ALLIANZ DRESDNER ECONOMIC RESEARCH

Working Paper 101

June 11, 2008

MACROECONOMICS | FINANCIAL MARKETS | ECONOMIC POLICY | SECTORS

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New dawn in Africa

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Working Paper
No. 101

1. A summary of the most important statemants 3
2. Risks: The burdens from the past 3
3. Opportunities: Spurring the commodity boom 10
4. Projection: Why, how much and who? 16

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1. A SUMMARY OF THE MOST IMPORTANT STATEMENTS

- Though some countries in sub-Saharan Africa[1] are benefiting from the **boom in commodities,** others are at a disadvantage. Even if prices are unable to maintain their currently exceptionally high level, they will nonetheless remain buoyant compared to previous decades and bolster economic momentum.

- Although a number of countries are still embroiled in civil war and economic chaos, the region has experienced a general rise in **political** and **economic stability**. The foreign currency liquidity situation in many countries can be termed comfortable, with economic policy being determined to a lesser degree by regional interests.

- The fragmentation of sub-Saharan Africa into many small countries makes it practically impossible to achieve high **economies of scale** in industrial production due to the lack of cross-border free trade agreements, single jurisdictions and larger economic centers. Efforts being undertaken in the manufacturing industry will focus on the processing of mining and agricultural commodities.

- A **middle class** is starting to emerge in bigger cities, which is stoking up demand for higher-quality products. The service sector and, here in particular, the **financial sector** will benefit from this. The expansion of infrastructure and of housing construction should further boost the **construction industry**.

- The sub-Saharan African **economy** can be expected to grow in the **next 10 years** in real terms by at least 6-7.5 % a year.

- We expect **above-average growth rates** to be achieved in, among other places, **Nigeria**, **Angola** and **Mozambique**.

Economic take-off?

There are growing signs that the economy in Africa is taking off. This is all the more encouraging given the many disappointments in the continent‘s recent economic past. Natural catastrophes, famine, civil wars, corruption and excessive debt threw sub-Saharan Africa behind other developing regions and prompted international companies to avoid the continent when developing their business strategies. Temporary glimmers of hope, e.g. the adoption by a number of countries of a market economy following the collapse of the Soviet Union, were generally followed by disappointment, with deteriorating external conditions - such as a collapse in commodity prices - frequently standing in the way of an upswing. Is the latest germ of economic recovery likely to experience the same fate? Or do key factors suggest that the sub-Saharan African economy will latch on to the momentum of Asia and Latin America and that emerging markets will develop from the African developing nations?

In the course of this study we will weigh up the negative and the positive factors and attempt to derive from them the long-term trends of economic growth.

2. RISKS: THE BURDENS FROM THE PAST

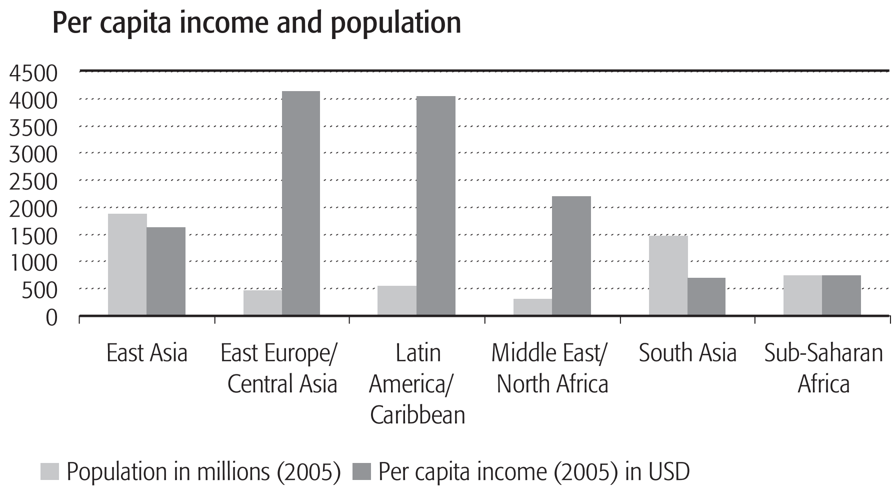
2.1 Low per capita income - wide prosperity gap

Compared to other developing regions, the central and southern part of Africa generally lags behind in the economic and social core indicators. In terms of per capita income, the region ranks only fractionally ahead of southern Asia[2]. The result would be even less favorable were **South Africa** to be removed from the calculations. In many respects, South

[1] Sub-Saharan Africa is the term used for the part of the African continent lying to the south of the Sahara Desert. The Sahara represents a separation point in geographical, climate and ethnic terms.
[2] Among other countries India, Sri Lanka and Nepal.

Africa assumes a special status on the African continent. In terms of its infrastructure and financial market, the country has more in common with an industrialized country. This is reflected in the country‘s economic performance; despite a population share of only 6 %, South Africa generates 40 % of the total GDP of the sub-Saharan African countries.

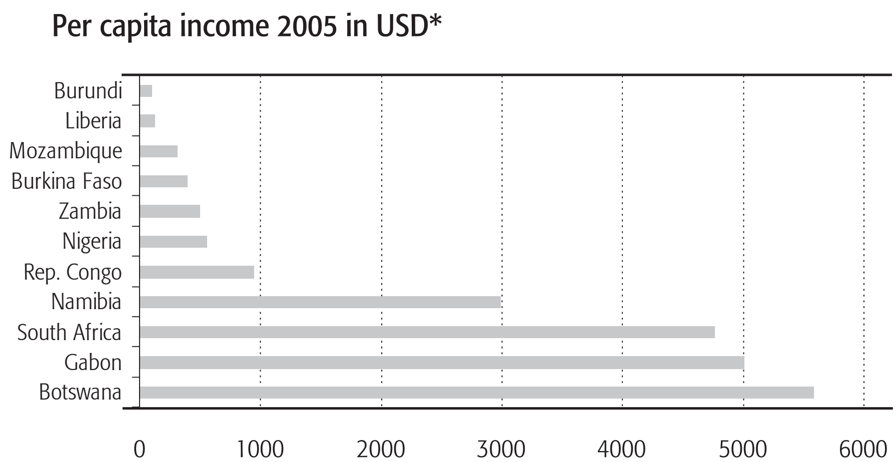
Chart 1



Source: World Bank

The differences in the standard of living, as documented in Chart 2, are not limited to South Africa. There is also a considerable prosperity gap between the other countries; for example, the per capita income of Botswana, where diamond mining is a major industry, is more than 50 times that of Burundi.

