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Eighth Joint Annual Meetings of the African Union Specialized Technical Committee on Finance, Monetary Affairs, Economic Planning and Integration* and the Economic Commission for Africa Conference of African Ministers of Finance, Planning and Economic Development

Meeting of the Committee of Experts
Addis Ababa, 25–27 March 2015

Overview of economic and social conditions in Africa

Introduction

1. Despite the weak global economy, Africa's growth prospects remain strong. Over the past decade, Africa has recorded impressive economic growth of 5 per cent on average, making it the second-fastest growing region after East and South Asia. Growth continued to increase in 2014 and is expected to increase further over the forecast period (see figure 1).

2. The continent's growth is underpinned by improved governance and macroeconomic management, investment in infrastructure, rapid urbanization, a growing middle class and rising aggregate demand, diversified trade and investment ties with emerging economies, and improved regional integration and diversified trade partnerships within the region.

3. However, in the medium term, the outlook for the continent could change as a result of the fall in the price of oil and other commodities, the slow economic recovery of developed countries, tighter global monetary policies, weather-related shocks, and political instability in some African countries.

I. Developments in the global economy and the implications for Africa

4. Global growth increased moderately from 2.4 per cent in 2013 to 2.6 per cent in 2014. The potential for higher global growth rates has been dampened by emerging geopolitical tensions in Western Asia and the Crimean peninsula, and the economic slowdown in Japan. Global growth is projected to increase to 3.1 per cent in 2015.

* The Specialized Technical Committee replaces the Conference of African Ministers of Economy and Finance (CAMEF) and the Conference of African Ministers of Integration (COMAI). The Specialized Technical Committee brings together ministers of finance, monetary affairs, economic planning and integration.

5. In developed countries, growth picked up from 1.2 per cent in 2013 to 1.7 per cent in 2014, driven by stronger performance from the major European economies and some positive growth in other European countries after a period of negative growth. The European Union recorded growth of 1.3 per cent in 2014, up from 0.0 per cent in 2013, and growth is expected to rise to 1.7 per cent in 2015. Growth in the United States of America rose to 2.3 per cent, up from 2.2 per cent in 2013, and is expected to rise to 2.8 per cent in 2015, as a result of growth in business investment and increased consumer confidence driven by improved employment. In Japan, growth fell to 0.8 per cent, down from 1.5 per cent in 2013, but it is expected to increase to 1.2 per cent in 2015.

6. GDP growth in developing countries slowed from 4.7 per cent in 2013 to 4.4 per cent in 2014, largely because of low growth in Western Asia and Latin America and the Caribbean, as a consequence of ongoing geopolitical tensions, weak domestic investment demand and deteriorating terms of trade. Growth was strongest in East and South Asia, where it reached 5.9 per cent, up from 5.8 per cent in 2013. It is expected to rise to 6.0 per cent in 2015, driven by increases in investment and economic activity in general.

7. Economies in transition experienced a slowdown in growth, with a real GDP growth rate of 0.7 per cent, partly as a result of dampened growth in the Russian Federation, owing to the Crimean crisis and the associated economic sanctions. China is also expected to see growth fall, to 7.3 per cent, down from 7.7 per cent in 2013, as a consequence of the change in focus towards a more service- and consumption-oriented economy.

8. The global employment situation remains weak. Unemployment decreased from 6 per cent in 2013 to 5.9 per cent in 2014 (International Labour Organization, 2014). Unemployment in developed economies remains high, at 7.8 per cent. Unemployment also continues to be high in Africa and Latin America and the Caribbean, with unemployment rates of 10.1 per cent and 6.6 per cent respectively in 2014. Young people are particularly affected, with global youth unemployment rising to 13.0 per cent in 2014, up from 13.1 per cent in 2013.

9. The rate of global inflation picked up slightly, to 3.1 per cent in 2014, up from 3.0 per cent in 2013, but is expected to slow to 2.9 per cent in 2015. Inflation remains low in developed countries, particularly in the eurozone, owing to weak economic recovery and temporary shocks such as the fall in food and energy prices. Low inflation in the eurozone coupled with persistently high unemployment continues to present the risk of deflation and a consequent return to the debt crisis and economic uncertainty in Europe. In developing countries, inflation fell from 5.8 per cent in 2013 to 5.7 per cent in 2014, as a result of lower inflation in South Asia, and is expected to decrease further, to 5.4 per cent in 2015, owing to the fall in global commodity prices and tighter monetary policies.

10. With the exception of Latin America and the Caribbean, fiscal balance improved in all regions (International Monetary Fund, 2014). Developed countries continued their fiscal tightening, reducing the overall deficit from 4.9 per cent of GDP in 2013 to 4.2 per cent in 2014. In the eurozone, the overall deficit was brought down to 2.6 per cent, from 3 per cent in 2013. In Japan and the United States, the fiscal deficit is estimated to have been reduced to 7.2 per cent and 6.4 per cent respectively, down from 8.4 per cent and 7.3 per cent in 2013.

11. World trade slowed in 2014, as the growth rate of exports fell to 3.3 per cent, down from 3.8 per cent in 2013. Nevertheless, global export growth is expected to increase to 6.8 per cent in 2015 thanks to a rebound in export growth in developing regions, in particular South Asia and Latin America and the Caribbean. Current account balances remained relatively stable in the major

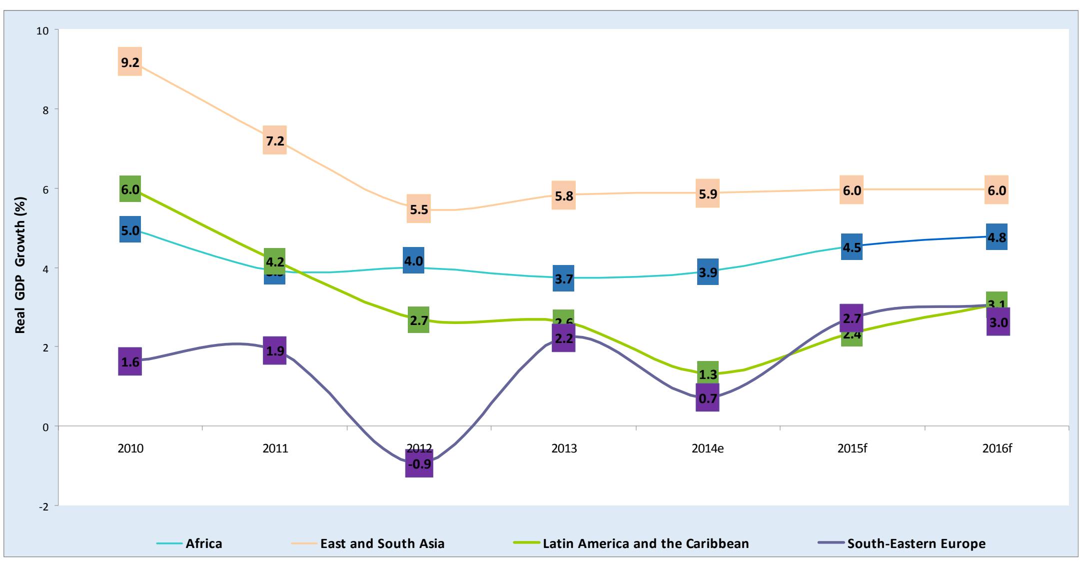
economies in 2014 relative to 2013 levels. Global foreign direct investment (FDI) remained stable at 2.7 per cent of GDP, unchanged from the previous year (Economist Intelligence Unit, 2014). However, FDI inflows to emerging economies have fallen, as a result of improved business confidence and economic recovery in developed countries.

12. The outlook for 2015 remains uncertain owing to the fragility of the global economic recovery, particularly in the eurozone, as evidenced by the lack of improvement in employment and the continuing risk of deflation. Furthermore, slower growth in China may reduce demand for African exports. Current political tensions in the Crimean peninsula and Western Asia pose a risk for the global economy as a whole, and may have indirect consequences on Africa through reduced demand from affected trading partners. In addition, the consequences of tapering quantitative easing measures in developed countries remain uncertain; indeed, the possible increase in interest rates in the United States has already led to capital outflows and the depreciation of currencies in developing countries as investors return to safer assets (United Nations, 2014).

