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Current Issues
Emerging markets

Sub-Saharan Africa

A bright spot in spite of key challenges

July 15, 2013

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Sub-Saharan Africa (SSA) is growing fast with annual real GDP growth of over 5% in the last decade, second only to developing Asia. Medium-term growth will remain robust, on the back of a recovering global economy, still high commodity prices and investment in productive capacity. Annual growth projections until 2015 are close to 6%, higher if one excludes South Africa.

Robust growth is increasingly spread over countries. Not confined to commodity exporters, it also applies to countries not categorised as rich in raw materials, such as Ethiopia and Rwanda. East and West Africa are the fastest-growing subregions.

Improved macroeconomic management and increased political stability have underpinned strong public spending, especially on infrastructure and services. Investment has been an important driver of growth in much of SSA, although it remains low in a developing world context. FDI to SSA is strongly increasing.

A large consumer market is emerging. Consumer demand has grown rapidly in recent years, on the back of solid real income growth. Many SSA countries are expected to reach middle-income status in coming years.

Social development is improving but remains low and uneven. In spite of clear progress in health and education, the poverty rate is still close to 50% and around 30% of the population is undernourished. Inequalities remain striking.

SSA's population is growing fast, becoming more urban and experiencing a youth surge. On the positive side, this means lower dependency ratios, a major rise in demand and urban centres becoming potential hubs of innovation and employment. However, job creation is a particular challenge, in a context of skill deficits. Structural transformation has started, more through services than manufacturing.

Managing resource wealth is key to sustainable growth in SSA. Despite recent headwinds in commodities markets, new discoveries and further exploration promise strong revenue flows. They provide SSA with an opportunity to create employment and inclusive growth through value addition in all sectors.

The business environment remains challenging in SSA but the region is increasingly attractive for investors. Surveyed companies with an established business presence in SSA are happy with their situation. Investments in infrastructure/logistics and education, economic diversification, market reforms and improved governance are critical for SSA's long-term success.

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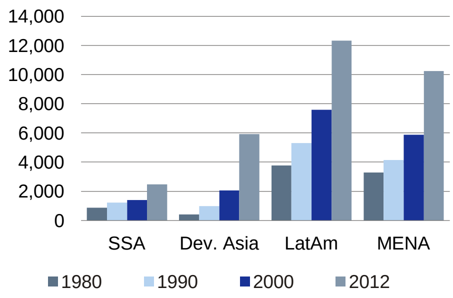
* The author would like to thank Kolja Johannsen for research assistance.

Sub-Saharan Africa: A bright spot in spite of key challenges

SSA still poor... 1

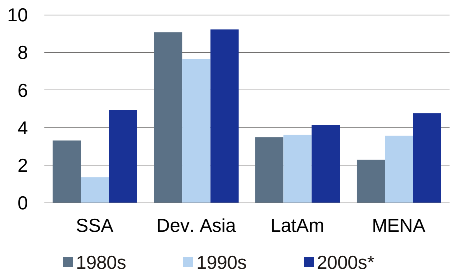
GDP per capita, PPP



Sources: IMF, DB Research

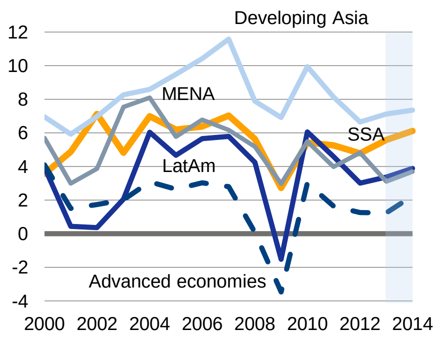
... but GDP per capita is picking up 2

Compound annual growth rate (CAGR), % (PPP)



* Includes 2011 and 2012.
Sources: IMF, DB Research

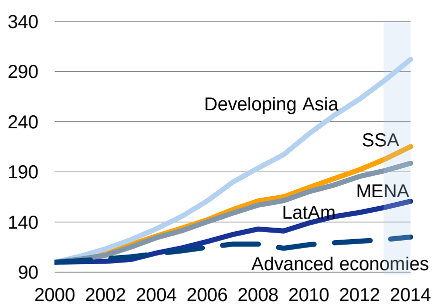
GDP growth by regions, % 3



Sources: IMF, DB Research

Second only to developing Asia 4

Cumulative GDP growth, index 2000=100



Sources: IMF, DB Research

Sub-Saharan Africa (SSA), 12 % of the world's total population, 2% of world GDP: a glass half-empty or half-full? For decades, the answer to this question seemed obvious. Africa was clearly falling behind in the development race. In the early 1980s, SSA's GDP per capita (valued at purchasing power parity) was twice that of developing Asia, but only ten years later developing Asia had almost caught up and its GDP per capita is now more than double that of SSA (see chart 1). It was not only Asia. Other developing regions grew faster than SSA: Latin America during the 1980s and 1990s, and MENA during the 1990s (see chart 2), contrary to what could be expected from the income convergence theory.

However, at the start of this century, SSA reversed course and started to grow at an accelerated pace. Since 2000, GDP per capita has grown by almost 5% per year, compared with 2.4% in the two preceding decades. This is faster than any other region except developing Asia. Most importantly, growth is expected to remain at that level for the next five to ten years. At the same time, the region does face key challenges: a still fragile economy, social inequalities, weak institutions, demographic challenges, infrastructure deficit and conflicts.

A. Impressive economic growth

SSA's growth momentum has been driven by growing infrastructure development and continued robust domestic demand – in a context of improved political and macroeconomic stability, business-friendly microeconomic reforms, still high commodity prices, new resource discoveries and large investment inflows. Growth is not confined to countries rich in raw materials.

A decade of strong and sustained economic growth set to continue

Over the past ten years, SSA's GDP grew at over 5 percent annually, in 2012 at 4.8% (see chart 3) – or 5.8% if one excludes South Africa, the continent's largest economy which was hit severely by the global economic downturn. This is higher than the emerging markets and developing economies' average of 5.1%. Since 2000, SSA's economic size has doubled in real terms and almost quadrupled in nominal USD terms (see chart 4).

SSA's nominal GDP is estimated at USD 1.3 trillion for 2012, comparable to Spain, and is expected to reach USD 2 trillion over the next five years. Indeed, medium-term growth will remain robust, on the back of a recovering global economy, still high commodity prices and investment in the region's productive capacity. Annual growth projections until 2015 are close to 6% – above 6% excluding South Africa.[1]

Robust growth increasingly spread over countries

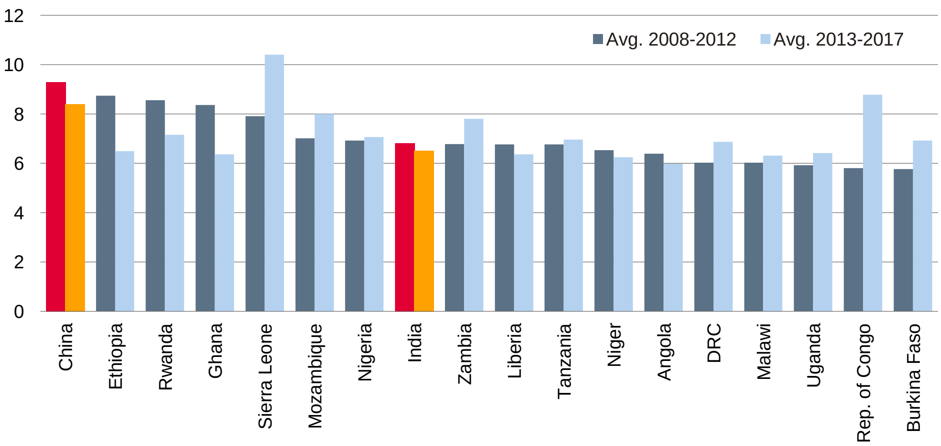
The African growth story has become more spread across countries, too: while in the early 1980s South Africa accounted for almost 40% of SSA's GDP, it now represents around 25%. Countries like Angola, Mozambique or Ethiopia reached average GDP growth rates of 8% and more over the last decade. This is comparable to the growth performance of India and China, among the fastest in the world (see chart 5). Over a quarter of SSA countries grew at 7% or more in 2012 and 6 of them outperformed China (7.8%): (in descending order) Sierra Leone, Niger, Cote d'Ivoire, Angola, Liberia and Burkina Faso.

[1] Downside risks for this forecast include prolonged sluggish growth in the eurozone, a slowdown in major market economies and a sharper-than-expected decrease in commodity prices, although these are not expected to have a drastic effect on SSA's growth.

Commodity exporters have benefited from the post-2009 boom in commodity prices. Oil producers such as Angola and Nigeria have flourished as well as exporters of raw materials such as Sierra Leone (diamonds), Zambia (copper) and Tanzania (gold). Countries not categorised as rich in raw materials are on a very robust growth path as well, for instance Ethiopia and Rwanda. Based on IMF forecasts for the next five years, a few countries will join the group of fastest-growing economies, such as Cote d'Ivoire, Gabon, Chad and Burkina Faso. In fact, 13 of the 25 fastest-growing economies in the world will be in SSA (see chart 6).

Fastest-growing SSA economies over the last 5 years 5

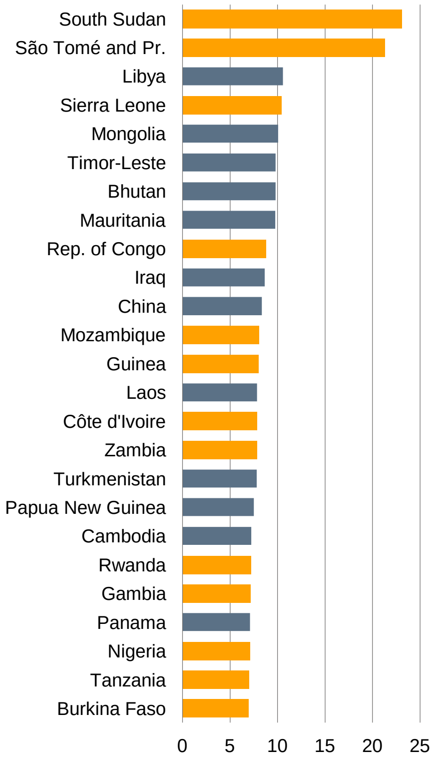
Real GDP growth, % yoy



Sources: IMF, DB Research

World's fastest growing 6

GDP growth, %, 2013-2017



Sources: IMF, DB Research

Regional differences

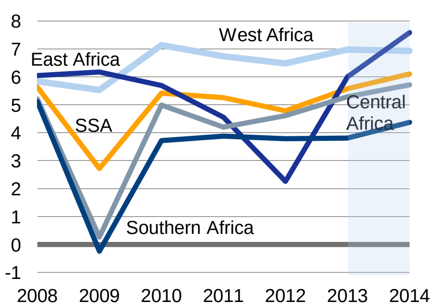
Among the four subregions, West Africa has recently recorded the highest growth followed by East Africa (excluding Sudan and South Sudan), Central Africa and Southern Africa (see chart 7). West and East Africa are still expected to be the fastest growing in 2013 (7% and 6% respectively). West Africa (6.5% in 2012) will continue to benefit from commodities – especially oil and minerals as Ghana, Niger and Sierra Leone exploit new discoveries – and from increased stability in Cote d'Ivoire. Nigeria, the continent's second-largest economy, is set to experience renewed growth (7.2% in 2013) after a slight slowdown in 2012 – reflecting receding fiscal stimulus and slowing oil investments on security concerns across the Niger Delta and in the north of the country. Political instability in Guinea-Bissau and Mali exert downward pressure on the subregion's growth.