Chart 2



*Based on purchasing power parity
Source: World Bank

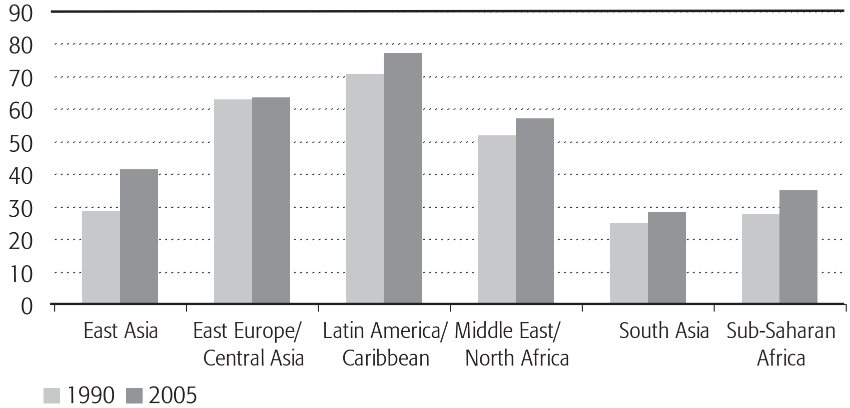
2.2 The long-term consequences of colonialism

Many countries, low economies of scale

A glance at the map reveals one of the main dilemmas facing Africa, namely the **plethora of countries**. Leaving aside the north African countries, the Continent is home to no less than **48 nations**. This fragmentation hampers, among other things, major **economies of scale** in production, particularly given the absence of cross-border agreements on **free trade zones** and **single jurisdictions**. The fragmentation also prevents the formation of larger **economic centers** which is where a sizeable part of aggregate output is generated in Latin America and eastern Asia. In terms of development policy, larger agglomerations such as Shanghai or Sao Paulo, offer the advantage of a relatively cost-efficient establishment of the infrastructure necessary for modern production. A further advantage is that the networking within the centers promotes the division of labor and, by extension, productivity. No metropolitan areas of this kind exist in sub-Saharan Africa, as also expressed in the relatively low degree of urbanization (Chart 3). A further point is that many countries with no **access to the sea** lack direct and cost-efficient means of transport.

Chart 3

Urbanization
(share of urban population in % of GDP)



Source: World Bank

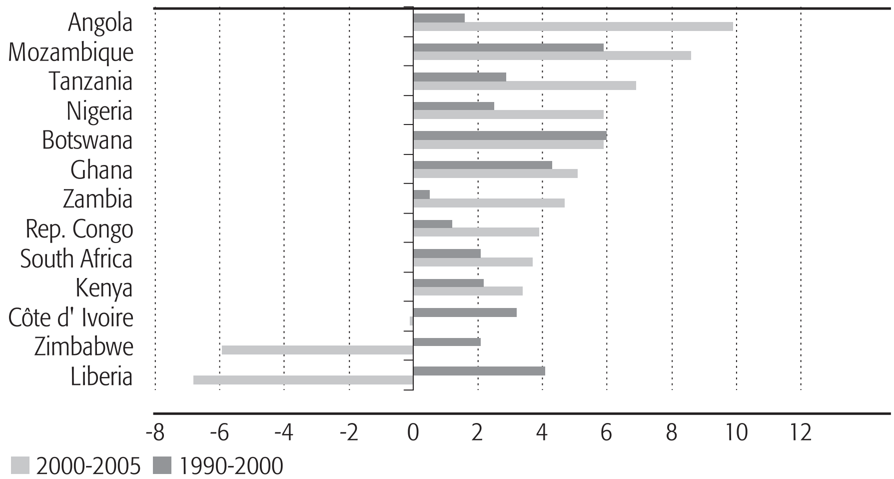
National borders and civil wars

National borders, above all in central Africa, strongly reflect the **colonial past** and frequently have little in common with uniform **ethnic groups**. As a result, many nations are home to ethnic minorities with either no or only insufficient government participation. Open violence results as a consequence of the disadvantages experienced by certain groups of peoples as also reflected in the great imbalances in income and wealth distribution within the countries. In Rwanda, more than 500,000 people were killed in 1994 in what was the worst ever case of **genocide** on the African continent. That such catastrophes by no means belong to the past is revealed in, among other things, the current conflict in the Democratic Republic of Congo, Sudan and most recently in Kenya which prior to this had actually been considered by the west as one of the politically most stable countries of Africa.

Civil war-like conditions tear deep wounds in an economy. Domestic production enters a decline for long years, as revealed in Chart 4 in the case of Liberia during the period 2000-2005. A similar case could be found or still exists in comparable conflicts in Sierra Leone, the Democratic Republic of Congo and Somalia. However, the reverse can also apply, with an end to these conflicts unleashing massive growth forces as happened in the case of Angola and Mozambique. Both countries have achieved political stability in the last 15 years after years of civil war. Obviously this was not the only factor in the relative economic success. Other factors also played a role, such as the tapping of Angolan oil reserves.