II. Africa's economic performance and prospects

13. Africa's growth increased from 3.7 per cent in 2013 to 3.9 per cent in 2014. Only East and South Asia grew faster, at 5.9 per cent (see figure 1). Africa's GDP growth rate is expected to increase to 4.5 per cent in 2015 and 4.8 per cent in 2016.

Figure 1
Growth in emerging and developing regions, 2010–2016



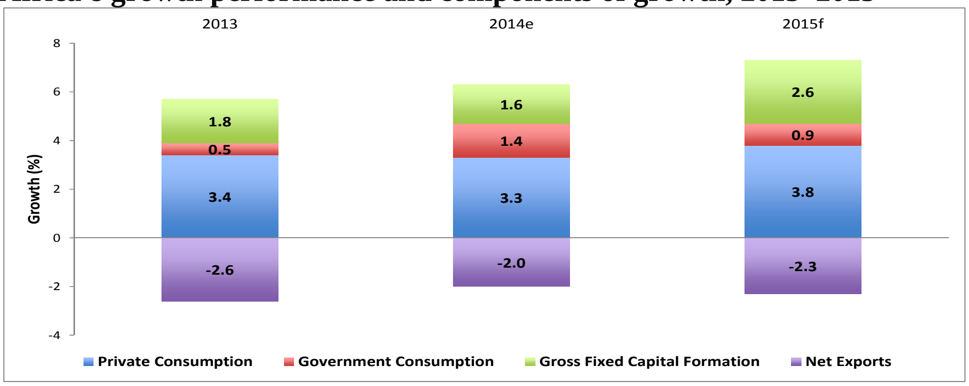
Source: Calculations based on United Nations Department of Economic and Social Affairs (UN-DESA), 2014; data for Africa exclude Libya.
Note: e = estimates, f= forecasts.

A. Private consumption and investment are key drivers of growth

14. Private consumption and investment, which grew by 3.3 per cent and 1.6 per cent in 2014, down from 3.4 per cent and 1.8 per cent respectively in 2013, remain the key drivers of GDP growth (see figure 2). Growth in private consumption is underpinned by greater domestic demand as a result of increased consumer confidence and an expanding middle class. Investment (gross capital formation) is driven mainly by an improved business environment. Increased government

spending on infrastructure was also an important driver of GDP growth in 2014. Its contribution is expected to decline to 0.9 percentage points in 2015 owing to fiscal consolidation measures, mostly in Central, Southern and West Africa.

Figure 2
Africa's growth performance and components of growth, 2013–2015



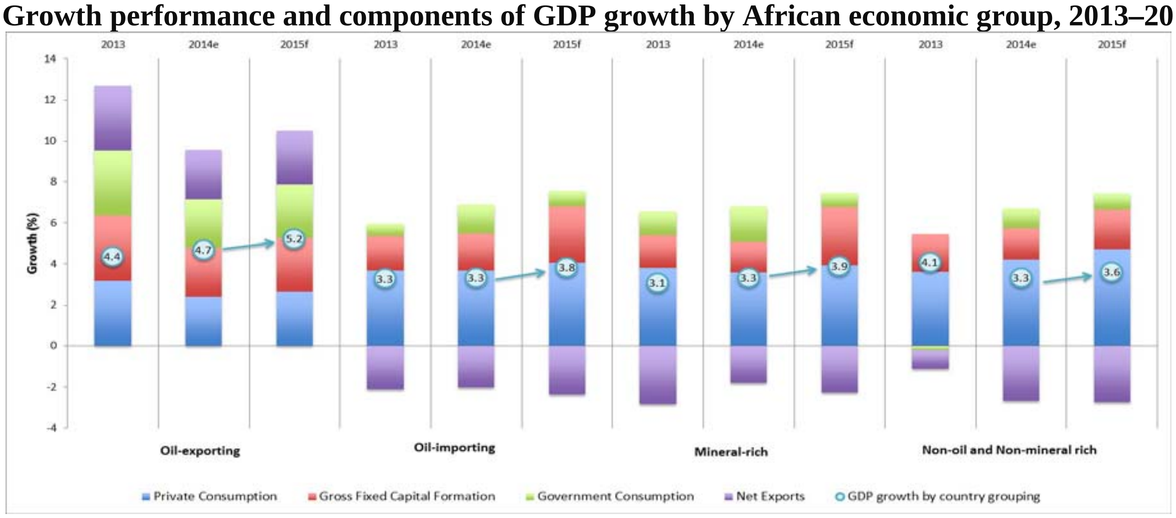
Source: Calculations based on UN-DESA, 2014; EIU, 2014.
Note: e = estimate; f = forecast.

B. Growth variations across economic groups and subregions continue

15. African oil-exporting countries (with the exception of Libya) grew faster than other African countries in 2014, with growth of 4.7 per cent, up from 4.4 per cent in 2013 (see figure 3). Despite falling oil prices, the growth of this group of countries is expected to continue into 2015, with growth of 5.2 per cent due to the recovery of growth in consumption and investment.

16. Oil-importing countries are expected to grow by 3.8 per cent in 2015, after stagnating at 3.3 per cent in 2013 and 2014, thanks to low oil prices and increased consumer and business confidence. Private consumption and investment are expected to grow by 4.1 per cent and 2.8 per cent respectively in 2015.

Figure 3
Growth performance and components of GDP growth by African economic group, 2013–2015



Source: Calculations based on UN-DESA, 2014; EIU, 2014.
Note: e = estimate; f = forecast. Data on growth of oil-exporting countries exclude Libya.

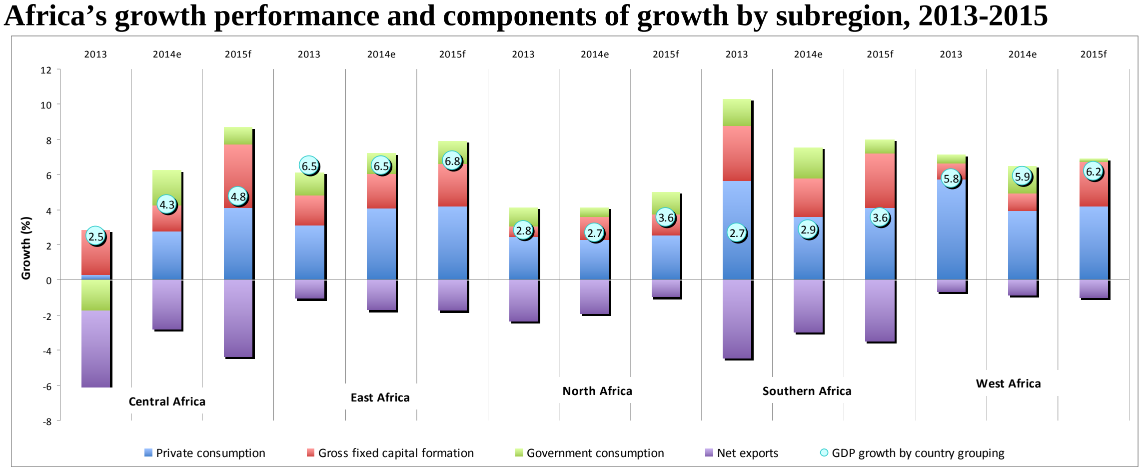
17. At the subregional level, Central Africa's growth momentum is expected to continue. After accelerating from 2.5 per cent in 2013 to 4.3 per cent in 2014, growth is expected to rise further to 4.8 per cent in 2015 (see figure 4), driven by high public spending on capital-intensive infrastructure projects in Cameroon and the Congo Republic, and new oil and gas developments in Cameroon and Chad.

18. Strengthened regional integration in the East African Community has continued to boost GDP growth in the subregion in 2014. After remaining flat at 6.5 per cent in 2013 and 2014, growth is expected to increase to 6.8 per cent in the subregion in 2015 (see figure 4). Djibouti, Kenya and Uganda will continue to be the key drivers of growth in 2015. Djibouti's growth is underpinned by considerable investment in the country's port capacity, driven by strong demand for port services from Ethiopia. Rapid expansion in banking and telecommunication services, a growing middle class, urbanization, and investment in infrastructure, particularly railways, is stimulating growth in Kenya, while Uganda's growth is underpinned by increasing activity in sectors such as construction, financial services, transport and telecommunications.