Growth in East Africa (5.7% in 2012, excluding Sudan and South Sudan, 2.3% otherwise) is expected to be boosted by increasing economic diversity, rising agricultural output and exports, as well as new natural resource discoveries. Ethiopia, Kenya, Mozambique, Rwanda, Tanzania and Uganda are among the fastest-growing SSA countries.

Central Africa is forecast to sustain moderate growth (4.6% in 2012, 5.3% in 2013 – excluding Sudan and South Sudan) with robust commodity production and export demand. This subregion relies heavily on output of primary commodities and extractive industries – making job creation and inclusive growth a major challenge – for instance oil in Chad, Cameroon, Republic of Congo, Equatorial Guinea and Gabon, diamonds in Central African Republic

Regional differences 7

Real GDP growth yoy, %



Sources: IMF, DB Research

and Democratic Republic of Congo (DRC) and cobalt in DRC (accounting for around half of world production).

Growth in Southern Africa will be the lowest in the region: 3.8% in both 2012 and 2013 – but 6.3% in 2012 and 5.8% in 2013 if one excludes South Africa – on the back of manufacturing and a more favourable international environment. Angola (6 to 7% in 2013-14) and Mozambique (around 8%) are the bright spots of the subregion, Angola on increased oil production and investment in natural gas and Mozambique, which became a coal exporter in 2011, on larger foreign direct investment (FDI).

Improved macroeconomic stability and strong public spending

The improvement of macroeconomic policies across SSA, together with its direct impact on investor and consumer confidence, has been a significant factor in SSA's renaissance. Growth in SSA continues to benefit from improved macroeconomic management which has increased policy space for public spending, especially on infrastructure and public services.

Public finances have improved in most SSA countries (see table 8) as a result of debt relief, prudent fiscal policy and strong GDP growth[2]. Public debt-to-GDP ratios are relatively low, at 38% on average for SSA in 2012 (vs 31% in 2008) – 34% for oil exporters versus 43% for oil importers according to the IMF. However, fiscal balances are mostly negative in SSA, although this is not the case in countries like Angola[3], Botswana, Gabon and Nigeria. Fiscal balances deteriorated in 2012 in many SSA countries, due to sluggish economic activity (like South Africa) or pre-election spending overruns (like in Ghana). In many oil exporters like Angola, sharp increases in public spending are resulting in a decline in budget surpluses.

SSA: Macroeconomic indicators 8

	2004-08	2010	2011	2012	2013	2014
Fiscal balance (% of GDP)	1.9	-3.9	-1.3	-1.7	-2.7	-2.9
Excluding oil exporters	-0.7	-4.6	-3.7	-4.5	-4.1	-3.2
Current account balance (% of GDP)	0.6	-1.3	-1.7	-2.8	-3.5	-4.1
Excluding oil exporters	-5.1	-4.7	-5	-7.9	-7.8	-7.9
International reserve coverage (months of import)	4.8	4.2	4.5	4.7	4.9	5.1
Inflation, end-of-period, (% change)	8.8	7.2	10.1	7.9	6.9	5.8

Source: IMF

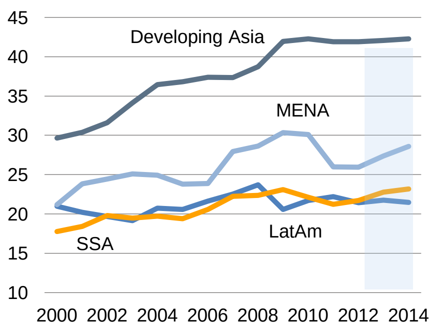
Current account deficits widened in much of SSA in 2012, due to sluggish exports from several middle-income countries. Oil exporters typically recorded improved trade and current account positions. Surging current account deficits may become a concern in some low-income and fragile countries although they coincide with large inflows of foreign direct investment, as in Mozambique (with a current account deficit of 26%) and Sierra Leone (21%). International reserves have increased in SSA on average, up to close to 5 months of imports.

[2] For specifics on individual SSA countries, please see Frontier country reports at www.dbresearch.com/emergingmarkets.
[3] See also "Oil economy on a diversification path". Schaffnit-Chatterjee. DB Research. June 2013.

Inflation in SSA has been dropping since 2011 and is forecast by the IMF to keep to its downward trend. This slowdown in inflation reflects several factors including moderating world food and fuel prices, a tightening of monetary policy in countries with high inflation, as well as improved weather conditions in East Africa and the arid Sahel region of West Africa, which have lowered food production costs. Some countries have experienced a drastic fall in inflation (over 8 percentage points in 2012), like Ethiopia, Kenya, Tanzania and Uganda.

Investment has risen but remains low 9

% GDP



Sources: IMF, DB Research

Investment: Key driver of growth across sectors and countries

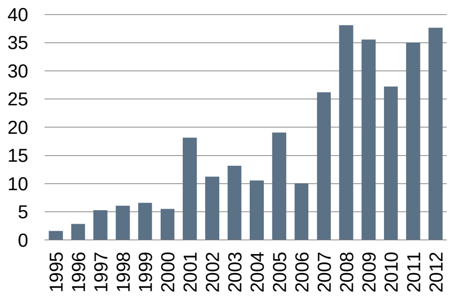
Investment has been an important driver of growth in much of SSA, with investment-to-GDP ratios increasing on average by 0.5 percentage points per year over the past decade. Both foreign and domestic as well as private and public investments have increased. However, at 22%, the investment-to-GDP ratio in SSA is the lowest among developing regions together with Latin America (see chart 9) and similar to levels observed in China in the early 1960s and India in the early 1980s. This suggests that there is room for further investment-driven productivity increases in SSA.

Net private capital flows to the region reached a record of USD 54 bn in 2012 – an increase of 3.3% – whereas developing countries overall experienced an 8.8% decline in capital flows due to a weaker global economic environment[4].

Strongly increasing FDI in extractive industry and consumer markets

Strongly increasing FDI 10

Net FDI inflows to SSA, USD billion



Sources: UNCTAD, World Bank, DB Research

Foreign direct investment dominates capital inflows into SSA – partly because the region is rich in natural resources. It is also because other forms of capital flows to the region are limited by less developed, though growing, capital markets and a banking sector less integrated with global financial markets. SSA has attracted increasing net FDI in the last fifteen years (see chart 10)[5]. In 2012, net FDI to SSA increased by 5.5% even though it fell by 6.6% for developing countries as a whole. This has been in line with rising commodity prices, new mineral discoveries and the longer time horizon of investment decisions in the extractive industry, which results in little sensitivity to short-term shifts in market sentiment.

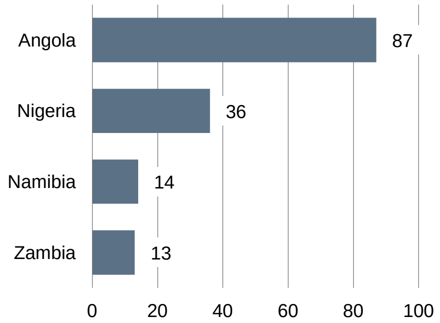
South Africa and Nigeria are the main FDI recipients but increasing shares are going to fast-growing countries such as Angola, Ghana, Kenya, Mozambique, Tanzania, Uganda and Zambia. At the same time, political instability and regulatory uncertainty are puting downward pressure on investment flows to some countries, e.g. Guinea.

FDI flows to SSA are not only directed towards its extractive industry, but also increasingly towards consumer-oriented manufacturing and services. In an environment of improved macroeconomic conditions and increased political stability, FDI is flowing towards infrastructure-related service subsectors such as construction, transportation, electricity, telecommunication and water but also retail and banking, in order to respond to new consumer needs associated with rising incomes[6]. Indeed, in some of the larger economies with a growing middle class such as Nigeria, South Africa, Angola, Kenya and Ghana, the consumer sector is rapidly expanding even though it is still small[7].

4 Word Bank. Africa's Pulse. April 2013.
5 UNCTAD uses a broad definition of FDI, including cross-border mergers and acquisitions as well as equity investments.
6 UNCTAD. World Investment Report. 2013.
7 Projections of consumption growth in Africa for 2011-16 indicate that 40% of the growth is likely to come from households that earn more than USD 20,000 a year – representing 1 to 2% of all households. McKinsey (2012). "The rise of the African consumer".

High inward FDI rates of return 11

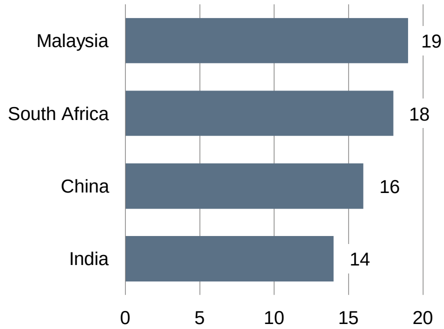
%, 2011



Sources: UNCTAD, IMF, DB Research

Large FDI from emerging countries 12

FDI stock in Africa in 2011, USD billion



Sources: UNCTAD, FDI

The rates of return for inward FDI to Africa are among the highest in developing economies (together with East/South-East Asia) at 9.3% in 2011, compared to 8.4% for developing economies, 13% for transition economies and 4.8% for developed economies. With natural resources, extractive and processing industries consistently contributing to higher rates of return, four SSA countries were among the top 20 economies with highest inward FDI rates of return in 2011 (see chart 11).

Higher share of FDI flowing into SSA from emerging markets

The highest FDI inflows in Africa in 2011 originated in France and the US, followed by Malaysia. The largest stocks of investments are from France, the US, the UK, Malaysia, South Africa, China and India (see chart 12). Indeed, FDI into SSA is increasingly flowing from emerging and developing economies. *Malaysia* (which sent 24% of its outward FDI to Africa in 2011, as opposed to 4% for the BRICS) is particularly active in agribusiness in both East and West Africa and finance in Mauritius. The fifth-largest holder of FDI stock in Africa in 2011, *South Africa* mostly reinvests earnings in the private non-banking sector. The largest share of its outward FDI stock in Africa goes to Mauritius while one-fourth of the stock is concentrated in Nigeria, Mozambique and Zimbabwe. The leading recipient of *China*'s FDI in Africa is South Africa, followed by Sudan, Nigeria and Zambia. In addition to resource-seeking FDI, these countries attract Chinese FDI in manufacturing. The bulk of *India*'s FDI in Africa is in Mauritius although India's involvement in the rest of Africa is rising, e.g. in Cote d'Ivoire, Ethiopia, Senegal and Sudan.

