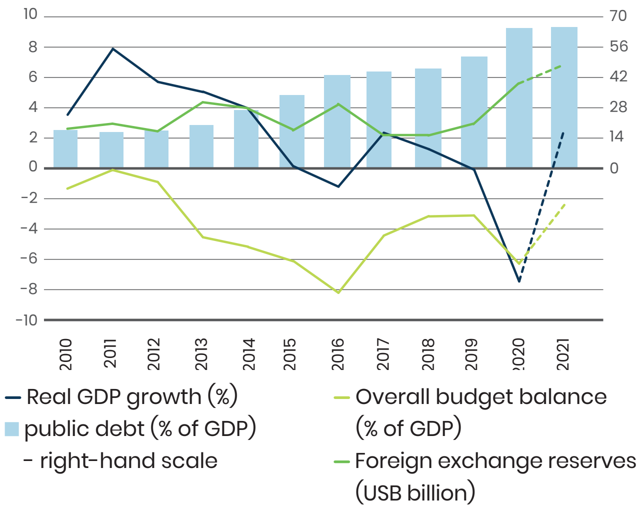
One of President Lasso's priorities is to support activity through the development of the private sector and the revitalization of the oil sector. He will have to deal with a poorly diversified and unproductive private sector and with considerable structural rigidities. Above all, the new administration will also have to conduct a fiscal adjustment, which it intends to do by cutting spending, even though the economy as a whole depends heavily on public spending.

Ensuring the sustainability of public finances

The last decade has been marked by a deterioration in public finances. The overall budget balance has been continuously in deficit since 2009. This is the paradoxical consequence of rising oil revenues (which led to an more than proportional increase in current spending and investment under the Correa administration) until 2014 and then a decline in oil prices from 2014 to 2017. The fiscal consolidation initiated by the Moreno administration from 2017 was interrupted by the COVID-19 crisis and the new drop in oil prices, with the result that the public deficit rose to 6.3% of GDP in 2020.

These developments brought about an increase in public debt from 17.7% of GDP in 2010 to 64.6% of GDP in 2020. The debt was increasingly financed over the period from 2014 to 2017 by the central bank, putting pressure on foreign exchange reserves, which had already been weakened by the decline in oil prices. Recourse to international

Graph 16 - Main macroeconomic aggregates



Source: IMF (WEO April 2021; IFS)

markets has also intensified, and the share of public debt held by private foreign creditors rose from 9% in 2010 to 37% in 2019. This led to a deterioration in the sustainability of public debt: the average effective interest rate rose from 3.7% in 2010 to 5.9% in 2019, and the public debt service went up from 2.2% of GDP in 2010 to 9.7% in 2020.

Due to the increasing burden of debt service, the severe recession, and a drop in revenues, the PFN rose to almost 15% of GDP in 2020. It was against this backdrop that, in the spring of 2020, Ecuador announced a selective default on a portion of its debt owed to private foreign creditors, before negotiating a restructuring in the summer of 2020. This will make it possible to significantly reduce debt service over the coming years (from an average of 11.3% of GDP over the past three years to 6.7% of GDP over the next three), while the international community has intervened massively to cover two-thirds of the PFN under the aegis of an IMF program, in an amount of USD 6.5 billion, that was agreed in September 2020.

The issue of improving public accounts and the sustainability of public debt remains fully relevant. The IMF considers the debt to be sustainable provided that an adjustment of the non-oil primary fiscal balance of 7 percentage points of GDP is achieved by 2023, which is very ambitious—first because it could be difficult for the new administration to implement it in the face of public opposition to austerity measures (as demonstrated by the popular protest movements in 2019); second, because it carries the risk of depression for an economy that depends on the public sector; and finally, both because this pace of adjustment has never been observed in the past and because the primary budget surplus target has never been reached in the low potential growth regime (2.5% by 2025) forecast by the IMF.