19. Growth in North Africa (excluding Libya) has failed to recover, despite improving political stability in Tunisia. Growth fell slightly, from 2.8 per cent in 2013 to 2.7 per cent in 2014. Weak oil prices, the slowdown in investment in Egypt, and tight monetary policies in Algeria, Egypt, Morocco and the Sudan were the main constraints to growth. However, growth is expected to improve in 2015 as more stability returns to Egypt, the subregion's largest economy. GDP growth is also expected to be supported by growth in government expenditure on infrastructure projects in the subregion.

20. Southern Africa is expected to experience accelerated GDP growth, from 2.9 per cent in 2014 to 3.6 per cent in 2015 (see figure 4), driven by increased investment in the non-diamond sector in Botswana, the recovery of private consumption in South Africa, and increased investment in mining and natural gas exploration in Mozambique. Furthermore, GDP growth is expected to be supported by the acceleration in private consumption amid growing consumer confidence in the countries of the subregion. However, the slowdown in oil and mineral prices poses a threat to the subregion's medium-term growth prospects, given that two thirds of the countries are mineral-rich or oil-exporting.

Figure 4
Africa's growth performance and components of growth by subregion, 2013-2015



Source: Calculations based on UN-DESA**,** 2014; EIU, 2014.
Note: e = estimate; f = forecast. Growth for North Africa excludes Libya.

21. West Africa grew by 5.9 per cent in 2014, up one percentage point from 2013. The subregion's growth is expected to accelerate to 6.2 per cent in 2015 (see figure 4). Rising private consumption and investment, particularly in Cabo Verde, Nigeria and Senegal, are the key drivers of growth. In 2015, private consumption and investment in the subregion are expected to grow at 3.5 per cent and 2.5 per cent respectively, an increase on the figures for 2014. The services sector in Nigeria is also a key driver of West Africa's growth. However, there is some uncertainty in the subregion owing to political challenges in Mali and the Ebola outbreak, which are expected to be the major internal risks for the West African economies, although recent estimates from the Economic Commission for Africa (ECA, 2014a) reveal that the impact of Ebola on growth is expected to be negligible.

C. Impact of oil prices on growth is marginal

22. Although crude oil prices continued to fall between June and December 2014, with an average monthly decline of 8.0 per cent, the impact on Africa's growth has been marginal. In fact, the low prices helped the continent's GDP to grow by an extra 0.03 per cent, thanks to the positive impact on oil-importing countries and the marginal negative impact on oil-exporting countries, given the continued depreciation of their local currencies (especially in Angola, Ghana and Nigeria).

23. In addition, the marginal effect of the continued decline in oil prices on growth has been sustained in non-oil sectors, driven by the expansion of services sectors in some countries, such as Kenya and Rwanda, the strengthening of intra-African trade in manufacturing sectors, and improved productivity and structural transformation (ECA and AUC, 2014).

24. Oil-exporting countries have protected themselves somewhat from volatile crude oil prices by saving oil revenue during periods of high oil prices and using these savings to attenuate the impact of falling crude oil prices on their economies.

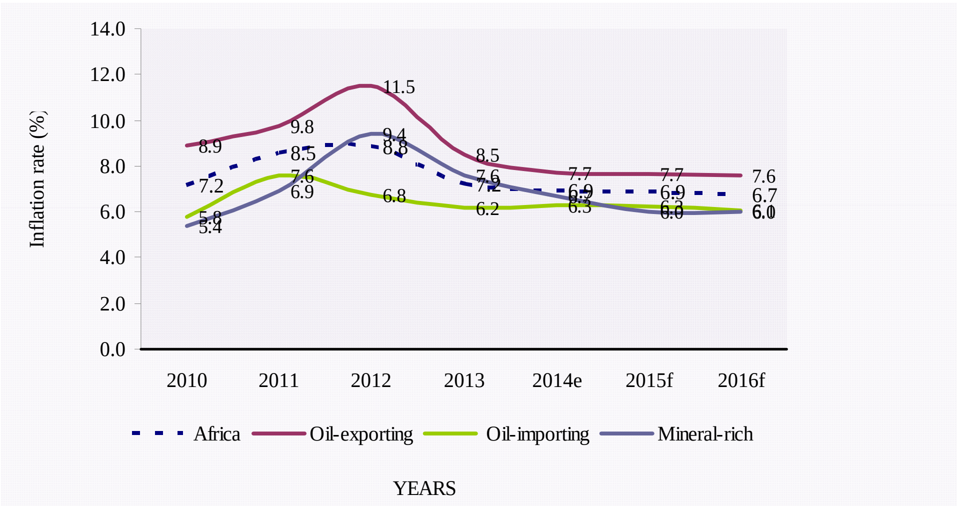
D. Negligible economic effect of the Ebola outbreak on Africa's GDP

25. Although the impact of the Ebola outbreak on the GDP of the three most affected countries (Guinea, Liberia and Sierra Leone) is significant, the effect on the GDP of the West African subregion and Africa as a whole is expected to be negligible. This is because Guinea, Liberia and Sierra Leone together account for 2.4 per cent and 0.7 per cent of the GDP of West Africa and Africa as a whole, respectively. Forecasts for 2014 and 2015 reveal that growth in West Africa will be affected by 0.1 percentage point, while the growth of Africa as a whole will be affected by just 0.02 percentage points (ECA, 2014a).

E. Inflation will continue to fall

26. Inflation in Africa is expected to continue on the same downward trend that it has been experiencing since 2012. It is expected to stabilize at 6.9 per cent between 2014 and 2015 and decelerate to 6.7 per cent in 2016 (see figure 5). Oil-exporting countries are expected to experience an increase in inflation in 2015 before the rate tips down a little in 2016. Exchange rate depreciation is observed to be the main driver of rising inflation among oil-exporting countries, with marginal effects on oil-importing and mineral-rich countries, which could be attributed to the effects of falling global oil and commodity prices.

Figure 5
Inflation rate by economic group, 2010–2016



Source: Calculations based on UN-DESA, 2014.
Note: e = estimate; f = forecast.

27. At the subregional level, Central Africa is expected to be the least inflationary region, mainly because of the common monetary policy pursued by most of its countries through the shared euro-pegged currency, the CFA franc. Followed by Southern Africa, due to lower oil and global food prices, as well as improved domestic food supply in Malawi and Zambia, tighter monetary policy in Lesotho and South Africa, and appreciation of local currencies in Botswana and Zambia.

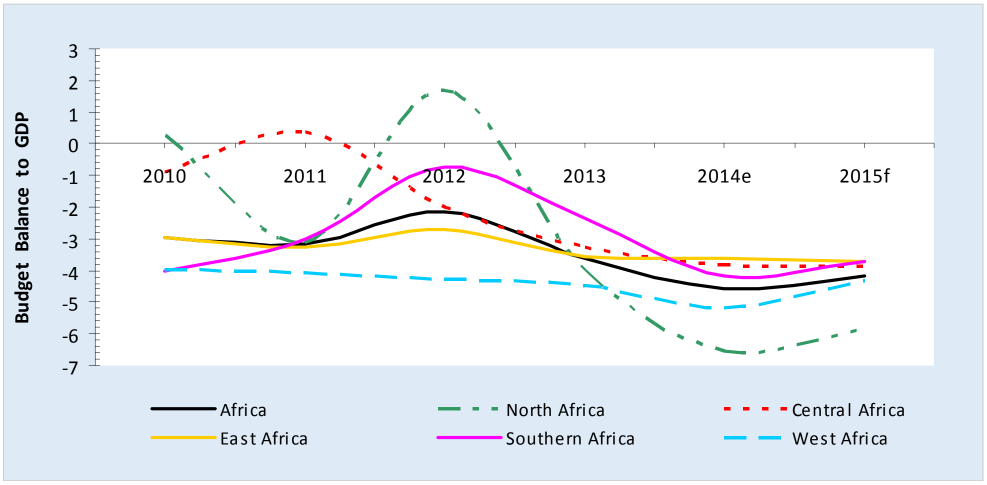
F. Most African currencies will continue to depreciate

28. Declining oil and commodity prices, the tightening of monetary policies in developed countries and large trade and fiscal deficits will continue to drive exchange rate depreciation in most African countries. South Africa's currency is expected to pick up by 1.2 per cent to 10.66 rand to one United States dollar in 2015, though some volatility is possible as it is the most heavily traded African currency. The Central Bank of Nigeria devalued the naira in November 2014 to minimize the erosion of foreign currency reserves, and raised the monetary policy rate by 100 basis points to 13 per cent. The Kenya shilling depreciated in 2013 and 2014 on the back of weak tea prices and low tourist inflows due to security concerns. In the West African Economic and Monetary Union, the CFA franc appreciated against the United States dollar in 2014; however, it is expected to depreciate in 2015.