Intra-Africa investment, comparatively small, is increasing and tends to go to services and manufacturing. Outward FDI flows from Africa (including North Africa) nearly tripled in 2012 to USD 14 bn (from USD 5 bn in the previous year) with USD 4.4 bn from South African companies active in the mining, wholesale and health-care industries and also outflows from Angola, Nigeria, DRC, etc.[8]

In terms of new FDI projects for the period 2003-2012, the top investors were the US (516 projects), the UK (456), France (398), India (237), South Africa (235), UAE (210), Spain (194), Germany (173), China (152) and Portugal (137).[9]

FDI prospects are strong

Increased investment is likely to remain a major driver of growth over the medium term. Foreign investment is expected to remain strong in agriculture, mining, and oil and gas – on the back of new oil and gas discoveries, mine expansions or constructions in a context of still high, though moderating, commodity prices – as well as hotels and restaurants.[10]

Investments in infrastructure critical for competitiveness and growth

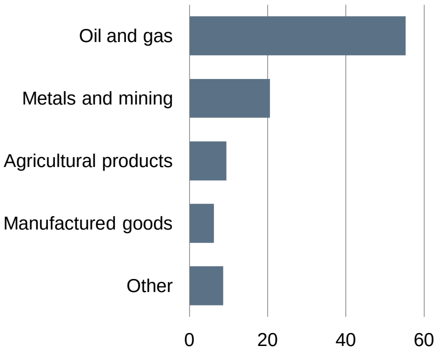
Governments in SSA are spending to reduce infrastructural weaknesses which inhibit competitiveness and growth. Infrastructural shortcomings may be depressing firm-level productivity by 40% in some SSA countries and investment in infrastructure can potentially boost growth rates in the region by 2 percentage points[11] (see also last section on Improving the business environment).

[8] UNCTAD. World Investment Report 2013.
[9] fDi Markets. Ernst & Young.
[10] UNCTAD. World Investment Report 2013.
[11] World Bank. Global Economic Prospects. January 2013.

Sub-Saharan Africa: A bright spot in spite of key challenges

Export growth mostly from oil and gas 13

Contribution to SSA growth, %



Sources: Comtrade, World Bank, DB Research

Continued investment in infrastructure will be critical to maintaining and strengthening growth over the medium term. Public infrastructure programmes may in some countries be financed by accessing international capital markets. Rwanda and Nigeria have recently issued eurobonds and Angola, Kenya, Rwanda and Tanzania have expressed interest in raising international bonds.

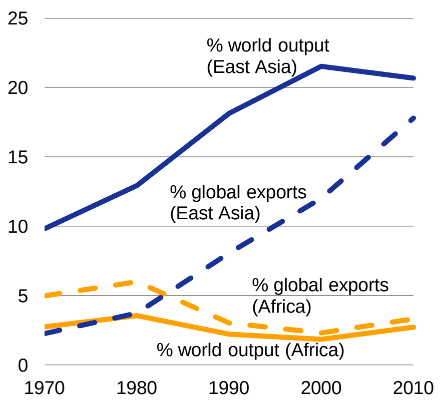
Exports underpin SSA's economic growth

Robust export growth has underpinned economic growth in SSA and has been driven mostly by natural resources (see chart 13). Between 2000 and 2011, total exports increased from USD 100 billion to USD 420 billion. The latter represents around 30% of SSA GDP and 2% of world exports (see chart 14). Resources (including oil, ores, base metals and gold) account for three quarters of total exports from SSA.

The main export destinations from SSA countries are the EU, China and the US. The main EU destinations are the UK, the Netherlands, Spain, Germany and France (see chart 15).

Exports lag behind 14

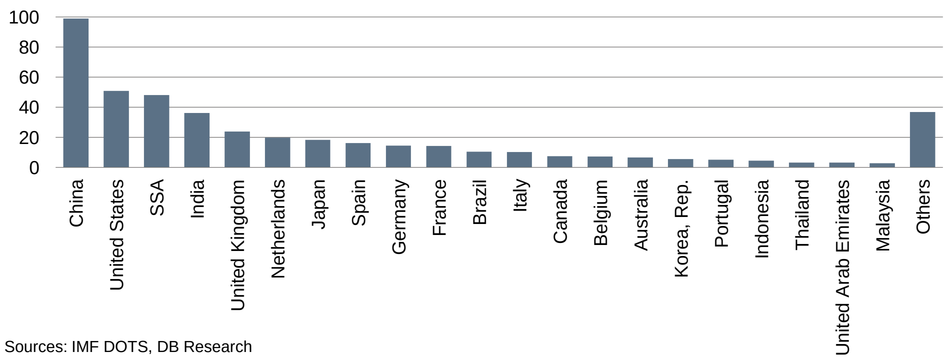
Shares in global output and exports, %



Sources: World Bank, DB Research

Exports from SSA by country, 2012 15

USD billion



Sources: IMF DOTS, DB Research

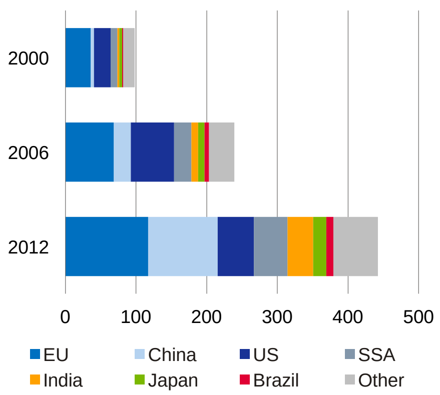
Increasing South-South and intra-regional trade

Since 2000, exports to emerging markets (including China, Brazil and India) and within the region have grown faster than those to developed markets (see chart 16). Total exports to China, Brazil and India were larger than those to the EU in 2011. Export diversification varies with the destinations: intra-regional exports are most diversified, with manufactured goods and agricultural products accounting for 46% of total exports whereas they represent only 5% of total exports to Brazil, India and China, 10% to the US and 30% to the EU[12]. With regard to services exports, tourism is an important driver of growth in the region, both in traditional destinations (Cape Verde, Kenya, Mauritius, Seychelles) and in newer destinations such as Rwanda. Sierra Leone and South Africa also recorded strong growth in tourist arrivals in 2012.

Exports from SSA are likely to rapidly increase further in the next few years. This partly reflects the strengthening of global demand expected in 2013 and beyond, but also productivity growth in the region and new mineral exports from several countries (e.g. Burkina Faso, Mozambique, Niger, Cameroon, Gabon and Sierra Leone).

Exports from SSA 16

USD billion



Sources: IMF DOTS, DB Research

[12] World Bank. Africa Pulse. April 2013.

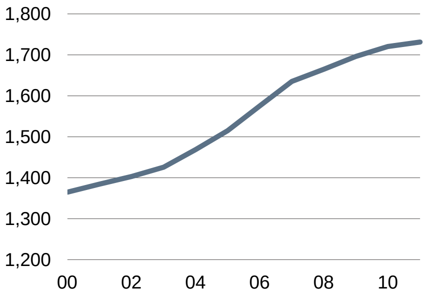
Increasing consumer spending

Consumer demand has grown rapidly in recent years, on the back of solid real income growth – averaging 2.3% per capita p.a. Consumer spending accounts for more than 60% of SSA's GDP. Consumption growth has been boosted by various factors: declining inflation, improved access to credit (for instance in Angola, Ghana, Mozambique, South Africa and Zambia), lower interest rates, a weather-driven rebound of revenues in the agricultural sector and steady remittance inflows (USD 31 bn per year in 2011 and 2012), equivalent to 2.5% of SSA's GDP [13].

Rising income per capita

Up from a low base 17

Income per capita, USD, PPP



Sources: IMF, DB Research

SSA has seen major achievements in terms of income per capita (see chart 17) – even though starting from a low base. During the five years preceding the global financial crisis, from 2003 to 2008, real income per capita grew 3.2% a year. It is now on average USD 1,731 for SSA, compared to USD 9,147 for East Asia, USD 10,147 for Latin America and USD 10,733 for developing Europe and Central Asia (PPP, constant 2005 international USD).

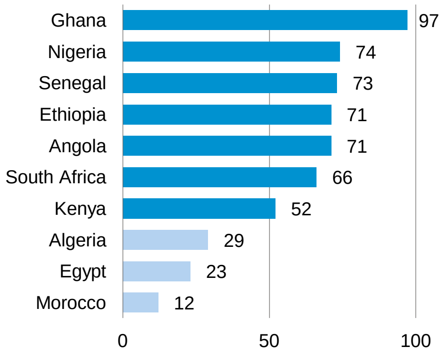
Between 2000 and 2011, average incomes tripled in Equatorial Guinea, doubled in Angola and rose by one-third or more in 10 SSA countries. Most of the resource-rich countries benefited from increases in commodity prices. Over the past decade, Cameroon, Ghana, Nigeria and Zambia crossed the threshold from low-income to lower middle-income status (per capita income between USD 1,026 and USD 4,035). If stable countries continue to grow at the same rate as the last decade's, most will reach middle-income status by 2025. Four countries (Angola, Gabon, Nambia and South Africa) are in the upper middle-income group (USD 4,036-USD 12,475) and four countries (Botswana, Equatorial Guinea, Mauritius and Seychelles) are classified as high-income countries.

Many net commodity-importing economies also grew faster than their population. For instance, gross national income per capita increased significantly in Ethiopia, Rwanda and Uganda.

Growing consumer markets

Optimistic Sub-Saharan Africa 18

Share of people who feel that their household will be better off in two years, % (2011 and 2012)



Sources: African Consumer Insights Center, McKinsey

Private consumption in Africa rose by USD 568 billion (in nominal terms) from 2000 to 2010 and is higher than in India or Russia[14]. From 2012 to 2020, consumer-facing industries are expected to grow by USD 410 billion, with apparel, consumer goods and food accounting for USD 185 billion[15]. Indeed, more than half of African households are forecast to have discretionary income by 2020 – almost 130 million compared to 85 million today. And Africans from SSA are particularly optimistic about their future: the vast majority of them expect their households to be better off in two years (see chart 18).

New consumer markets are emerging in SSA, largely for basic goods and services. The telecommunications, banking, retail and construction sectors are booming in various countries. The increased demand for capital goods to meet infrastructure and other investment needs, growing demand for oil and rising per capita income should further boost demand for consumer durables and other imports.

[13] World Bank. Africa Pulse. April 2013.
[14] IHS Global Insight.
[15] "Lions on the move". McKinsey. June 2010.

The African ICT revolution

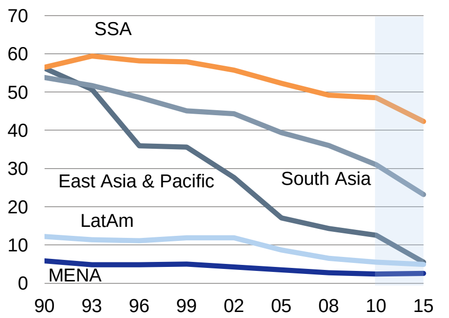
In a recent survey by McKinsey[16], over 50% of urban Africans reported they had accessed the internet in the previous four weeks, similarly to figures for urban China and Brazil. Over half (56%) of urban consumers own internet-capable mobile devices and a third of them accesses the internet on a daily basis. In Kenya, internet penetration reaches 70%, driven by affordable mobile broadband and high penetration (95%) of internet-capable mobile devices.