Chart 4

Economic growth (real in %, annual averages)



Source: World Bank

A further consequence of colonialism is that national economies are frequently geared to only a **handful of products**, above all in the **farming sector**. Crops are frequently cultivated according to monoculture, mostly for export to the industrialized countries. This constellation prevented the establishment of commercial structures and also left the countries heavily exposed to **price fluctuations** on the **international commodity markets**.

2.3 Young population, but insufficiently educated

Young population, but ...

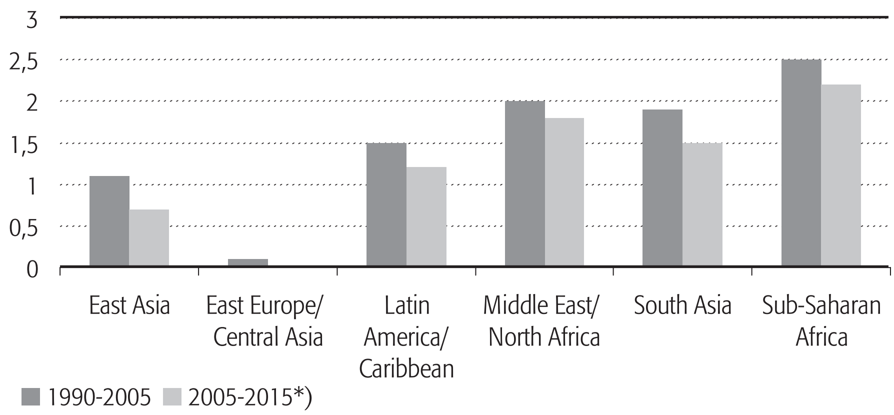
In no other developing region is the **population** growing so quickly as in Africa (Chart 5), in spite of the great vulnerability of the people to **epidemics** and to often lethal diseases such as **malaria** and **AIDS**.

The population will continue growing strongly in coming decades because the share of young people in the total population is especially high here. After all, youngsters below the age of 15 account for more than 40 % of the total population. In all other major developing regions, the corresponding ratio is well below 35 %.

A young quickly-growing population offers both economic advantages and disadvantages. One disadvantage is the fact that they cause the share of the economically inactive population in the total number of inhabitants to surge upwards. In other words: relatively few have to feed a large number. On the other hand, ever more people entering working life at a low average age, represents a factor which propels future economic growth.
It comes as no surprise to learn, therefore, that pension funds from industrialized countries with populations showing a high average age prefer to invest above all in young economies in order to finance high pension payments in the future from the capital earnings. Although pension funds have not yet discovered the investment potential in the younger economies of sub-Saharan Africa, these may hopefully play a notable role in the future.

Chart 5

Annual average population growth in %



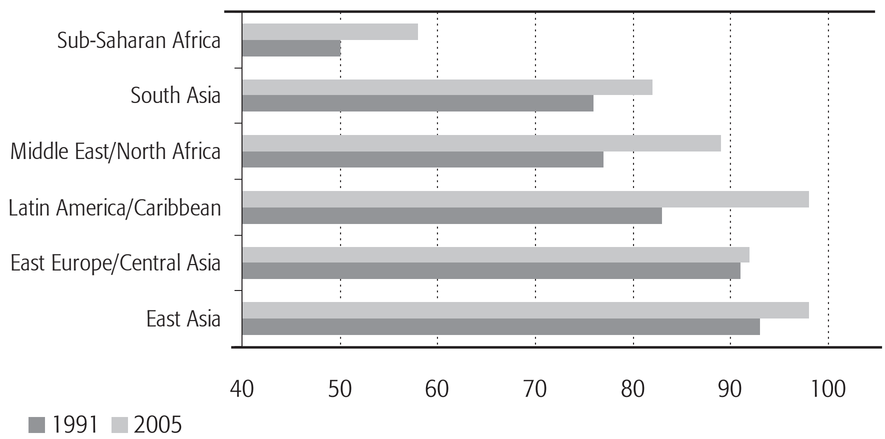
*) forecast

Source: World Bank

However, for this calculation to work out, a further condition has to be fulfilled: The young maturing population must be sufficiently **well-educated** otherwise a danger exists that unemployment might start climb steeply with corresponding negative repercussions for social and political stability. **Rising productivity** almost inevitably demands a more qualified workforce.

Chart 6

Share of students with primary school graduation in corresponding age group (in %)



Source: World Bank

Sub-Saharan Africa shows a considerable need to catch up in the “production factor **education**“, as documented for example in Chart 6. Practically all the other pertinent education indicators regularly published by the World Bank point to huge deficits in Africa. Despite some improvement there is not much justification for the assumption that a higher education standard is only a matter of time, with the African continent automatically latching on to the levels of the other developing regions. The chart above highlights the fact that, more than 15 years ago, the education level in Asia, Latin America and the Middle East had already been far better than that today in sub-Saharan Africa.

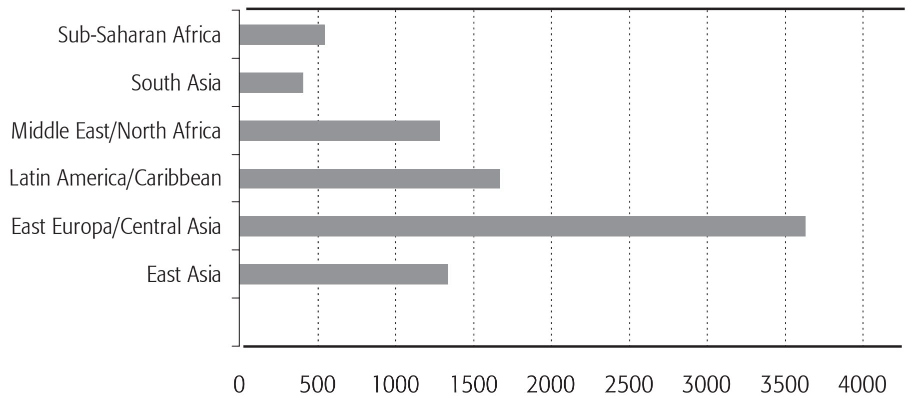
2.4 Need to catch up: Infrastructure and financial system