G. Fiscal deficits are narrowing

29. The region's average fiscal deficit widened from 3.6 per cent of GDP in 2013 to 4.6 per cent in 2014 (see figure 6), but should narrow to 4.2 per cent in 2015, tracking decreases in North Africa (from 6.6 to 5.8 per cent), Southern Africa (4.2 to 3.7 per cent) and West Africa (5.2 to 4.3 per cent).

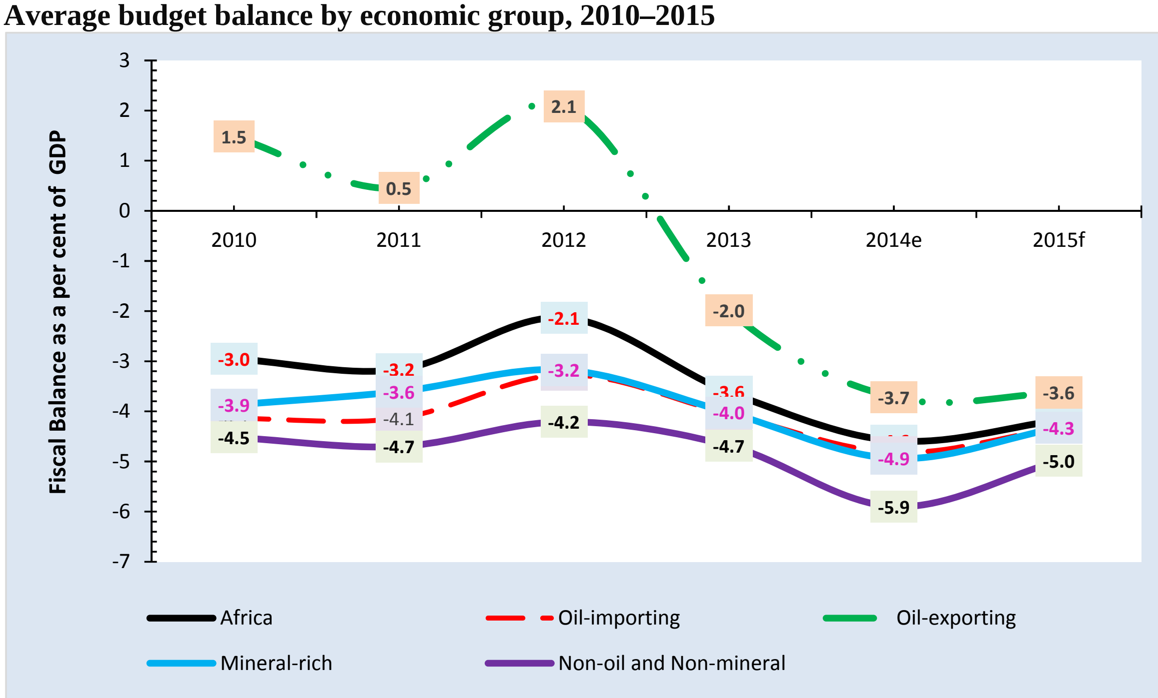
Figure 6
Average budget balance by subregion, 2010–2015 (percentage of GDP)



Source: Calculations based on EIU, 2014.

30. Deteriorating oil prices are the key driver of fiscal deficit increases among oil-exporting countries, in addition to fuel subsidies and infrastructure spending in many countries. Oil-importing, mineral-rich, and non-oil and non-mineral-rich countries are expected to experience the largest gains of 0.5, 0.6 and 0.9 percentage points in 2015 on the back of lower oil prices (see figure 7).

Figure 7
Average budget balance by economic group, 2010–2015



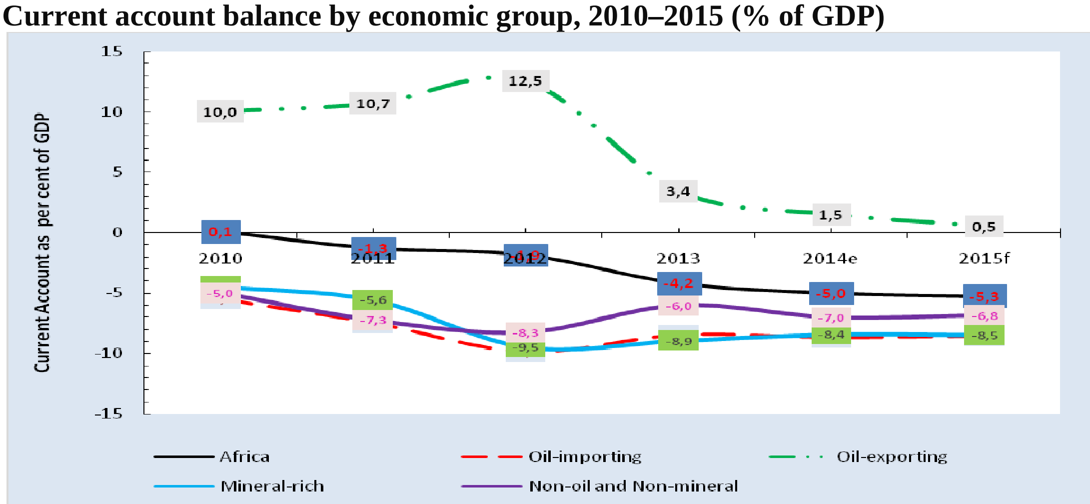
Source: Calculations based on EIU, 2014.

H. Falling oil prices will affect current account balances

31. Africa's overall current account deficit will remain owing to trade deficits and increased demand for capital goods. Oil-exporting countries will keep their current account surpluses, but they will be much lower in 2015 than in 2013 and 2014, while other economic groups will retain persistent current account deficits (see figure 8).

32. More specifically, in 2014 the current account deficit of oil-importing countries deteriorated by 0.2 percentage points to 8.7 per cent of GDP, although this is expected to improve in 2015 to 8.6 per cent. Mineral-rich countries will maintain large current account deficits because of their reliance on imported services and their structural deficits on the income account, as multinational companies (which dominate the mining sectors of African countries) continue paying external debts and repatriating profits (EIU, 2014). After improving by around 0.5 percentage points in 2014, the current account deficits of these economies are expected to deteriorate by 0.04 percentage points to 8.5 per cent of GDP in 2015. Non-oil-exporting and non-mineral-rich countries will have the largest current account deficits, mainly due to limited access to foreign currency reserves.

Figure 8
Current account balance by economic group, 2010–2015 (% of GDP)

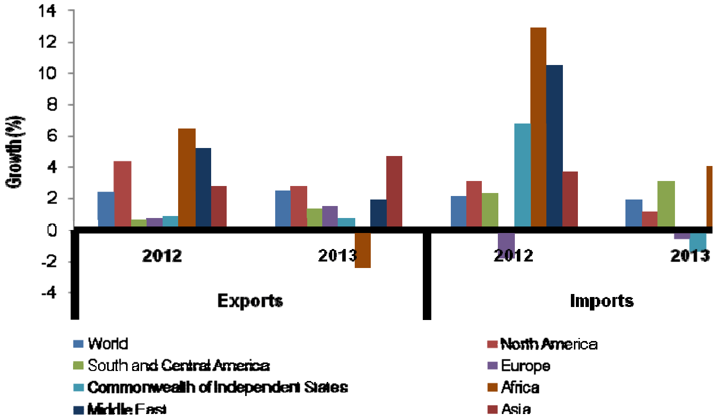


Source: Calculations based on EIU, 2014.
Note: e = ECA estimates; f = forecasts.