The growth in internet usage as well as mobile telecommunications has been phenomenal in Africa, propelling Africa to become the world's second-largest mobile market behind Asia and its fastest-growing one. It is expected that by 2015 there will be more people in SSA with access to mobile networks than access to electricity.[17] Information and communications technologies (ICTs) are growing on average at 20% per year in Kenya, accounting for 5% of its GDP in 2010. Other innovation-oriented sectors include agricultural value chains (seeds, post-harvest technologies), energy, water and manufacturing[18].

The booming growth in mobile telephony in Africa has already improved the lives of millions of people – privately and at work. ICTs are transforming various industries. Mobile banking provides many SSA unbanked households with various financial services, such as saving, paying bills and transferring money. It allows farmers to access much needed agricultural information regarding weather conditions or market developments. ICTs can also make a fundamental difference to health systems (e.g. increasing the availability of equipment and supplies and educating communities about disease prevention and treatment). They have given citizens a stronger voice and are increasingly being used to push for social accountability, transparency and governance, too.

Poverty rates continue to fall 19

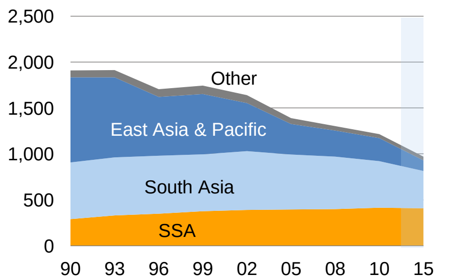
%



Sources: World Bank, DB Research

Fewer people live in extreme poverty globally, but not in SSA 20

Number of people, million



Sources: World Bank, DB Research

B. Social development improves but remains low

Despite Africa's growth renaissance, and major improvements in education and health over the past decade, SSA has not performed well in terms of poverty and malnutrition. The region lags in achieving all the Millennium Development Goals but some countries have fast-tracked progress towards poverty, hunger, education and health.

Poverty rate in SSA is still close to 50%

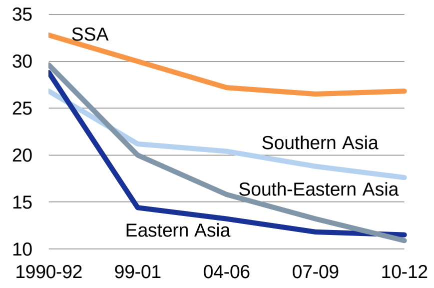
The poverty rate (share of the population living on less than USD 1.25 a day) is close to 50% in SSA and has changed little over the last decade (48% in 2012 little down from 52% in 1981 and 56% in 1990). In contrast, East Asia as well as South Asia have experienced a remarkable poverty reduction (see chart 19). The number of people living in extreme poverty is declining globally but SSA is the only region where it is increasing (see chart 20). In terms of intensity of poverty, countries with the highest intensity of deprivation include Ethiopia, Mozambique, Burkina Faso and Senegal.[19]

Progress on the poverty front is uneven across countries. Some rapidly growing countries, such as Burkina Faso, Mozambique and Tanzania, have barely

16 "The rise of the African consumer". McKinsey. October 2012.
17 Mobile Africa Report. Mobile Monday. March 2012.
18 According to NEPAD (New Partnership for Africa's Development), African Ministerial Council of Science and Technology.
19 Based on the Multidimensional Poverty Index which looks at overlapping deprivation in health, education and standard of living (Human Development Report 2013).

Hunger persists in SSA 21

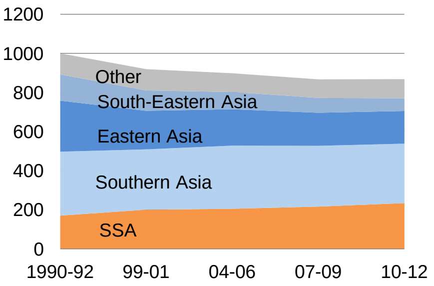
Prevalence of hunger, % population



Sources: FAO, DB Research

Fewer hungry globally, not in SSA 22

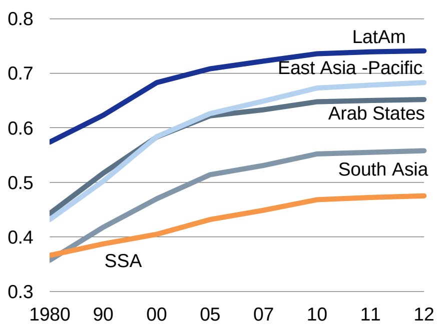
Number of undernourished, million



Sources: FAO, DB Research

HDI improving from a low base 23

HDI Index



Based on fewer than half the countries in each region.

Sources: UNDP, DB Research

managed to reduce their poverty rates. In contrast, Ethiopia experienced a dramatic reduction in its poverty rate, from 56% in 2000 to 31% in 2010.

Around 30% of the SSA population is undernourished

Around 30% of the population in SSA is undernourished (15% in Asia-Pacific) and the rate of progress in the reduction of undernourishment has been higher in Asia and in Latin America than in SSA (see chart 21). The absolute number of people who are undernourished is decreasing in most regions but increasing in SSA (see chart 22).[20]

The undernourishment associated with missing micronutrients is also particularly severe in SSA. A recent report presenting the "Global Hidden Hunger Index" highlights that the twenty countries which are most affected by multiple micronutrient deficiencies are all in SSA except for India and Afghanistan[21]. This has wide-ranging implications for health and development.

The absolute number of undernourished children has risen in SSA over the past two decades and is expected to rise further – this both in terms of stunted growth (chronic malnutrition) and underweight (acute malnutrition). The situation is of particular concern in East and West Africa.

Some progress in the Human Development Index

Although improving every year since the 1980s (see chart 23), SSA scores low in all three dimensions of the UN Human Development Index (HDI) – health, education and income. In 2012, the HDI for SSA (0.475) was about a third below the global HDI (0.694). Quite noteworthy is the contrast with South Asia, which had a similar HDI value to SSA in 1980 (around 0.36) and had reached 0.56 in 2012.

Of 46 SSA countries, only two (Mauritius and Seychelles) are in the very high or high HDI category respectively, and only eight (Botswana, Cape Verde, Equatorial Guinea, Gabon, Ghana, Namibia, South Africa and Swaziland) are in the medium HDI category. Among the 30 countries ranked at the bottom of the HDI scale, only Afghanistan, Haiti and Yemen are outside SSA.

However, SSA's progress in the HDI has been significant in the last 10 years and nine of the ten countries with the largest gains overall are in SSA, for instance Rwanda, Sierra Leone, Ethiopia, Mozambique, Tanzania, DRC and Angola.

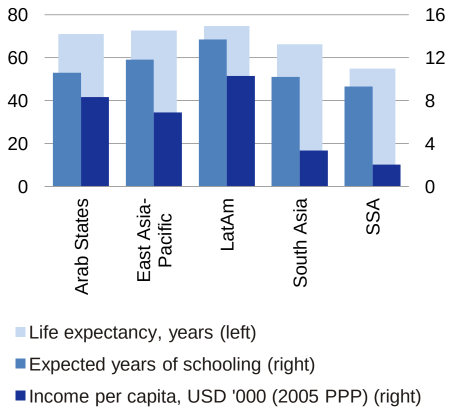
Comparing the ratio of the highest to the lowest HDI values within a region, SSA has the highest ratio. Most of the disparity arises from differences in income per capita and mean years of schooling. Progress since 1990 has been particularly rapid in Ghana, Rwanda and Uganda.[22]

Rising but still low enrolment and completion rate in primary schools

SSA has made substantial progress in terms of the completion rate for primary education. Up from 50% in 1990, it has now reached 70% but still lags behind other regions. A child spends on average 4.7 years in school in SSA – compared with 4.7 too in South Asia, 7.2 in East Asia-Pacific and 7.8 in Latin America. This figure ranges from 1.2 in Mozambique to around 9 in Botswana

[20] The State of Food Insecurity in the world. FAO, WFP and IFAD. 2012.
[21] The Global Hidden Hunger Index. Muthayya, Rah, Sugimoto, Kraemer et al. (2013), also The global food equation. Schaffnit-Chatterjee (2009).
[22] UNDP. Human Development Report. (May 2013).

HDI components: SSA behind 24



Sources: UNDP, DB Research

and the Seychelles, with Ethiopia at 2.2, Angola at 4.7, and Zambia and Kenya at around 7. SSA also scores lowest in terms of expected years of schooling (see chart 24). Many SSA children enroll in primary school but skip intermittently or drop out, especially girls since their work is needed at home. In Ethiopia, nearly all urban children complete first grade, but fewer than 80% of rural children do. Parents' education has a strong impact on school attendance[23].

The quality of education also needs improvement, as the pace of enrolment has not been matched by investment in school infrastructure. The share of primary school teachers trained to teach is only 74%. Some 37 million African children perform so poorly at basic skills that they are not much better off than those who missed school. In a few countries like Ethiopia, Nigeria and Zambia, over half of the students are not reaching the base primary school level.[24]

And even though the continent has seen a rapid enrolment increase in primary school, progress in secondary and tertiary enrolment is lagging. Respectively at 40% and 6%, it falls far behind other regions. Still, secondary-school enrolment grew by close to 50% between 2000 and 2008 after many states expanded their education programmes and removed school fees[25].

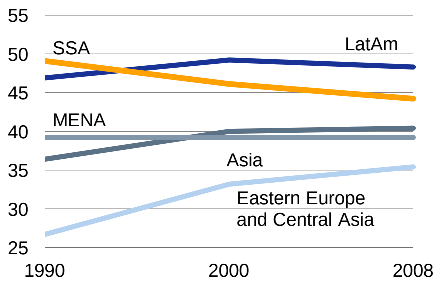
Substantial improvement in health, starting from low base

In SSA today, one out of nine children dies before their fifth birthday and fertility rates are the highest in the world – partly due to low social expenditure on education. (Countries with lower levels of education, especially where girls lack secondary education, tend to have higher fertility rates since education enhances information, changes behaviour incentives and empowers people to pursue their own preferences). Substantial progress has been made over the past four decades – at varying speeds across countries along the various indicators – but from a low base.The maternal mortality rate improved from 850 deaths per 100,000 live births in 1990 to 500 in 2010 – compared to a fall from 400 to 210 for developing countries globally. The under-5 mortality rate declined in SSA from 178 deaths per 1,000 live births in 1990 to 109 in 2011 – compared to a decrease from 87 to 51 globally over the same period.

Life expectancy stagnated at 49.5 years between 1990 and 2000, a result of the HIV and AIDS pandemic. Between 2000 and 2012, however, it increased by 5.5 years. Malaria deaths have declined by 30% over the past decade in some of the worst-affected countries and HIV infections by 74%.

Income inequality second highest in SSA 25

Gini coefficients, %



Sources: World Bank, Unicef, DB Research

Striking inequalities

In income per capita

Income inequality in SSA remains high, with Gini coefficients[26] close to 45% (see chart 25). Many resource-rich countries are highly unequal. The poorest 10% of the population account for less than 1.5% of national income in Angola, South Africa, Central African Republic and Namibia (see chart 27). In these four countries, more than 45% of national income accrues to the richest 10% of the population.