Lack of infrastructure

All developing nations and emerging countries show an enormous need to catch up in matters of **infrastructure**. This is particularly the case in sub-Saharan Africa. With many economies being geared to monocultures, the infrastructure is essentially confined to extracting and transporting mineral resources or agricultural products. On top of this comes the generally **low quality** of the **sea ports** and the inadequate links to the hinterland. As a rule, the **energy supply** is not secured and time and again the countries experience production disruptions. Even South Africa which – as mentioned above – can almost boast of having the infrastructure of an industrialized country is regularly affected by power cuts which have even managed to bring gold mining to a temporary standstill.

Chart 7

Consumption of electricity per capita (2004, in kWh)



In comparison: Industrial countries (2004): 9609 kWh, Euro area (2004): 6869 kWh
Source: World Bank

Underdeveloped financial markets

Similar weaknesses can also be seen in the **financial market**. A hefty portion of financial intermediation is located in the unofficial and statistically unrecorded area of the economy (e.g. based on so-called “Rotating Funds”, which are vaguely reminiscent of western-style building society savings schemes). In **South Africa** these funds **(stokvel associations)** also account for a significant share of the savings schemes popular among wide sections of the black population, despite the efficiency and modernity of the country‘s financial market which sets it positively apart not only from the young African countries but also from all emerging markets.

The **banking markets** mostly consist of a few, frequently state-owned credit institutions which pass on the deposited funds primarily in the form of loans to state-owned companies or to the state itself. From time to time, loans raised abroad substitute the inadequate deposit base at home, rendering the banks highly vulnerable to **short-term withdrawals of capital. Branches of foreign banks** play practically no role in the private client business, and focus essentially on **foreign trade finance**. There are no domestic bond markets and – apart once again from South Africa – bonds from African issuers on the **international capital market** are difficult to find.

South Africa‘s dominance in the financial area is also reflected in the **equity market** which can boast of a capitalization nearly seven times that of Nigeria‘s, the next largest stock market in sub-Saharan Africa. In Nigeria's case, in particular, share prices have just staged a tremendous show of strength, and the decline as a result of the subprime crisis has also remained limited, at least by international comparison. After all, the Nigerian equity index has more than doubled in the past 15 months. Generally speaking, the frequently unfavorable **corporate structure** prevents the equity market from playing a greater role in financial intermediation. This is because only a few companies achieve the size necessary for a listing. On top of this, the capitalization concentrates on only a few companies frequently operating in the energy sector and in telecommunication. **Foreign investors** predominate on the buyer side, while institutional domestic investors remain the exception.

South Africa in particular could certainly assume a key role on the financial market for the entire region of southern Africa. The financial market infrastructure and high liquidity existing here could offer an ideal platform for companies from the neighboring countries to list their shares and mobilize capital.

2.5 China's motives far from altruistic

China: Securing raw materials

China's activities in Africa can be viewed in various lights. Some engagements provided much needed dynamism to the economies. But not all aspects are positive for sub-Saharan Africa[3]. However, a factor that should not be forgotten is that development aid from western countries also frequently failed and was often spurred by equally selfish motives. China is essentially pursuing three goals in sub-Saharan Africa: First, the investments are intended to secure the **raw materials** for China's booming economy in the longer term. Second, Peking views the African countries as a developing **sales market** for Chinese products. And third, in **political terms**, the country is nurturing hopes of an alliance – in, among other things, multilateral organizations such as the UN – as a way of countering critical demands from the west.

There are naturally no reasons to object to an expansion of trade in goods between sub-Saharan Africa and China. But from a western viewpoint and also taking Africa's development perspectives into account, this is not desirable between nations which have had an **embargo** imposed on them in connection with **human rights violations**, such as Sudan for example, or Zimbabwe. China's dealings here are strengthening the position of the African despots because China is not intervening in the disastrous inner-political relations of the countries concerned and is additionally financing the imported commodities in some cases by means of **weapons supplies**. It is also difficult to grasp why western governments and multilateral financial institutions should agree to waive extensive debt repayments only to see China following in their footsteps as creditor.

A further problem is that China is flooding the markets of sub-Saharan Africa with **cheap Chinese goods** (e.g. electrical devices, haberdashery and, above all, textiles of all kinds). Although wages in China are higher compared to sub-Saharan Africa, China is still able to significantly undercut the prices on local markets thanks to its mass production (higher economies of scale). It is practically impossible, therefore, for these countries to build up **jobs**. Hence China's involvement poses a threat to domestic production and to the progress of development policy. At some large building sites in Africa, you can meanwhile see nothing but Chinese workers while the local labor market gains no much from the construction activities. On the other hand, the question is whether western companies would be prepared to take on the high sovereign risk existing in some of the countries when making their investment decisions. Chinese companies with state backing are, by contrast, less put off by this. In this sense, Chinese investments could also function as a door opener in sub-Saharan Africa which would prompt western companies to invest sooner or later.

[3] For example, the "Stiftung Wissenschaft und Politik" comes to a very negative conclusion in its study "The Africa Policy of the People's Republic of China", August 2005.