I. Merchandise trade boom is tapering off

33. Africa's merchandise exports declined by 2.4 per cent in 2013, after growth of 6.5 per cent in 2012, one of the highest of any region (see figure 9). Growth was mainly driven by exports of fuel and natural resources in their raw form, which accounted for approximately two thirds of total exports. The decline in merchandise exports is the result of the downward trend in the prices of commodities, which are still dominated by natural resources. This underscores the need for Africa to diversify its production and export base by adding value to its commodity exports.

Figure 9
Growth in world merchandise trade by region, 2005–2013



Source: Word Trade Organization, 2014

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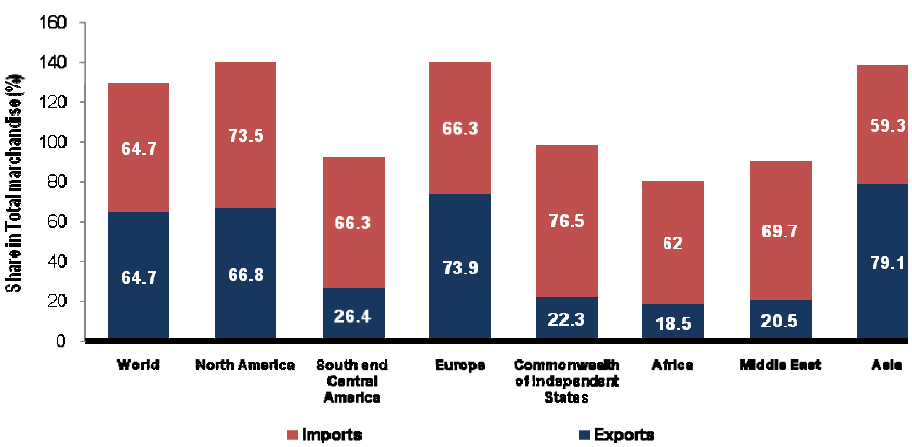
34. In 2013, Africa exported the lowest share of manufactured goods as a percentage of total merchandise exports of any region, at 18.5 per cent, with Asia having the highest share, followed by Europe(see figure 10). Trade in intermediate goods and participation in the high end of global value chains accounted for the high share of manufactured goods in total merchandise exports and imports of North America, Europe and Asia. Africa's low export figure is a reflection of minimal participation in global value chains.

Figure 10
Share of manufactured goods in total merchandise trade by region, 2013



Source: Word Trade Organization, 2014.

J. Private foreign inflows are on the rise

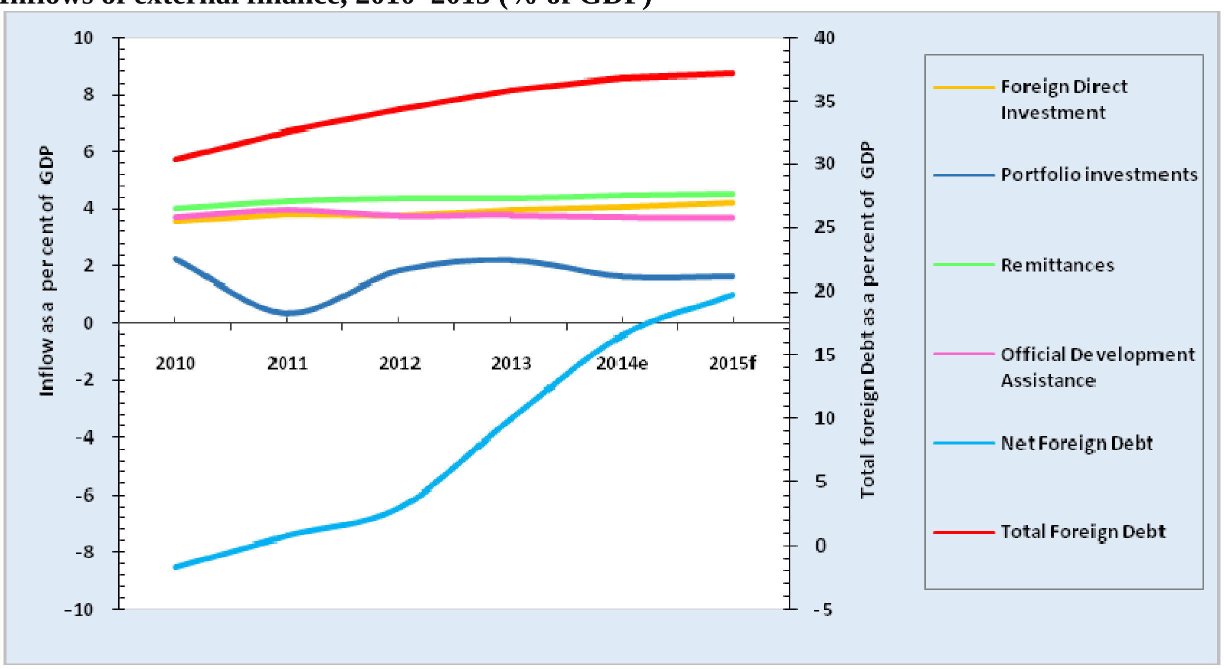
35. Africa continues to attract more and more private capital thanks to an improved business environment and increasingly positive corporate sentiment ratings as a result of, for example, regulatory improvements, such as those observed in Mauritius and Rwanda. FDI remains a large external source of finance, but was surpassed by remittances in 2010 (see figure 11), which are also the most stable source of external financing. Remittances nudged up from 4.4 per cent of GDP in 2013 to 4.5 per cent of GDP in 2014, and are expected to further increase to 4.6 per cent of GDP in

2015 as more African expatriates seek to invest in their home countries. To leverage increasing remittances, the continent needs to decrease the cost of sending money and develop financial instruments to channel remittances into developmental programmes.

36. FDI is the second largest source of external private equity inflows. FDI increased from $57.2 billion in 2013 to $61.1 billion in 2014 and is projected to increase to $66.9 billion in 2015, equivalent to 3.9 per cent, 4.1 per cent and 4.2 per cent of GDP respectively. However, FDI remains relatively concentrated in resource sectors, and policies that aim to diversify it towards the manufacturing sector are needed.

37. Portfolio flows averaged around 1.6 per cent of GDP between 2010 and 2015. They are volatile as they are often influenced by global monetary policy stances and the political outlooks of developing and emerging countries. They decreased from $31.6 billion in 2013 to $24.1 billion in 2014, but are projected to increase to $25.5 billion in 2015. Despite the slow recovery of developed and emerging economies, both FDI and portfolio equity flows are expected to continue increasing, underscoring the global private sector's appetite for the continent's opportunities. Frontier markets are key to attracting foreign private capital, bringing in 25.1 per cent and 26.3 per cent of Africa's total FDI inflows in 2013 and 2014, and 90 per cent and 63.2 per cent of its portfolio flows. In 2015, frontier markets are expected to attract 27 per cent and 59 per cent of total FDI and portfolio flows.

Figure 11
Inflows of external finance, 2010–2015 (% of GDP)



Source: Calculations based on EIU, 2014; UNCTADstat, 2014.
Note: e = ECA estimate; f = forecast.

38. Illicit financial outflows through trade mispricing are widespread in resource-rich economies. Such flows are estimated at almost $60 billion a year and grew by 32.5 per cent between 2000 and 2009. Cumulatively, over this period, illicit financial flows were equivalent to nearly all the overseas development assistance (ODA) received by Africa (ECA, 2014b). Policy interventions through tax incentives and close monitoring could help to curb such flows.