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23 World Bank. World Development Indicators 2013.
24 African Economic Outlook 2013. African Development Bank, OECD, UNDP, Economic Commission for Africa.
25 Africa Progress Report 2012. Africa Progress Panel.
26 A Gini coefficient of 0% theoretically implies perfect equality (each quintile owns the same share of national income) and one of 100% extreme inequality (where theoretically the richest household receives 100% of the national income).

There has been some improvement, however, especially during the 1990s, when Cameroon, Gabon, Guinea-Bissau, Lesotho, Malawi, Senegal and Sierra Leone reduced their Gini indices by ten or more points. The best performers between 2000 and 2008 – Burundi, Ethiopia, Lesotho, Malawi, Mali and Sierra Leone – have reduced their Gini values by two or more points[27].

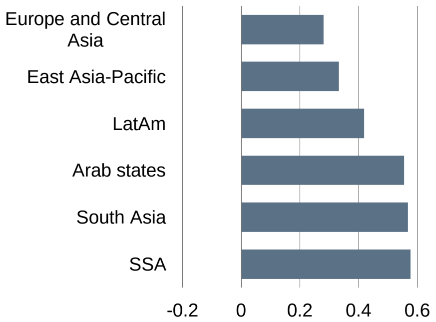
Highly skewed patterns of income distribution undermine both the pace of poverty reduction and of growth, since extreme inequality restricts productivity increases as well as market development.

In terms of health and education as well

High inequality is undermining the positive impact of economic growth and the UNDP has recently designed an Inequality Adjusted Human Development Index (IHDI) in order to gauge the level of inequality along the three basic dimensions of human development[28]. The loss in potential human development due to inequality is then derived as the percentage difference between the HDI and the IHDI. This loss is evaluated at 35% for SSA, highest among all regions – with South Asia at 29%, Latin America and the Arab States at 25%, and a world average of 23%. Compared to other regions, SSA is faring particularly poorly in terms of inequality related to life expectancy. Countries reported[29] with the highest loss in HDI due to inequality are Angola, Namibia, Nigeria, Guinea-Bissau, Central African Republic and Chad.

Gender inequality high in SSA 26

Gender Inequality Index



Sources: UNDP, DB Research

Low gender inequality also tends to be associated with higher levels of human development. The UNDP produces a composite measure reflecting inequality in achievements between women and men along the labour market (labour force participation rate), empowerment (seats in national parliament, population with at least secondary education) and reproductive health (maternal mortality rate, adolescent fertility rate) dimensions. Among world regions, SSA fares the worst on gender inequality, with South Asia and Arab states not much ahead (see chart 26). High gender inequality results from the persistence of discriminatory laws and practices which restrict women's access to opportunities, resources and power.

Inequality especially high in resource-rich countries

When one compares the ranks in income per capita and the ranks in HDI among 20 SSA resource-rich countries, 14 have a significantly lower HDI than income standing. Equatorial Guinea, Gabon and Angola have the largest difference between the two rankings (91, 40 and 38 places respectively). And the growth surge of the last decade has not resulted in a narrowing of the HDI-income gap. This applies to the various dimensions of the HDI – including education levels and life expectancy – as well as maternal mortality and child health. Today, 12 of the 25 countries in the world with highest child mortality rate are resource-rich countries. Income inequality is also particularly high in resource-rich countries (see chart 27).

The reasons why high economic growth has failed to significantly reduce poverty in resource-rich countries vary, but on the whole the following holds:

— inequitable public spending and neglect of regions and sectors with concentrated poverty (e.g. water development)

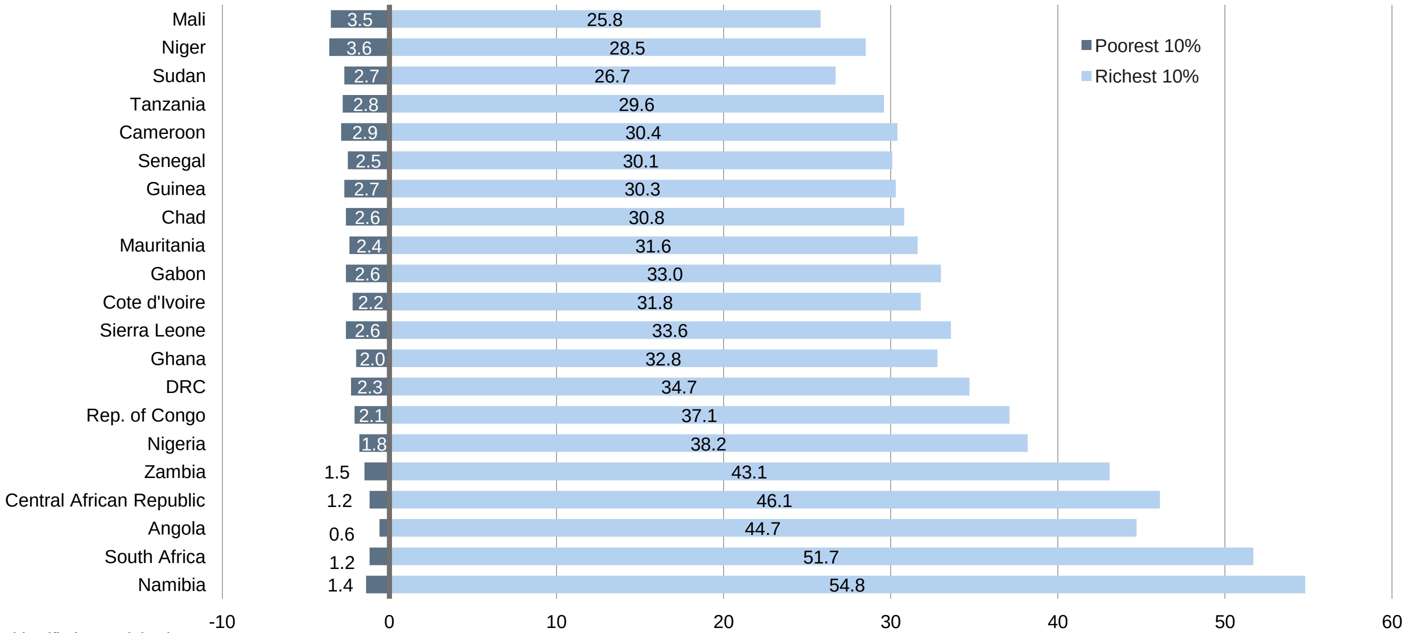
[27] World bank data as well as Ortiz and Cummins (2011). Global inequality: Beyond the bottom billion. UNICEF.
[28] UNDP. Human Development Report (May 2013).
[29] These data are not available for all countries.

— limited revenue collection due to weak management of concessions, tax evasion and corruption

— weak linkages between the resource sector and the rest of the economy.[30]

High income inequality 27

Income share of the poorest and richest 10% in Sub-Saharan Africa resource-rich countries*, %



* identified as such by the IMF

Sources: DB Research, World Bank

C. High population growth: A mixed blessing

Now estimated at 925 million, the number of Sub-Saharan Africans grew from 186 million in 1950 to 859 million in 2010, at a staggering 2.6% average annual rate. It is forecast to reach 1.2 billion in 2026 and 2 billion in 2050, when 1 in 5 people on the planet will be African – growing at a lower rate than earlier, but still the highest in the world for decades to come. This high growth rate is driven largely by high fertility rates, on average 5.2 children per woman (compared to a world average of 2.5).

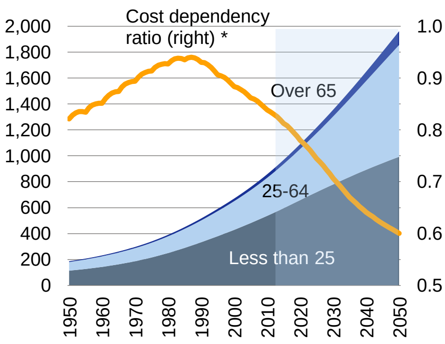
Youth surge: Half of population increase over next decade wil be less than 25

Today, 571 million Sub-Saharan Africans (62%) are under 25 years of age, 386 million (42%) are under 14 years of age. Only 3% of the population is over 65 (see chart 28).The median age is 18.6, the lowest in the world (developing world: 26.5; developed world: 39.6)[31]. With fertility rates as well as child mortality rates declining since 2000, working-age adults have become the fastest-growing population segment. The ratio of working-age people to dependants is consequently on the rise. Out of a 440 million increase in SSA's population over

[30] Africa Progress Report (2013). Africa Progress Panel.
[31] Calculations based on UN's population division (medium-fertility variant).

Population growth and youth surge 28

SSA population, million



* Ratio of number of people younger than 14 or older than 65 to the number between 15 and 65

Sources: UN, DB Research

the next decade, half will be below 25 (and one-third below 14). This could give economic growth a boost, as long as employment is available.

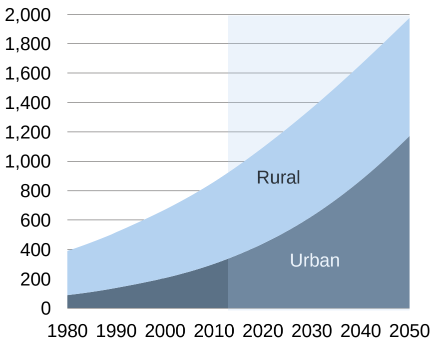
More urban: From one-third of population today to one half by 2035

Today, around one-third of SSA's population lives in urban areas. Around 2035, it may be half of it (see chart 29), as rural poverty and hope of employment push people towards the cities. In SSA like in Asia, the extremely high rural population growth rates of the 1970s and 1980s are moderating. If properly managed, urbanisation can propel social and economic growth as urban centres emerge as hubs of innovation, human networking and employment. Cities experience productivity gains through clustering, creativity and random connections, especially at a time when value generation and innovation increasingly involve breaking down silos.[32] Economies of scale also allow companies to offer low-cost goods.

On the flip side, it is also a challenge for governments to provide a fast-rising urban population with basic services such as education, health services, housing, drinkable water, electricity and waste disposal. Slums may continue to expand with limited job creation and continued under-investment, resulting in risks for public health and public order if public investments are not adequate to address availability of low-cost housing and create jobs.

More urban 29

Population, million



Sources: UN Population Division, DB Research

This also means that a growing number of SSA's children are brought up in urban environments. The city with the largest number of children in the world in 2025 is expected to be Kinshasa, DRC, the sixth-largest Lagos, Nigeria and the 17th Luanda, Angola[33]. This has implications for education as well as health. With a population of around 11 milion, Lagos is one of the 21 cities in the world with a population of over 10 million. Its expected growth rate for 2010-2030 is the highest among this group: at 75% it is well above that of the next fastest-growing cities in this group, at around 50% (Delhi, Beijing, Dhaka and Shenzhen).[34] (For a display of the largest SSA cities, see map 40.)