3. OPPORTUNITIES: SPURRING THE COMMODITY BOOM

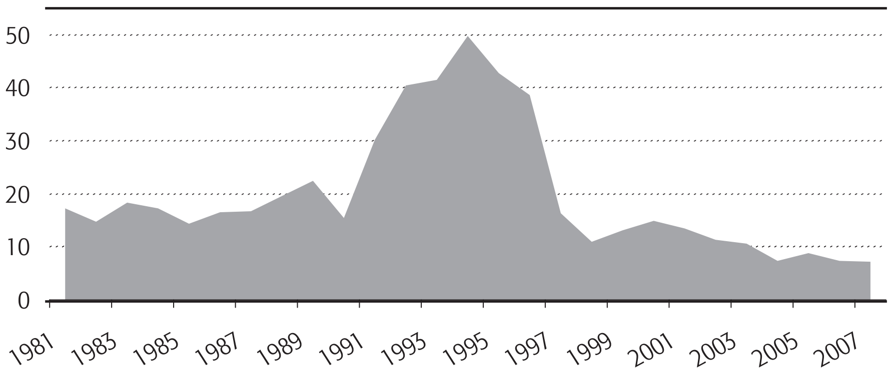
3.1 Good examples

Latin America as model

New beginnings and new dawns are nothing new in Africa. But these were followed all too frequently by disappointments as already described above. Nonetheless, a number of developments and their interplay now suggest that the signs of hope emerging on the horizon will intensify. **Good examples** of development regions at a more advanced stage, in which successes have been achieved thanks to, among other things, rational development policy, illustrate that the situation can indeed be substantially improved. "Models" of this kind include, for example, a number of Latin American countries such as Brazil, Peru and Colombia which have succeeded in raising their growth potential by means of a stability-oriented and predictable economic policy. Multilateral organizations such as the International Monetary Fund and the World Bank have played a crucial mediating role here.

Chart 8

Sub-Saharan Africa: Inflation rate (in %)



Source: International Monetary Fund

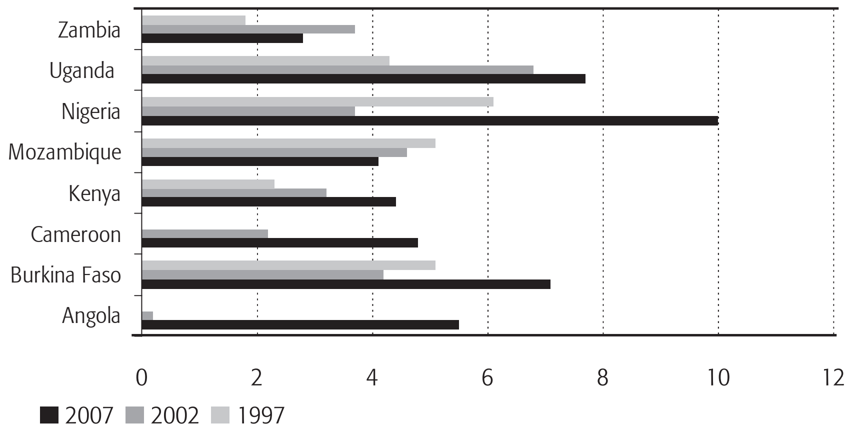
3.2 More macroeconomic stability

More crisis-resilient

Investors do not invest in conditions of political and macroeconomic uncertainty. High inflation rates not only compound the risk of investments failing to generate the desired return. They also harbor considerable exchange rate risks. The consequence is all too frequently a **flight of capital** and a very unfavorable income distribution among the poorest of the poor. Fortunately the inflation rates in most sub-Saharan African nations hovered in the single-digit region in 2007. But in Africa, too, prices have risen noticeably in recent months due, above all, to the sharp rise in energy and food prices. A particularly **negative example** is **Zimbabwe** which has been plagued by economic chaos and hyperinflation for years.

Chart 9

Foreign exchange reserves: Import cover in months



Source: Evaluation according to IMF data and national statistics

The better macroeconomic management in the region can also been seen in the **more realistic exchange rate relations** and in a better provision of **foreign currency liquidity**, all of which are serving to make the countries more crisis-resilient. As can be seen in Chart 9, foreign currency reserves have caught up noticeably in relation to imports of goods and services. As a rule, the import cover of reserves should not fall below three months, and this is now the case in many sub-Saharan African countries. Moreover, a whole series of countries have actually been recording **current account and budget surpluses** for several years now.

3.3 Democracies no longer the exception

Connection: Democracy and economic success

It is certainly no accident that most countries with stable macroeconomic conditions have also made the greatest progress in anchoring **democratic structures**. Even if setbacks can still be experienced here, as was recently the case in Kenya, the essential path towards a politically better future is nonetheless paved. Positive examples of political stabilization can be found in Liberia and Sierra Leone. But in heavily populated **Nigeria**, in which economic chaos had frequently gone hand in hand with an unjust policy towards minorities, governments have also pursued a strategy geared towards stability and more democracy. Encouragingly, the recent government change has not altered this.

3.4 Debt relief for good economic policy

Escaping the debt trap

The difficult external debt situation in sub-Saharan Africa took its course once western lender nations started substituting non-repayable development aid for loans. By so doing it was possible on the one hand to initiate more development projects by means of a higher credit total compared to the lost subsidies. But the calculation failed to work out in most cases. Debt increased, the recipient nations either did not want to or could not repay the debt service and the subsequent **rescheduling of debts** became a permanent state of affairs. In 1999 the G8 nations finally agreed to grant an extensive debt remission within the framework of the so-called **HIPC Initiative**. However, the pre-condition for this was that the countries pursued a sensible economic policy based on fixed criteria. In this way, the initiative clearly made a contribution that should not be underestimated towards ensuring greater macroeconomic stability in Africa. It also eased the recipient states' burden of high and untenable debt servicing, as shown in Chart 10.

Debt relief through the HIPC Initiative since 2004

PHASE 1:

Relief to date totaling USD 42bn for 19 countries (including Burkina Faso, Cameroon, Ethiopia, Ghana, Madagascar, Mali, Mozambique, Senegal, Tanzania, Uganda and Zambia).