Preserving external balances and the gains from dollarization

The external balance situation is at the heart of macroeconomic stability, because of the dollarization of the country since 2000. However, despite its oil resources, Ecuador has rarely been able to achieve a current account surplus (only five times since the start of the 2000s) because of its weak productive sector, its limited competitiveness, and its dependence on imports.

The country is also facing an increase in its level of external debt (from 20.6% of GDP in 2010 to 59.4% of GDP in 2020). This has been caused by external public debt, and has led to an increase in external debt service from 2.5% of GDP in 2010 to 9.6% in 2020. This explains the stagnation of foreign exchange reserves at a low level, which the crisis and the fall in oil prices helped bring to a historic low of USD 1.9 billion (less than one month of imports) in March 2020. These pressures on foreign exchange reserves eased thanks to IMF disbursements, and at the end of 2020 they stood at USD 5.7 billion (equivalent to 2.7 months of imports).

While rising oil prices, donor support, and the restructuring of public debt should help stabilize the level of reserves in the coming years, the country will need to attract external financing on a sustainable basis. This will be all the more important given that the net international reserves of the Central Bank of Ecuador—its liquid assets, minus its short-term external liabilities and bank deposits—have been negative since 2016, thus reflecting the vulnerability of this dollarized economy in the event of an exogenous shock, a drying up of external financing, or a slippage in public finances.

List of acronyms and other abbreviations

AAGR	Average annual growth rate
AFRREO	Sub-Saharan Africa Regional Economic Outlook
ARA	The IMF's Assessing Reserve Adequacy measure
BCEAO	Central Bank of West African States
BEAC	Bank of Central African States
CEMAC	Central African Economic and Monetary Community
CNY	Chinese yuan or *rénmínbì* (RMB)
COMS	French Overseas Collectivities
DROMS	French Overseas Departments and Regions
DSA	Debt Sustainability Analysis
DSSI	Debt Service Suspension Initiative
EBRD	European Bank for Reconstruction and Development
ECF	Extended Credit Facility
EDCS	Emerging and developing countries
EU	European Union
EUR	Euro
FACT	Front for Change and Concord in Chad
FDI	Foreign direct investment
FRD	Fund for Reconstruction and Development
FY	Fiscal year
GBP	Pound sterling
GD	*Kartuli ocneba - Demok'rat'iuli Sakartvelo* (Georgian Dream – Democratic Georgia, a political party)
GEFN	Gross external financing need
GDP	Gross domestic product
HIPC	Highly indebted poor country
IDS	International Debt Statistics, World Bank database
IEDOM	Institut d'émission des départements d'outre-mer
IMF	International Monetary Fund
JIRAMA	*Jiro sy Rano Malagasy*, the Malagasy state-owned water and electricity company
JPY	Japanese yen
LIC	Low-income country

LMIC	Lower-middle-income country
NLD	National League for Democracy, a Burmese political party
ODA	Official development assistance
OECD	Organisation for Economic Co-operation and Development
PC	Paris Club
PGFN	Public gross financing need
PI	Portfolio investment
RCF	Rapid Credit Facility
RFI	Rapid Financing Instrument
SDRS	Special drawing rights
SLPP	*Śrī Lamkā Podujana Peramuna* (Sri Lanka People's Front, a political party)
SSA	Sub-Saharan Africa
UMIC	Upper-middle-income country
UNCTAD	United Nations Conference on Trade and Development
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
USD	United States dollar
WAEMU	West African Economic and Monetary Union
WEO	The IMF's World Economic Outlook
Y/Y	Year-on-year change

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Agence française
de développement
5, rue Roland Barthes
75012 Paris l France
www.afd.fr

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Publication director Rémy Rioux
Editor-in-chief Thomas Mélonio
Graphic design MeMo, Juliegilles, D. Cazeils
Layout Luciole

Legal deposit 3rd quarter 2021
ISSN 2266-8187
Printed by the AFD reprographics department

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