The employment challenge

Economic growth in Africa is creating employment but not on the scale required to absorb new market entrants. Africa's youthful population can result in a dividend, but only if enough jobs are created. SSA's decade of growth has done little to alter underlying labour market conditions. For example, in Uganda, waged jobs grew at 13% a year between 2003 and 2006 but this absorbed less than one in five new labour-market entrants. SSA's total labour force is projected to increase by 70% between 2000 and 2020.

Few signs of structural transformation

In order to be job-intensive, growth must be accompanied by the reallocation of economic resources from activities with low productivity to more productive ones. This structural transformation encompasses both the rise of new, more productive activities (i.e. "within sector" productivity growth) and the movement of resources and labour from traditional activities to these newer ones ("structural" productivity growth). In Africa, within-sector labour productivity growth has been slower than in other parts of the world but structural labour productivity growth has started to take place, with labour moving from less

[32] "What drives 21st century cities?". Sanjeev Sanyal. DB Markets Research. July 2013.
[33] McKinsey. "Urban world" (2011).
[34] UN data on Urban Agglomerates.

productive activities to more productive ones since 2000 – less than in Asia but more than in Latin America.[35]

The degree and the path of the ongoing structural transformation vary within SSA. Most oil exporters have seen sustained increases in average labour productivity through spillovers into the non-oil sector. Most middle-income countries have experienced both labour productivity growth in the agricultural sector and a declining share of the sector in GDP. Agricultural productivity growth has occurred, to a lesser degree, in most non-fragile, low-income countries but hardly in most fragile countries, which have experienced low irregular growth[36]. Although its agricultural potential is huge, SSA has experienced on the whole slow growth in agricultural labour productivity over the past three decades, mostly due to low fertiliser use and soil depletion.[37]

Transformation more through services than manufacturing?

With respect to manufacturing, SSA clearly lags behind. The share of manufacturing in Africa's output declined to 11% in 2010 from 12% in 1980. In comparison, it remained at over 31% in East Asia.

The manufacturing sector is developing in a few countries like Ethiopia (leather industry), Kenya, Mozambique and Tanzania. But, in general, the services sector has been more successful in stimulating output, exports and labour productivity growth, with some countries moving up the value-added chain (Kenya, Mauritius).

It is not clear how much manufacturing is set to expand across SSA. It could become increasingly competitive given the rapid rise in real wages in Asia and SSA's demographic dividend. Depending on resource endowments and market conditions, some SSA countries may follow the Asian structural transformation path through low-wage manufacturing. There is, indeed, a close link between a strong and diversified primary sector and a strong manufacturing sector: countries which have a comparative advantage (exporting more than the average) in a large range of raw commodities also tend to have a comparative advantage in a wide-range of value-added products.[38]

However, output and employment trends in SSA's services sector have been stronger than in Asia, suggesting a path to transformation in which extractive industries, agriculture and the services sector play a dominant role and manufacturing a lesser role.

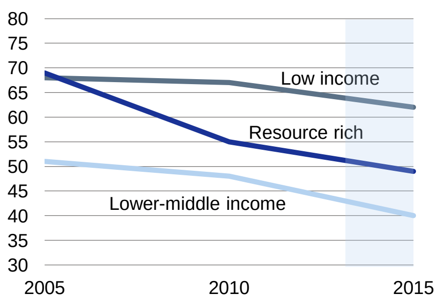
Conditions for structural transformation in SSA through a strong natural resources sector 30

— Infrastructure
— Education and skills
— Good institutions and regulations
— Government capacity
— A balanced tax system
— Financial access
— Effective markets

Source: African Economic Outlook (2013)

Structural transformation 31

Agriculture's share of employment, %



Sources: World Bank, IMF, DB Research

Structural transformation through a strong natural resources sector

The majority of SSA's labour force lives in countries with income per capita below USD 1,000 and 60% of those have agriculture as their primary economic activity, according to recent estimates by the IMF and the World Bank. The share of agricultural employment is decreasing – slightly in low-income countries, more so in lower-middle income countries and even more so in resource-rich countries (see chart 30). This reflects mostly a sharp increase in services through spillover from the natural resources sector, e.g. trading.[39]

To accelerate a budding structural transformation, SSA's countries must make the most of existing sectors and activities, particularly natural resources of

[35] African Economic Outlook 2013. African Development Bank, OECD, UNDP, Economic Commission for Africa.
[36] Regional Economic Outlook for SSA. IMF, October 2012.
[37] "Which growth for SSA? Tapping is huge agricultural potential is key". Schaffnit-Chatterjee and Lanzeni. Euromoney. Upcoming July 2013.
[38] Regional Economic Outlook for SSA. IMF. October 2012.
[39] Regional Economic Outlook for SSA. IMF. May 2013.

agricultural and extractive origin. This is a key sector for most economies of the region barring a few exceptions like the small island states. SSA is rich in arable land and agriculture accounts on average for over half of total employment and one-fifth of GDP. Rapid productivity growth is often accompanied by declining shares of agriculture in GDP and employment, reflecting the migration of resources towards higher-productivity activities in other sectors. However, an increase in agricultural labour productivity releases labour to the rest of the economy, so increasing agricultural productivity is an essential element of structural transformation in SSA – with a significant opportunity to raise living standards through improving relatively low agricultural productivity[40].

Although dependence on any commodity can impede diversification and although capital-intensive, extractive industries tend to provide little direct employment, countries with a diversified commodity sector tend to have more diversified activities in other sectors, through linkages with a wide range of higher value-added products. Indeed, extractive industries create more jobs when revenues are invested in labour-intensive, higher value-added production. According to recent estimates, the value of processed products – for a range of minerals from Africa – is typically 400 times greater (by weight) than the raw material (e.g. from smelters and refineries)[41]. Instead of holding a country back, a strong and diversified primary sector is a key step towards diversification and job creation.[42] So far, SSA's commodity producers have experienced little value addition and few forward and backward linkages to other sectors of the economy.[43]

In SSA, agriculture was considered backward and extractive industries as enclaves – offering few opportunities for employment and generating little expertise for higher-value activities. As a result, both sectors have been neglected, in terms of receiving financial support, research and skill-building.[44]

This has started to change, however. As global demand increased and commodity prices soared (to unprecedented levels for metals and fuel, to levels not seen since the 1970s for agricultural commodities), SSA experienced renewed commitment to agriculture and the extractive industries and resource production increased between 2000 and 2010 for all categories: by around one-third for soft and energy commodities and by about one-fourth for mining output (see table 36).

Africapitalism 32

"Nigerian entrepreneur and philanthropist Tony Elumelu defines Africapitalism as the private sector's commitment to Africa's development through long term investment in strategic sectors that drive economic prosperity and social wealth.

The message of Africapitalism seems to be gaining momentum on the continent and beyond – the UK Guardian newspaper ran a feature on it recently suggesting it could be the new model for Africa's development and many of his 30,000 or so social media followers on Twitter appear to agree ."

Source: allAfrica
http://allafrica.com/stories/201306271650.html?viewall=1

Low level of wage employment across SSA

Resource-rich and low-income countries have the lowest ratio of wage employment to the labour force (around 13%), compared to 18% for lower middle-income countries. Low-income countries, given high labour force growth not quickly absorbed by the small non-farm sector, are projected to experience little change in wage employment (14% in 2015)[45]. Livelihoods are mostly dominated by smallholder farming, off-farm employment and informal sector enterprises. Manufacturing is also dominated by small companies and the informal sector. In Ethiopia, only 5% of people engaged in manufacturing are working in firms with 10 or more employees[46].

Given Africa's demography, the structural transformation to a labour market dominated by private wage employment is likely to take several decades. Creating an environment where entrepreneurs grow businesses which flourish

[40] Regional Economic Outlook for SSA. IMF. October 2012.
[41] UN Economic Commission for Africa (2011). "Minerals and Africa".
[42] African Economic Outlook 2013.
[43] Economic Report on Africa (2013). United Nations Economic Commission for Africa.
[44] African Economic Outlook 2013.
[45] Regional Economic Outlook for SSA. IMF. May 2013.
[46] Africa Progress Report 2012. Africa Progress Panel.

requires improving infrastructure and logistics, access to finance as well as appropriate tax and trade policies (see also "Improving the business environment" on p. 25).

Skill deficits: Aligning education and employment

The majority of Africans enter the world market with limited education. Most did not complete primary education and only a minority went to secondary schools. These deficits represent an enormous cost in terms of lost potential for economic growth and social cohesion. Africa's labour productivity remains low, partly due to poor levels of education and high prevalence of diseases.

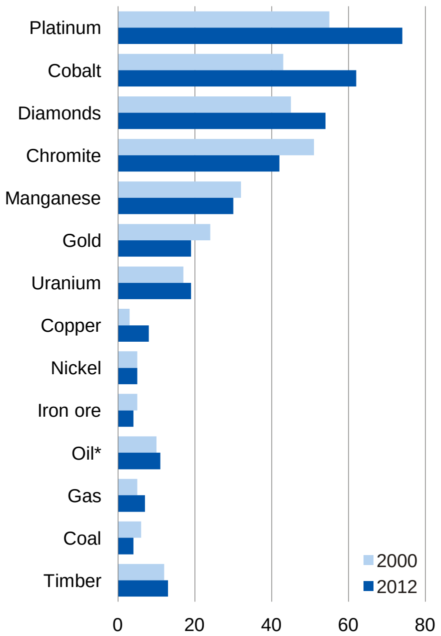
Strengthening human capital influences the rate of innovation and uptake of new technology and thus fosters structural transformation. An educated and healthy workforce is also often a key aspect in foreign investors' decision on where to locate. In spite of not faring well in this area, many SSA resource-rich countries have still managed to attract substantial growth-enhancing FDI investments. However, the impact of these investments on development is limited when they are confined to specific subsectors.

Allocating resources to health and education is not enough to raise human capital: decades of spending by donors and African governments have not led to adequate results. This is due to at least three factors: 1) resources do not always reach their intended recipients, 2) absenteeism is substantial in school and hospitals and 3) service quality is poor[47].

Few SSA countries have put in place an adequate programme for vocational education and training. However, some governments are starting to address skill deficits among the youth. For instance, Cameroon, Ethiopia, Rwanda and Mozambique have taken steps to strengthen coordination between several agencies for skills development. The Kenyan government has developed a public-private partnership to train 20,000 skilled information technology workers[48].

Natural resources wealth 33

Africa's share of global production, %



* Includes North Africa.

Sources: Africa Economic Outlook, DB Research

D. Managing resource wealth for sustainable growth

Resource-based wealth is undeniably one of the key forces shaping Africa. Although it is an engine of growth, it also poses risks and has not delivered expected results on social development.

Metals and mining ...

A major player in global markets for several minerals, SSA produces a significant share of the world's metal and mining output: 74% for platinum group metals (PGM) – used for catalytic converters in cars; 62% for cobalt – used for batteries and metal alloys; 54% for diamonds; 42% for chromite – for stainless steel; 30% for manganese – for steel production; and 19% for gold and uranium (see chart 33 and table 36).

At the country level, South Africa is one of the worlds' leading mining economies and other countries have significant market shares in some minerals (see table 34). Zimbabwe has the potential to become a major player in the diamond and

[47] "Africa's economic boom". Devarajan and Fengler. Foreign Affairs. May/June 2013.
[48] Africa Progress Report 2012.