PHASE 2:

USD 38bn relief process launched for 17 other countries (including Democratic Republic of Congo, Republic of Congo, Côte d'Ivoire, Liberia, Sudan and Togo).

Chart 10

Source: International Monetary Fund

3.5 Sky-high commodity prices

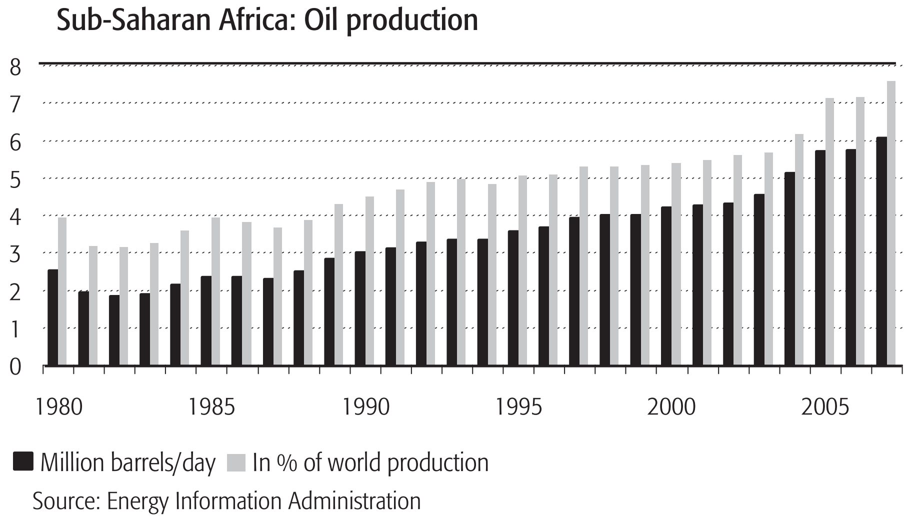
Oil as a blessing for some

The better balance of payments and budget data are also attributable to the high commodity prices which have unexpectedly blessed some countries with a veritable shower of **foreign currency**. This is particularly the case in Angola, Equatorial Guinea, Sudan and Nigeria which have substantial oil reserves. Due, though, to inadequate know-how, sub-Saharan Africa is directly and indirectly dependent on the cooperation of the international oil companies for tapping the oil fields and extracting their resources. However, this need not be a disadvantage because in matters of efficiency these companies are generally more superior to the state-owned oil companies in the other countries frequently holding a monopoly position.

While 10 years ago **Nigeria** accounted for more than half of sub-Saharan African oil extraction, the figure in 2007 was only 39 %. The **shooting star** is **Angola** which has expanded its output over the past 10 years from a good 0.7 to nearly 1.8 million barrels/day, already contributing 29 % in 2007 to total regional output.

On the other hand, it should be mentioned that the high commodity prices are a huge burden on those sub-Saharan African countries, not blessed with mineral deposits. Rising import bills are bloating the current account deficits dramatically as in the case of Ghana, Senegal, Ethiopia and Uganda.

Chart 11



Even if the current high level of commodity prices certainly cannot be extrapolated with any certainty into the future, a number of factors suggest that a reasonably strong price level will be maintained in coming years.

Full effects of high food prices being felt

But: As much as some countries are profiting from the high prices via rising exports, at the same time they are faced with rising **food prices** as consumers. In sub-Saharan Africa, in particular, basic foods are attached a far higher weight in the basket of goods than in the industrialized nations or in the more advanced developing countries. The effects of the higher prices are not only filtering through in full to household budgets. They also frequently mean malnutrition. It comes as no surprise to learn that the growing shortage of food in Africa has already resulted in protests and **unrest**.

The growing desertification of the Sahel region is leading to water and food shortages. As a result, this region is worst hit by the rise in food prices.

Sub-Saharan Africa: Share of commodities in exports

WEST AFRICA	
Burkina Faso	Cotton: 71 %, gold, copper, manganese and iron: 8 %
Côte d'Ivoire	Cocoa: 36 %, oil: 26 %
Ghana	Gold: 34 %, cocoa: 32 %
Guinea	Bauxit: 48 %, gold: 22 %
Mali	Gold: 69 %, cotton: 20 %
Mauretania	Iron ore: 43 %
Niger	Uranium: 20 %
Nigeria	Oil: 98 %
Senegal	Phospate: 4 %
Togo	Phosphate: 16 %, cottom: 16 %

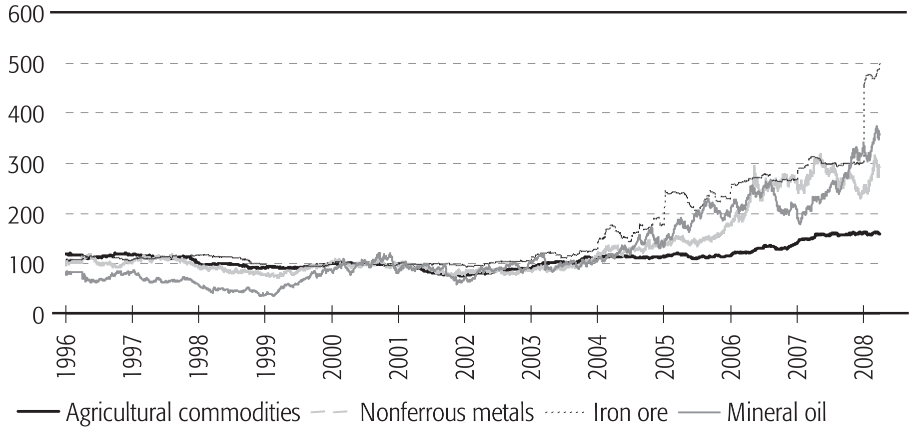
CENTRAL-AFRICA	
Equatorial Guinea	Oil and gas: 99 %
Gabon	Oil: 84 %, manganese: 3 %
Cameroon	Oil: 54 %
Congo, DR	Diamonds: 51 %, oil: 20 %, cobalt: 14 %, gold: 7 %
Congo, R	Oil: 91 %
Central African Republic	Diamonds: 66 %, uranium: 12 %, gold: 5 %