39. ODA will remain a key source of external public finance for many countries. In 2013 and 2014, ODA accounted for 3.8 per cent and 3.7 per cent of Africa's GDP respectively. However, the ebb and flow of ODA is tied to the (often short-term) priorities of development partners, which can be driven by non-developmental concerns, including geopolitics and security. This is why Africa must prioritize financing and mobilize resources to achieve structural change.

40. Total foreign debt has been above 30 per cent of GDP since 2010 and is expected to rise to 37.1 per cent of GDP in 2015. It is expected that net foreign debt (total debt minus reserves) will be equivalent to 1 per cent of GDP in 2015. Net foreign debt has been negative since 2006 owing to high international reserves in oil-exporting economies. Mineral-rich and oil-importing countries have positive net foreign debt, and some extreme cases[1] have very high ratios, raising issues of debt sustainability.

K. Private equity: a new alternative for raising additional resources

41. Given the debt burden of many African countries and the growing challenges faced by the continent as a result of rapid urbanization, population growth and rising demand for infrastructure, additional resources are required. Private equity could provide part of the solution. Indeed, the countries that have recorded most progress in terms of economic growth over the past decades are also the ones that have attracted the greatest share of private equity capital (ECA, 2014c).

42. The concept of using private equity to raise additional resources is particularly promising for the manufacturing sector in Africa, which is mainly made up of small- and medium-sized enterprises. Given the rigidities inherent to financial intermediation in Africa and the high interest rates charged by banks, private equity could also enhance domestic financing by driving resources towards medium- and long-term investment.

43. Over the past decade, private equity investment has risen significantly, with average annual growth of 26 per cent, reflecting an improved and sound business environment. The consumer discretionary (28 per cent), industrial (26 per cent), materials (20 per cent), energy (12 per cent) and financial and information technology (10 per cent) sectors received the highest share of private inflows between 2006 and 2012 (ECA, 2014c).

L. African countries with higher savings make fewer domestic investments

44. The diversification of resources for investment is very important in the context of global uncertainty as it gives room for flexibility and reduces dependence on donors. Reducing dependence on external sources of finance is a way forward for Africa to transform structurally. The mobilization of domestic savings for investment should be strengthened. In East Asia, regional economic growth has been underpinned by high domestic savings and investment (North-South Institute, 2010). However, this trend of using domestic savings for investment purposes has not yet been observed in many African countries, where higher savers tend to have higher savings-investment ratio, indicating that they invest little at home (see figure 12). Africa's biggest savers invest little, especially the oil-exporting countries, because their focus is on building buffers against exogenous shocks (ECA and AUC, 2014).

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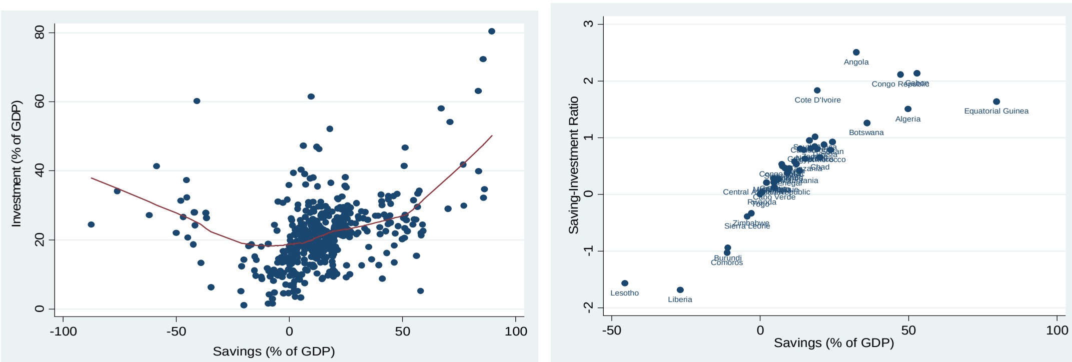
[1] Such as Cabo Verde (59 per cent of GDP), Ghana (28 per cent of GDP), the Sudan (55 per cent of GDP), Mauritania (52 per cent of GDP), Mozambique (28 per cent of GDP), Sao Tome and Principe (117 per cent of GDP), Senegal (25 per cent of GDP), Seychelles (90 per cent of GDP), Tunisia (50 per cent of GDP) and Zimbabwe (338 per cent of GDP).

Figure 12
African savers and investors, 2000–2010



Source: Calculation based on World Development Indicators.

III. Risks and uncertainties surrounding Africa's continued growth

45. A number of internal and external risks could affect Africa's medium-term prospects. The continued decline of oil and commodity prices, the slow recovery of the United States, the eurozone and Japan, and the decline in demand for commodities in China could hamper Africa's medium-term trade performance.

46. In addition, tighter global financial conditions in developed economies might lead to a rise in interest rates, resulting in the outflow of private capital and increased volatility of currencies. This could affect frontier market economies such as Ghana, Nigeria, South Africa and Zambia, as the reversal of capital flows could lead to the weakening of their currencies. While controls on capital flows offer a temporary solution, more robust strategies, such as adjusting funding strategies and plans and improving the business environment to retain capital, could play a vital role.

47. Political instability, terrorism and violence in a number of African countries, including the Central African Republic, the Democratic Republic of the Congo, Kenya, Lesotho, Libya, Mali, Nigeria, Somalia and South Sudan, are causes for concern. Nevertheless, the number of armed conflicts in Africa has decreased since 2000, and more initiatives are being undertaken at the continental level to address issues of peace and security (ECA, 2014d).

48. Weather-related shocks also pose a threat, given that most African economies are still dependent on rain-fed agricultural practices. Global cooperation in addressing climate change will go a long way towards mitigating some of these risks.

IV. Need to link structural change and social development

49. Africa's low level of development stems in part from its slow pace of change from commodity-based activities, which hinders the effective accumulation and harnessing of physical and human capital. To ensure that robust and resilient economic performance through industrialization and trade contributes to sustained and inclusive development, Africa must adopt social development strategies that are consistent with the expansion of modern, industrial sectors. The essential features that define economic change are tied to social transformation.

A. Improvement in some indicators

50. Africa continues to make consistent progress towards social outcomes, as measured by the Millennium Development Goals. Poverty has decreased overall on the continent and there have been marked improvements in primary school enrolment. Gender parity at primary school level has been reached by the majority of African countries. Women representation in parliament now stands at 20 percent, the second highest rate in the world after Latin America. Health outcomes have also improved, with under-five mortality dropping from 146 to 90 per 1,000 live births between 1990 and 2010. In addition, there has been a 1 percent decline in HIV prevalence from 2001 to 2011, with new infections among children decreasing by 52 percent over the same period (ECA, 2014e). However, these aggregate figures vary considerably across income, location and gender. Low-income rural communities, women and vulnerable groups remain excluded from participating in socioeconomic development.

B. Poverty and inequality lead to social exclusion

51. Poverty has declined but inequality permeates African societies and reinforces a vicious circle of inequity, low incomes and social exclusion. The responsiveness of poverty to economic growth is weakened by persistent socioeconomic inequality in Africa. Widening inequalities in access and the outcomes of education and health significantly reduce the gains from growth accruing to the poor (Ravallion, 2001; Fosu, 2011).

52. The unequal distribution of assets and uneven access to public services such as education and health care deepens the gap between the haves and the have-nots. For example, children from the poorest households are three times more likely to be out of school. In urban areas, more than 90 per cent of women are looked after by a trained professional during childbirth; this drops to 71 per cent in rural areas (ECA, 2013).

C. Measuring social inclusion

53. In response to a call from its member States, ECA has developed a tool – the African Social Development Index – to assess progress towards increased social inclusion. Following a life-cycle approach, the tool is intended to measure progress in the reduction of human exclusion in six dimensions of well-being, including health, education, employment and in come. Its key feature is that it can be used at different levels using national data to assess the impacts of exclusion between urban and rural areas and across gender and groups of the population, capturing inequalities within countries. In addition, the results of the Index can be used to identify the drivers of exclusion in each country or subregion, and assess the impact of social policies on exclusion, thereby improving the effectiveness of social policy targeting.