Global production shares in metal and mining 34

- South Africa: 83% rhodium, 75% platinum, 40% chromite, 23% titanium, 18% manganese, 10% gold
- DRC: 50% cobalt, 25% industrial diamonds, 14% tantalum, 3% copper and tin
- Botswana: 25% diamonds, 22% copper
- Namibia: 10% uranium, 7% diamonds
- Angola: 9% diamonds
- Mozambique: 9% coltan
- Guinea: 8% bauxite
- Zambia: 7% cobalt, 4% copper
- Burkina Faso, Ghana, Guinea, Mali and Tanzania together: 9% gold

Sources: African Development Bank, DB Research

platinum (also gold) sectors in the coming years as long as political risks are mitigated.[49]

Beyond current production, mineral reserves in SSA hold significant potential, particularly in iron ore, the second most traded commodity behind oil (table 34). Given that costs are rising in traditional exporting countries such as Australia and Brazil, the West African iron ore belt has attracted surging foreign investment and exploration, in Guinea, Sierra Leone and Liberia.

... and oil and gas ...

SSA accounted in 2012 for around 7% of oil production and exports 5% of known global reserves. Oil production is dominated by Nigeria and Angola which have increasing reserves: Angola's have doubled between 2001 and 2010, Nigeria's increased by 20%.[50] At the same time, other countries are emerging as global suppliers. Rising world energy prices have driven a new wave of exploration and several recent discoveries are significant, such as those in Ghana, Uganda, DRC, Kenya and Ethiopia.

New finds of natural gas off the coasts of Mozambique and Tanzania could be a game changer in the coming decades: they exceed the known reserves of the UAE and Venezuela and are only slightly lower than those of the US. West Africa is also emerging as a major natural gas producer as gas capture is becoming a strategic focus in Angola and Nigeria, as well as Cameroon, Equatorial Guinea and Gabon.[51]

SSA is also expected to become a key player in coal exports in the coming years as production picks up in Mozambique, South Africa and, to a lesser degree, Zambia and Botswana.

... promise strong revenue flows

Expected annual revenue flows from additional production of raw materials 35

- Ghana: 2.3% of GDP (oil)
- Mozambique: 18% (gas and coal)
- Tanzania: 15% GDP (gas, gold and nickel)
- Uganda: 10% GDP (oil)

Sources: IMF, World Bank

Natural resources have played a critical role to support growth in SSA – through exports and FDI fueling the import of capital goods, technologies and know-how and the development of infrastructure.

The levels of known reserves of natural resources have been rising in SSA, driven by increasing investment in exploration, technology-related lower discovery costs and increasing demand. Still, the reserves are likely to be grossly underestimated since SSA remains largely unexplored: the region spends less on exploration than one-tenth the amount spent (per unit area) by major mineral producers such as Australia and Canada. Reserves quality and improved business environments also bode well for frontier markets like SSA.

Although future revenue flows are tricky to estimate since they depend on investment levels, world commodity prices and taxation policies, they are set to be very large compared to current budgets and GDP (see table 35).

[49] Business Monitor International. "Frontier mining". April 2013.
[50] BP Statistical Review of World Energy (2013).
[51] US Geological Survey (2012). Africa Progress Report (2013).

Production of natural resources 36

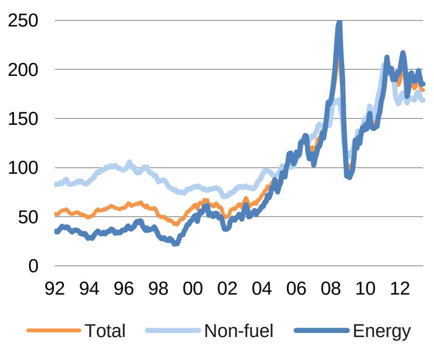
	2000			2010				
	Africa's share of global production %	Value of Africa's production 2010 USD million	Number of countries	Africa's share of global production %	Value of Africa's production 2010 USD million	Number of countries	Real production growth 2000-10 in %	Potential prod. increase by 2017 %
PGMs	55	10,588	2	74	14,191	4	34	33
Cobalt	43	490	6	62	1,775	8	262	87
Diamonds	45	4,265	16	54	4,967	17	16	14
Chromite	51	1,578	4	42	2,442	4	55	
Manganese	32	493	4	30	3,131	8	535	
Phosphates*	28	4,607	10	26	5,662	10	23	
Gold	24	25,568	36	19	19,947	39	-22	53
Uranium	17	111	3	19	1,013	4	813	
Copper	3	2,871	11	8	7,806	12	172	86
Nickel	5	1,225	5	5	1,535	5	25	
Iron ore	5	4,637	10	4	6,404	9	38	466
Oil*	10	216,001	18	11	284,875	19	32	
Gas	5	39,036	14	7	68,423	18	75	new fields in Mozambique and Tanzania
Coal	6	21,266	15	4	23,759	13	12	
Timber	12	77,267	46	13	87,229	54	13	
Mining total	14	59,592	44	12	73,286	44	23	
Energy total	10	276,303	11		377,056	36	36	
Agriculture total	8	200,675	54	9	266,605	54	33	

*Figures apply to the whole of Africa. Phosphates production is concentrated in North Africa.
The shares of production for SSA are significantly lower in oil and gas.

Sources: African Economic Outlook, DB Research

Commodity prices: Historically high ... 37

Monthly commodity price index, 2005=100, USD



Source: IMF

Commodity dependence poses a risk for the economy

The fact that commodities make up an overwhelming share of SSA's exports hardly heralds stable prospects, given the supply/demand uncertainty and the price volatility surrounding commodity markets. Industrial commodity prices may decline in the next few years on the back of slowing demand (particularly in China) and increasing supply, although they are likely to stay high by historical standards[52]. The potential emergence of shale gas and oil (through fracking in North America, China and other countries) could also have implications for global markets and thus for African exporters.

Resource-rich countries are also at risk of contracting "Dutch disease" when resource exports drive up the real exchange rate and inflation – thus increasing the competition from imports faced by domestic producers and reducing the competitiveness of exports overall.

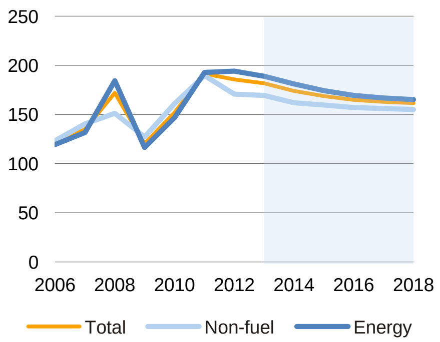
While exports of natural resources have boosted economic growth in SSA, they have also deepened its integration into the low value-added area of international trade. SSA remains an exporter of unprocessed or lightly processed commodities. Diversification and investments in adding value to exports will be critical.

As discussed above, strong growth across SSA has not translated into broad-based economic and social development and the gap is particularly noticeable for resource-rich countries.

[52] See also Commodities Quarterly. Deutsche Bank Markets Research. June 2013.

... and expected to stay on a high plateau 38

Yearly commodity price index, 2005=100, USD



Source: IMF

Unlocking the potential of natural resources

Given that, despite headwinds, commodity prices are expected to remain relatively high (see charts 37 and 38) and the production of natural resources is set to expand significantly in SSA over the next few years, the region has a window of opportunity to capitalise on its resource wealth to create employment and inclusive growth. This requires providing fundamentals such as quality public services (e.g. infrastructure/logistics and education), a favourable institutional and regulatory environment (with transparent, accountable and inclusive governance systems) and access to finance and markets.

It also involves implementing a balanced tax system and sound public finance management systems, capable of coping with price fluctuations and variable revenue flows – for instance through a commodity stabilisation fund (savings to protect against a fall in income from commodity exports). For example, when international oil prices rose above USD 100 a barrel in 2008, some oil exporters (Angola, Gabon, Nigeria) planned their budgets as if oil prices were USD 65 a barrel. This provided them with a buffer when oil prices did fall to that level in the autumn of 2008.

The impact of resource extraction on communities and the environment also needs to be prudently managed, in order to increase broad-based growth and avoid natural resource depletion.

Adopting a global common standard for extractive transparency (not just for SSA) will help, leading to broader distribution of benefits and public spending. Economic transformation through (profitable) value addition and diversification and managing social and environmental impacts are also needed.[53]

E. Governance and investment climate

Some improvement in political stability

Prudent economic policies before 2008 and during the crisis have contributed to significant growth through the global recession and afterwards despite volatility in the global economy (see chart 3). One reason for the improvement of macroeconomic policies in SSA since the 1990s is political liberalisation[54].

Political liberalisation drove improvements in macroeconomic policies

It started with the end of the Cold War. As support from the United States or the Soviet Union decreased, autocratic regimes started to lose their power and countries began to hold competitive elections. In several countries, including Ghana, Nigeria, Tanzania and Uganda, new leaders chose to appoint to government's senior positions some internationally educated technocrats who were more willing than their predecessors to embrace reforms.

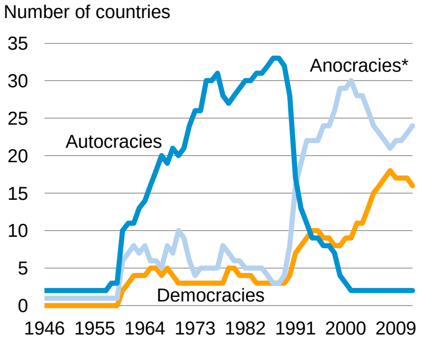
Improved macroeconomic policies also arose with the need to gather broad support for competitive elections. Instead of focusing on pleasing the urban elite as in previous authoritarian regimes, new governments started in some ways to cater to the rural poor. One way was to allow the exchange rate to decrease (thus making it easier for farmers to export their crop) rather than keeping the rate artificially high (thus benefiting the rich eager to buy imported goods – as well as making it cheaper to import goods necessary for industrialisation).

53 Africa Progress Report 2013.
54 "Africa's economic boom". Devarajan and Fengler. Foreign Affairs. May/June 2013.

Donors also contributed to political liberalisation by making the international aid needed in the 1980s conditional on the adoption of reform programmes designed with input from the World Bank or the IMF. In 1999, donors also started to require that African governments consult with civil society, businesses and community organisations in order to qualify for debt relief. This process made it possible to implement sometimes painful reforms by making it easier for the affected groups to accept the changes.

Democracies are maturing but political stability is still fragile

Regime types in SSA 39



* Anocracy refers to countries whose governments combine a mix of democratic and autocratic traits.

Source: Polity iV Project (Center for Systemic Peace)

SSA experienced wars of independence during the 1955-1980 de-colonisation period and many civil wars during much of the post-independence period. The region has been ruled by autocratic regimes for much of the contemporary period but autocracy has almost disappeared in SSA since the end of the Cold War (see chart 39).[55] Almost all African nations now elect their governments. Over the last few months, a few countries such as Angola, Ghana, Kenya and Sierra Leone held elections which were mostly peaceful. A reduction of civil violence in the majority of African countries in 2012 confirms the last decade's trend of maturing democratic attitudes[56].