SOUTHERN AFRICA	
Angola	Oil: 94 %, diamonds: 4 %
Botswana	Diamonds: 73 %, copper and nickel: 4 %
Malawi	Tobacco: 52 %, tea: 9 %
Mozambique	Aluminum: 55 %
Namibia	Diamonds: 42 %, other minerals such as uranium: 18 %
South Africa	Precious stones: 24 %, uranium, gold and platinum: 18 %, other metals: 15 %
Zambia	Copper: 95 %, cobalt: 2 %
Zimbabwe	Gold: 16 %, tobacco:13 %

EASTERN AFRICA	
Ethiopia	Coffee: 61 %, flowers: 21 %
Kenya	Flowers: 34 %, tea: 17 %, coffee: 4 %
Sudan	Oil: 91 %
Tanzania	Gold: 42 %, cotton: 5 %
Uganda	Coffee: 63 %, tea: 14 %

Chart 12

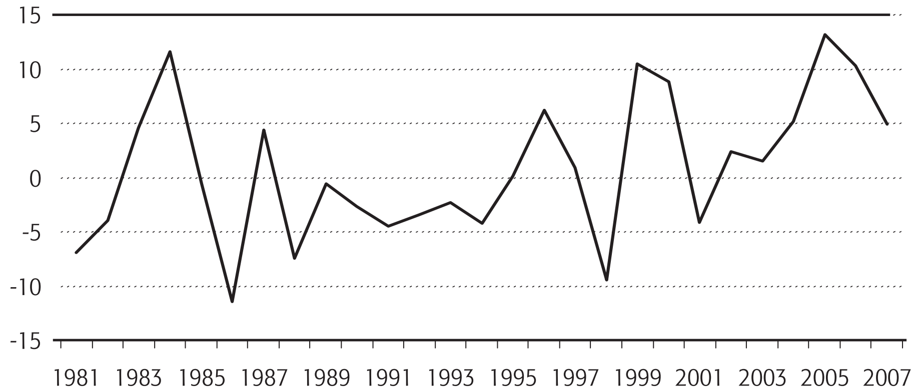
Commodity price indices of the HWWA (Hamburgisches Welt-Wirtschafts-Archiv)



Source: Reuters-Ecowin

Chart 13

Terms of trade (change in % of the ratio of export and import prices)



Source: International Monetary Fund

Higher commodity prices are also responsible for the recent improvement in the **terms of trade** of the sub-Saharan African countries. Since the beginning of this decade, this relation of export and import prices has altered clearly in favor of these countries, leading to an improvement in the standard of living. The better terms of trade can also lead to higher purchasing power, even if commodity extraction and real GDP were to decline[4].

3.6 Higher savings – more investment

Higher savings - more investment

Sub-Saharan Africa is also following the trend towards greater **savings formation** typical for many emerging markets.

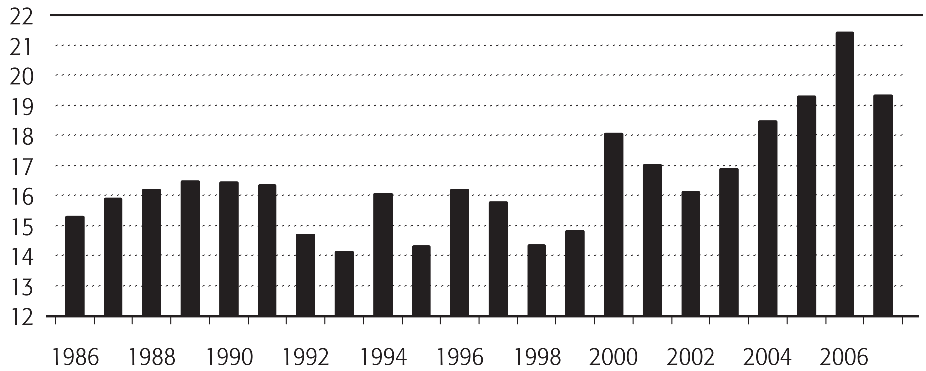
Higher savings means higher investment, thereby raising an economy's **potential growth**. This chain of effects is one of the main factors determining the economic success in the Far East where savings rates have meanwhile reached double the level of those in sub-

[4] More on this effect can be found in the Special Publication of Dresdner Bank, 2006: „An embarrassment of oil riches", Authors: I. Angermann, R. Schäfer and D. Thiesen (in particular page 4).

Saharan Africa. Chart 14 reveals a distinct uptrend in aggregate savings in Africa since the end of the nineties. While in other developing regions the formation of capital is being powered by private households and, above all, by the rapidly expanding middle class, in sub-Saharan Africa the formation of savings is likely to be propelled above all by companies via **retained earnings**, and by the state via an improved ratio of current income to spending. The higher commodity prices are also aiding the positive development as they generally raise the profits of companies active in the primary sector.