D. Population dynamics and urbanization

54. Africa's population is expected to rise by 3.2 billion (of the projected 4 billion worldwide increase) by 2100. Its working-age population will increase by 2.1 billion over the same period, accounting for 41 per cent of global working-age population by 2100, a surge from 12.6 per cent in 2010 (Drummond, Thakoor and Yu, 2014). If adequately harnessed towards structural change, the continent's rising share of the working-age population and the resulting decline in the dependency ratio could lead to higher economic output through productivity gains, savings and investment.

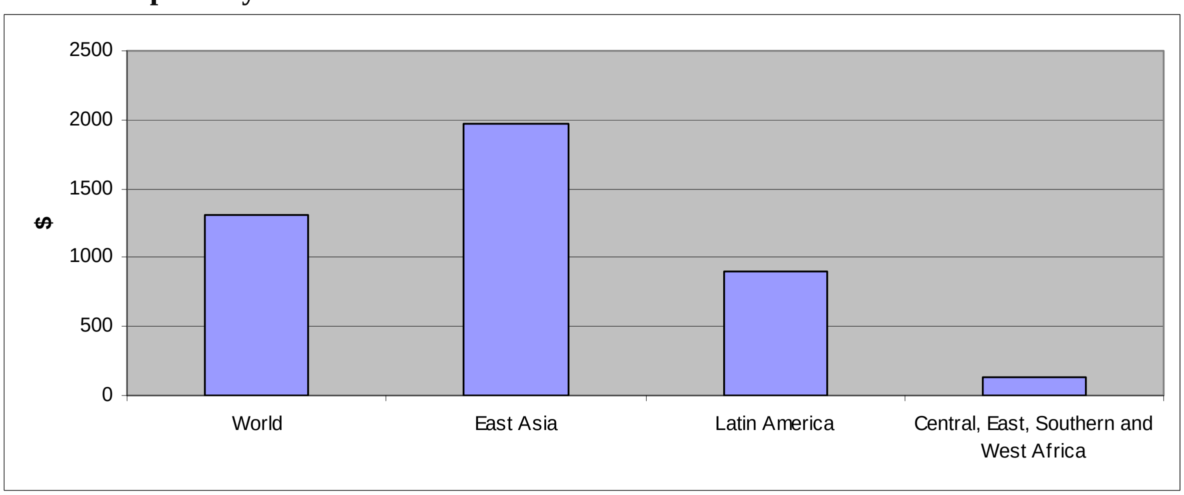
55. Despite rapid urbanization, Africa is still the least urbanized continent. Just 38 per cent of Africa's population lives in cities, and most African countries have an urbanization rate of less than 20 per cent. However, African urban areas grew 1.7 times faster than peri-urban and rural areas between 2005 and 2010 (UN-Habitat, 2010). As the locus of economic activity has shifted from the countryside, Africa has gained 43 cities, with combined mega-cities and smaller urban areas accounting for 55 per cent of GDP (African Development Bank, 2011). However, Africa's urban development has occurred without accompanying industrialization, with a negative spill over effect on informal employment, inequality and poverty.

E. Quality of education remains an issue

56. Although primary school enrolment increased by 24 per cent in Africa over the period 1990–2012 (ECA, 2014e), completion rates remain the lowest in the world. The improvement in enrolment rates, while noteworthy, has not resulted in better learning outcomes because the quality of education has declined over the same period. Data show that one out of three children in a selected group of African countries falls short of the minimum learning threshold for numeracy and literacy, leading to skills gaps and increasing barriers to socioeconomic opportunities (Watkins, 2013).

57. Indeed, the overall quality of education in Africa remains poor, despite the fact that good education systems are essential for an industrial workforce. Large class sizes as a result of the increased number of students remain a challenge. Of 162 countries with data, 26 have a pupil to teacher ratio of above 40:1; and 90 per cent of these countries are in Africa (to ensure that children receive a high-quality education, there should be 1 teacher per 25 primary-school pupils). Africa has a shortfall of about 1.7 million teachers and there is a need to expand teacher training programmes (UNESCO, 2014). The number of children enrolled in school has increased from 62 million in 1990 to 149 million in 2012 but resources have failed to keep up with this increase (ECA and others, 2014). In Africa, annual public expenditure per primary school child is $131, one tenth of the world average and far below the East Asian average of $1,974 (see figure 13).

Figure 13
Unit cost of primary school in 2010



Source: Calculations based on UNESCO (2014).

F. Transition from school to work

58. Completing secondary school is essential in order for young people to acquire the skills they need to access more specific technical and vocational training courses, which can encourage productivity gains (African Centre for Economic Transformation, 2014). Enrolment in lower secondary education increased from 29 to 49 per cent between 1999 and 2011 in Central, East, Southern and West Africa. However, completion rates, especially for girls and young women, remain low on average, at 37 per cent, and highly skewed towards higher-income urban populations.

59. Providing education to transform knowledge into productivity is key for Africa's industrialization. This includes ensuring wider access to secondary education. Tertiary enrolment, which could help to address the inadequate supply of teachers, is growing at 6 per cent. Africa's university enrolments are skewed towards humanities and liberal arts, with science and engineering constituting only 25 per cent of enrolment.

60. Traditional schools are ill-equipped, and technical and vocational education and training centres are not sufficiently prioritized to meet the needs of industrial development. In Africa, these centres train less than 5 per cent of young people. Many centres do not provide recognized certificates and have too few qualified staff, obsolete equipment, ill-adapted programmes and weak links to the job market. The skills required for transformation go beyond the acquisition of formal schooling. National productive capacities develop through the interrelated processes of capital accumulation, along with a skills set that enables technological adoption and imitation and progress. Combining formal education with on-the-job training and apprenticeships helps to produce the skills required for transformation.

61. Beyond hard technical competencies, soft skills are needed – such as cognitive, creative, problem-solving and managerial skills – which are difficult to develop in traditional school systems. Recent evidence shows that programmes combining in-class and on-the-job training provide soft (behavioural) skills and hard (technical) skills, which can have a positive impact on employability and earnings. A poorly skilled and educated labour force is the top supply bottleneck underscored by global executives when considering manufacturing investment decisions in Africa (African Center for Economic Transformation, 2014).

G. Progress in health is essential for labour productivity and industrialization

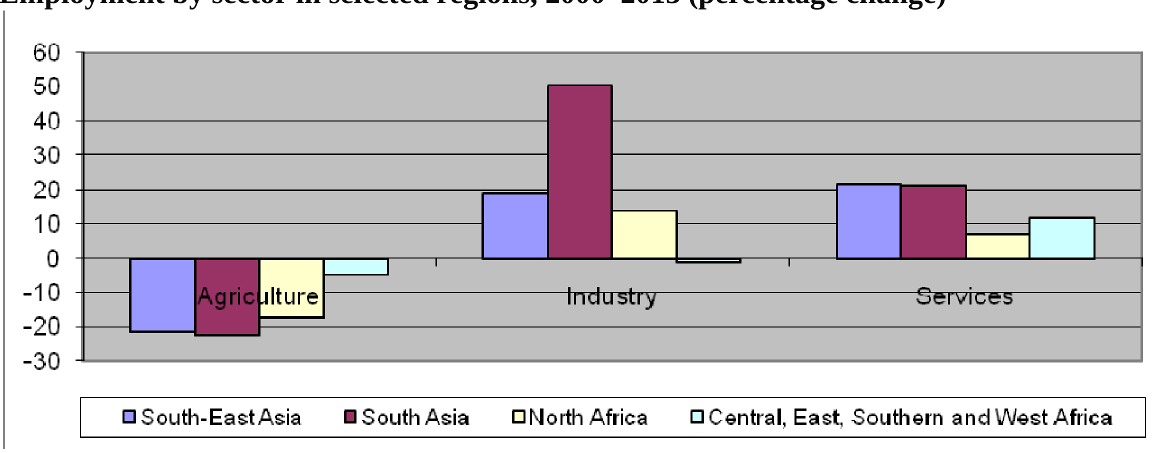
62. Targeted programmes that alleviate poor health and malnutrition can help to increase educational attainment and productivity, with multiplier effects on growth and development. Indeed, labour productivity forgone (measured by working hours lost) due to child mortality related to under nutrition can affect the whole economy, reaching 11.9 percent of GDP in Ethiopia, 1.4 percent in Swaziland and 2.0 percent in Uganda (AUC and others, 2014). Failure to prevent or respond to under nutrition early on in a child's life often leads to incremental health costs and exclusion from full labour market participation in later life.