However, a coup d'etat occurred in Mali and Guinea-Bissau and there have been several incidences of social unrest, which shows that democratic consolidation in SSA remains fragile. (Mauritius is the only fully institutionalised democracy in Africa.) Electoral politics are often dominated by a single party and the region still lacks a level of societal development which is sufficient to sustain democratic forms of governance and stability (see map 40)[57].

According to the Center for Systemic Peace, there are currently two institutionalised autocratic regimes in SSA (Eritrea and Swaziland) but there are a number of uninstitutionalised autocratic regimes, considered as a type of anocracy. Anocracies are countries which are neither fully democratic nor fully autocratic but combine a mix of traits of both regimes.[58] Their presence in SSA has increased since the end of the Cold War, albeit the number of democracies as well, though to a lesser extent (see chart 39). The following map displays a State Fragility Index for SSA countries, based on effectiveness and legitimacy in security, political, economic and social areas[59].

Sub-Saharan Africa has a high average State Fragility Index in a global context. A comparison between current indices and those from 1995 shows that some countries have experienced large improvements in their fragility score including Angola, Togo and Guinea. Other countries have worsened fragility scores, including Central African Republic, Cote d'Ivoire, Burkina Faso, Republic of Congo, Ethiopia and Gambia.

[55] Center for Systemic Peace, Polity 4. Sub-Saharan Africa. www.systemicpeace.org
[56] African Economic Outlook (2013).
[57] Center for Systemic Peace, Polity 4. Sub-Saharan Africa. www.systemicpeace.org
[58] Marshall and Cole. Global Report 2011. www.systemicpeace.org
[59] A country's fragility is indeed closely related with its ability to manage conflict, implement public policy and deliver essential services and with its resilience in maintaining system coherence, cohesion and quality of life, in responding effectively to challenges and crises and in sustaining progressive development, as per the reference above.

Social tensions reflect a range of concerns, particularly socio-economic frustrations, such as wage issues (recently leading to protests for instance in South Africa, Zimbabwe, Kenya, Zambia and Cote d'Ivoire) and the increasing cost of living (e.g. in Angola, Burkina Faso, Gabon, Nigeria, South Africa and Uganda).[60]

Inter-ethnic tensions are also a cause of civil unrest. Increased terrorism has underpinned rising civil violence in Nigeria and Kenya. Prolonged cross-border conflic affect quite a few SSA countries including Mali and the Sahel region, Nigeria, Somalia, Kenya, Sudan and South Sudan. Africa still accounts for over 20% of refugees and 40% of internally displaced people worldwide[61].

On the positive side, the fact that demonstrations take place – also facilitated by increased usage of social media – reflects higher levels of civic activism which are correlated with better control of corruption, through citizens demanding more accountability from their governments.

[60] African Economic Outlook (2013). These protests could stand in the way of fiscal balancing if governments feel pressured to keep or establish financially unsustainable policies - such as food and fuel subsidies – in order to prevent social instability.
[61] Africa Progress Report (2012).

From little to extremely fragile 40

State Fragility Index, 2012

Note: The State Fragility Index is based on effectiveness and legitimacy in security, political, economic and social areas.
Source: Center for Systemic Peace

Governance remains an issue although some improvements are under way

Apart from Botswana, Cape Verde, Mauritius, Rwanda and Seychelles, all SSA countries score below 50% in Transparency International's 2012 Corruption Perception Index (CPI)[62]. This is similar to Eastern Europe and Central Asia. Most of the countries at the bottom of the list have emerged from prolonged conflict. Somalia, Sudan, Chad, Burundi, Zimbabwe all score below or at 20%.

A number of countries are taking a stance against corruption. For instance, the Kenyan government is implementing monitoring tools and a central base of contract information to increase transparency in public spending. With the same

[62] The CPI is a composite indicator of perception of corruption in the public sector on a scale from 100 (very clean) to 0 (very corrupt) based on surveys of business people and assessments of country analysts.

objective, in Ghana, social auditing clubs monitor public tenders and watch for the quality and effectiveness of public spending.[63] Although starting from a low base, Angola introduced important institutional reforms in 2011, to enhance accountability in public spending and predictability of oil revenue transfers to the budget. It has incorporated the quasi-fiscal operations of state oil company Sonangol into the 2013 budget. Backdated to 2007, revised figures largely account for the USD 32 bn which were unaccounted for between 2007 and 2010.[64]

With all countries engaged in enacting new laws to combat bribery and corruption, the critical issue is to implement and enforce the legislative framework. Governments are key actors here but the private sector also has a critical role in adopting greater corporate transparency. This issue is currently high on the international policy agenda.

Improving the business environment

Doing business in SSA is challenging in terms of infrastructure and institutions ...

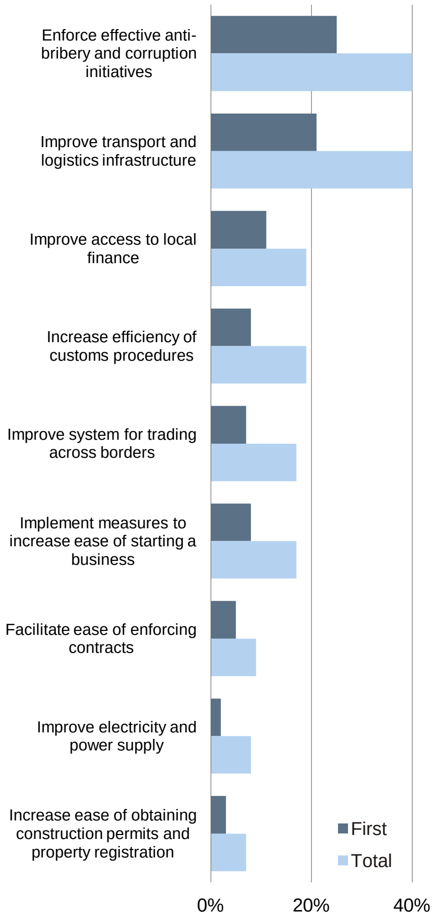
SSA's business environment remains challenging in terms of infrastructure and institutions. The main impediments to development in SSA from the perspective of the private sector are the degree of corruption and the inadequate transportation and logistics infrastructure (see chart 41 and table 42): Four types of infrastructure are of particular concern: power, transportation, water supply and sanitation, and telecommunications[65].The opportunity cost of power outages in terms of sales lost is substantial. The low road density and logistics performance result in high costs of exporting goods.

A regional comparison of the World Bank's Logistics Performance Index suggests that SSA is doing particularly poorly in terms of rail and airports infrastructure, as well as information and communication technologies (see table 43).

In terms of the World Bank's Ease of Doing Business Index benchmarking 11 areas of business regulations, SSA does not fare well. Out of the 16 worst performers world-wide, all but two are in SSA. The best-ranked SSA countries are Mauritius (19 out of 185), South Africa (39), Rwanda (52), Botswana (59) and Ghana (64).

Perceived challenges to doing business 41

Share of respondents, answering: What measures should be implemented to increase Africa's ease of doing business? (2 answers: first and second choice)



Sources: E&Y, DB Research

Structural impediments to doing business 42

	South-East Asia	SSA
Road density, km of road (per 100 sq km of land)	35.00	14.50
Cost to export, USD per container	774	1,927
Logistics performance index, efficiency of customs clearance (1=low, 5=high)	2.60	2.20
Value lost to electric outages, % sales	3.40	6.10
ICRG corruption (0=high, 6=low risk)	2.50	2.30
Transparency, accountability and integrity of the public sector (1=low, 6=high)	3.00	2.80

Sources: IMF, DB Research

Respondents rating the quality of infrastructure type as "high" or "very high" 43

Percent of respondents

	Ports	Airports	Roads	Rail	Warehousing and transloading	ICT
East Asia and Pacific	18	22	14	3	15	41
Europe and Central Asia	14	33	15	12	27	43
LatAm	21	24	15	4	19	39
MENA	25	29	5	10	19	39
South Asia	16	23	7	8	11	35
SSA	18	10	12	1	15	28

Source: World Bank (Logistics Performance Index 2012)

[63] African Economic Outlook (2013), IMF.
[64] IMF Angola country report. August 2012, DB Research. "Angola: Oil economy on a diversification path". Schaffnitt-Chatterjee. June 13, 2013.
[65] Columbia FDI perspectives No. 97 by AG Mijiyawy. June 2013.

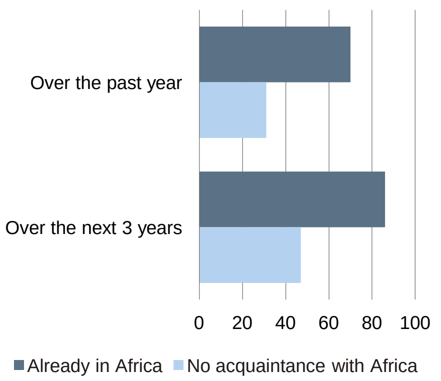
... but it is getting better...

Significant institutional and regulatory improvements have been made in SSA since 2005. Corruption is increasingly being tackled by SSA countries in order to further attract FDI even if public governance still falls behind, which also contributes to the poor state of infrastructure. Many SSA governments have renewed their focus on developing infrastructure (see above), mostly in the areas of transport and power, including South Africa, Nigeria, Angola, Uganda, Kenya, Mozambique, Tanzania and Cameroon.

Clear improvement is visible on the World Bank's Ease of Doing Business Index. Out of the 50 economies making the most improvement in business regulation for domestic firms since 2005, 17 are in SSA. Out of the top 25 countries in terms of improvement, the following 8 are in SSA: Rwanda improved the most in SSA (the second most in the world), followed by Burkina-Faso, Mali, Sierra Leone, Ghana, Guinea-Bissau, Senegal, Angola and Mauritius[66].

Perception divide: Already in vs not yet 44

Share of respondents voicing that Africa's attractiveness is improving, %



Source: Ernst & Young

... and those already doing business in SSA like it

Ernst and Young[67] identified an ongoing significant gap between respondents with an existing business presence in Africa and those who have not yet invested. Most of those with an established business presence in Africa view the continent's attractiveness as a place to do business as increasing, both currently and in the future (see chart 44). A similar gap exists in terms of relative attractiveness compared to other regions of the world. In fact, those already doing business in Africa ranked it as a more attractive region than any other region in the world except Asia. It bodes well for investments in Africa that those who are active are happy with their situation.

According to the same survey, the sectors perceived as having the highest growth potential in Africa are mining and metals, agriculture, oil and gas, infrastructure, IT and financial services.

Conclusion: Optimism is warranted

SSA is at a crossroads. It has a window of opportunity to capitalise on its youth surge and resource wealth to create employment and inclusive growth. Political change and reforms are key. It will not be easy but democratisation, urbanisation and virtual connectedness bode well. Investments in infrastructure/logistics and education, economic diversification, market reforms and improved governance are critical for long-term success.

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[66] African Economic Outlook 2013.
[67] Ernst & Young's attractiveness survey Africa 2013.

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Printed by: HST Offsetdruck Schadt & Tetzlaff GbR, Dieburg

Print: ISSN 1612-314X / Internet/E-Mail: ISSN 1612-3158