63. Potential productivity gains could be even greater if the issues of unequal access and utilization of health services across income, gender and location are addressed. Health-related costs hit low-income groups disproportionately. Families can have to pay for up to 90 per cent of any health care they receive, putting a heavy burden on low-income families, and is one of the main causes of families falling into poverty (AUC and others, 2014).

H. Employment in manufacturing and modern services key to structural transformation

64. Structural transformation is critical for spurring labour productivity and employment opportunities in developing countries. Central to this is the movement away from low-productive to high-productive activities and from capital-intensive to labour-intensive activities, including manufacturing. In some countries, such as Algeria, Tunisia and South Africa, the decline in the contribution of low-productive agricultural employment, supplemented by a rising share of productive industrial activities, has opened avenues for economic diversification and has increased the competitiveness and integration of these countries' transformed products into global value chains. The employment shift from agriculture to industry and services, a feature of structural transformation, is occurring in Central, East, Southern and West Africa but at a slower pace as compared to the successfully transformed economies of East Asia. In addition, people who do leave the agricultural sector are usually absorbed into the services sector; as a result, between 2000 and 2013, employment in the industrial sector remained stagnant at around 8.4 per cent of the working population (see figure 14). This hampers economic and employment prospects as most services jobs are informal and characterized by low productivity, low wages and poor working conditions. However, the increase in the number of jobs in high-end services (such as ICT and financial services) is a positive development that needs to be encouraged across the continent (African Development Bank, 2011).

Figure 14
Employment by sector in selected regions, 2000–2013 (percentage change)



Source: Calculations based on Key Indicators of the Labour Market (KILM) (ILO, 2014).

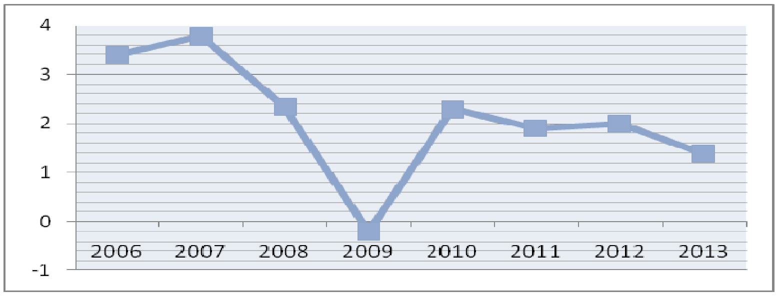
I. Weak labour productivity is curtailing Africa's employment prospects

65. One of the major challenges for meaningful job creation in Africa is low labour productivity, particularly in agriculture, which reinforces the persistence of the continent's food insecurity problem. In 2012–2013, labour productivity in Africa grew by just 1.4 per cent, slower than in any other region (see figure 15). Productivity gains are still held back by too little investment in factors of production, including human resources. In a selected group of African countries with data (including Morocco, South Africa, Uganda and the United Republic of Tanzania), about 1 in 10 workers are underemployed.[2] The skills of the workforce are underused, with consequences for current and future productivity. Investment in education linked to technology and innovation, and in

[2] The indicator refers to underemployment as a percentage of the total labour force or of total employment.

developing skills that boost productivity and meet labour-market needs, is inadequate. One successful example is the human resource strategy of the Government of Cabo Verde, which ties tertiary education to labour demand, particularly in the services and tourism sectors of the country's economy (African Development Bank, 2011). High-end productivity shifts to the services sector have been created through the production of knowledge-driven services driven by innovation and entrepreneurship, and building on e-governance tools.

Figure 15
Labour productivity growth in Central, East, Southern and West Africa (percentage change)

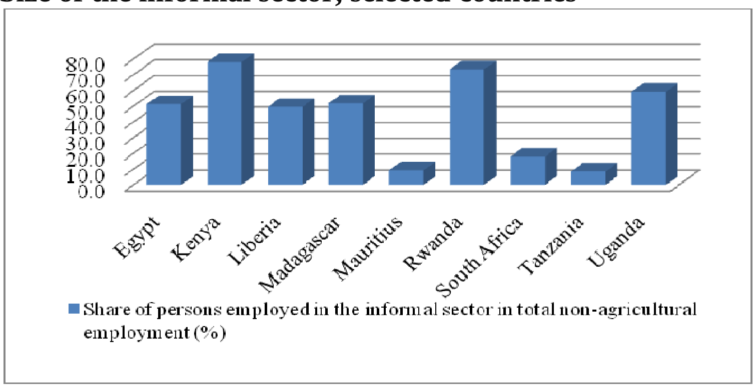


Source: ECA calculations based on KILM (ILO, 2014).

J. Informal sector continues to drive jobs creation

66. As the formal sector –both public and private – cannot absorb the growing tide of job seekers, informal employment drives job creation in most African countries (see figure 16). In 2012, 77.2 per cent of workers in Central, East, Southern and West Africa were estimated to be either self-employed or contributing family workers (ILO, 2014).

Figure 16
Size of the informal sector, selected countries



Source: Calculations based on KILM (ILO 2014).

67. In terms of gender, informal trade is the most important source of employment among self-employed women in Central, East, Southern and West Africa, at 60 per cent of non-agricultural employment. Informal cross-border trade in the Southern African Development Community (SADC) is worth $17.6 billion a year and accounts for 30–40 per cent of intra-SADC trade. Some 70 per cent of the cross-border traders are women (ILO, 2004).

68. Although informality is mainly used as a coping mechanism, there is a great deal of scope to harness the potential of the informal sector in Africa through targeted enabling policies that expand

social protection systems, tax incentives, skill development programmes, technology transfer and infrastructure investment. Some countries have already launched such programmes. At present, the social protection coverage of informal workers in Africa is very limited, at around 10 per cent, compared to over 50 per cent in Latin America and the Caribbean.

V. Policy implications

69. African countries need to build on the progress that has been made so far and continue establishing robust institutions that maintain and improve the business environment, economic governance and macroeconomic management, with a view to increasing resilience against external shocks such as declining capital inflows resulting from tighter monetary policies in developed economies; declining growth in emerging economies, such as China; and economic fragility in the eurozone.

70. Strategies need to be developed to close the human capital gap, overcome the physical infrastructure deficit, address the manufacturing deficit in Africa’s growth and reposition Africa in global value chains through facilitated trade in intermediate goods and services. A selective trade policy framework, with strategic sequencing, can be used to maximize the benefits of trade for industrialization.

71. These efforts call for innovative financing mechanisms to direct savings into industry (particularly manufacturing) and mechanized agriculture. Remittances, the largest and most stable source of external financing, must be leveraged. The first step would be to lower the cost of sending money to Africa. On average, sending $200 to Africa costs $23.8 (11.9 per cent of the total) (World Bank and European Commission, 2013). Governments also should make better use of pension funds and private equity. Governments with large international reserves should not only save them to build buffers against exogenous shocks but also use them for development, especially in growth-enhancing sectors.

72. Although Africa’s growth has been robust and resilient, the continent is still not on the inclusive development trajectory necessary to translate growth into employment opportunities and to reduce poverty and inequality. African countries need to embark on strategies centred around social development, because human capital is central to innovation, industrialization and structural transformation. Education should place an emphasis on studies aimed at enhancing the transformation process in areas where Africa has a comparative advantage, such as the processing of its natural resource endowments. Incentives should be provided to encourage children and young people to study sciences and engineering across all levels of education.

73. Given the large informal sector involved in trade and its contribution to GDP, there is need for: labour market policies (to help in developing human skills and adaptability, and to facilitate mobility across occupations, companies, industries and countries); an efficient regulatory framework, while keeping the burden to the minimum, fostering competition and helping to ensure market openness; social protection mechanisms; fiscal and credit incentives for private sector development, mainly to small- and medium-sized enterprises; and better infrastructure and increased access to public goods, services and technology for informal enterprises.

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