Chart 14

Sub-Saharan Africa: National savings in % of GDP



Source: International Monetary Fund

3.7 More investments by other emerging markets:

New investors: state funds

Recent years have seen a remarkable shift in financial assets in the global economy. High current account surpluses and net inflows of private capital from the industrialized countries have resulted in a veritable explosion of currency reserves in the developing countries. In the meantime, the central banks of emerging markets and developing countries account for more than 75 % of currency reserves held worldwide. They essentially consist of secure but low interest-bearing bonds in the industrialized countries. As these reserves go way beyond the countries' actual requirements, the countries have started to divert at least the new inflows into other funds which focus on riskier but higher-yielding exposures. Practically no reliable information exists on the actual capital allocation of these so-called **"sovereign wealth funds"**[5]. Due, though, to their targeted risk/ return profile the assumption is that more funds are flowing from them into exposures outside the industrialized countries. Measured in terms of the size of these funds, capital allocations of this kind could easily outweigh the annual flow of development aid. Africa can profit from this at least in the longer term. For the immediate future, though, the corporate structures represent a hindrance. This is because as a rule the capital from the "sovereign wealth funds" are flowing into large-sized companies also and particularly in developing countries. However, these remain the exception in sub-Saharan Africa.

4. PROJECTION: WHY, HOW MUCH AND WHO?

Long-term growth potential

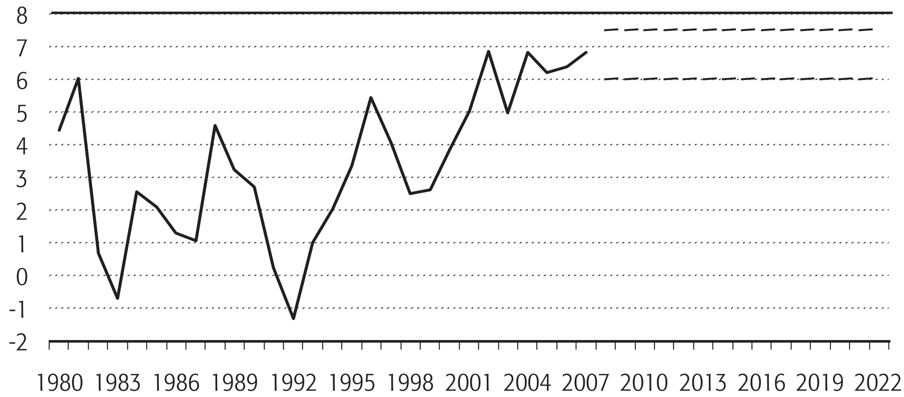
Chart 15 reveals a steady upswing in growth of real GDP in sub-Saharan Africa over approximately 10 years. One would have to look back to the early eighties of the

[5] Only a few single transactions are listed. Cf. Santiso, Javier: Sovereign Development Funds, in: OECD Development Centre: Policy Insights No. 58, January 2008.

last century to find a similarly positive economic development. At that time, too, the economic upswing was bolstered by high **commodity prices**.

Chart 15

Sub-Saharan Africa: Real economic growth (in %, 2008-2022 projection interval)



Source: International Monetary Fund, projection interval Allianz Dresdner Bank

The aspects already mentioned suggest that commodity prices will continue having a considerable influence on the region's economic momentum. This should not necessarily be viewed as negative because other states in a similar constellation, e.g. Chile, Peru and Kazakhstan, can also look back on a highly satisfactory longer-term economic development, particularly given that sub-Saharan Africa also has the possibility of raising **value added** by **processing** the domestically extracted and cultivated products. South Africa is successfully attempting this, as are the oil states in the Arabian Gulf which are deploying their energy wealth for example in the petrochemical industry or in aluminum smelting. As the value added share increases, the dependence on commodity prices declines and economic development stabilizes. Above all the countries located in southern Africa could profit from the know-how of their big South African neighbor.

In our opinion, the African countries will not be able to start an **export initiative** via **low wage products** and by so doing follow in the footsteps of the development strategies pursued in the Far East. Low wages per se do not justify an attractive location for the manufacturing industry as long as **productivity** is unable to keep pace. And the disadvantages predominate here, such as the fragmented structure of the countries which make production with high economies of scale practically impossible, not to mention the expensive transport routes and insufficient infrastructures. Sub-Saharan Africa will in any case find it extremely difficult to keep pace with the high competitiveness of the far eastern countries in this field.

Middle class - the key to success

Success in the primary sector and the higher purchasing power accompanying this will also give other sectors impetus, and these sectors will for their part also help to propel economic growth. The **construction industry** in the large cities is a case at hand. To start with, commercial construction projects exist which are then followed later by housing construction. Furthermore, a **middle class** forms in the **agglomerations** which spurs demand for higher quality products. These also include products of the **finance industry** which in the next 10-15 years will in all likelihood develop dynamically in Africa. A further glimmer of hope for a relatively manageable number of countries is also offered by **tourism** which has been hampered until now above all by the political uncertainty.

A sizeable chunk of economic output, for example farming, is either hardly or only incompletely statistically recorded. And, similar to other developing regions, the **parallel economy** accounts for a particularly high proportion of aggregate economic output in sub-Saharan Africa. Experience shows that the higher the development level, the more the **migration movements** into the formally recorded and division-of-labor economy increase, a factor also powering economic growth. This phenomenon is particularly well-known in China where migration of labor and capital contribute several percentage points to economic growth each year[6]. In Africa, this effect is certainly likely to be lower, also because the integration of the parallel economy into the formal economy is taking place relatively slowly. In South Africa, the apartheid policy came to an end more than 15 years ago. Nonetheless the economic integration of the black population majority has only been achieved to a greatly limited extent. The stokvel associations in the finance sector mentioned above are still not a part of the official banking system, with practically no statistical records existing.

All in all, these aspects point to a **long-term growth potential** of at least 6-7.5 % p.a., which would slightly exceed the annual average increase of real GDP in recent years[7]. A point to be noted is that the developing and emerging countries have generally benefited in the immediate past from an **exceptionally favorable backdrop** in the guise of flourishing world economy trade. This cannot of course be extrapolated into the longer-term future. This argues against an even more dynamic future for sub-Saharan Africa. On the other hand, we have assumed that local exchange rates will develop in line with the difference in inflation rates against the main currency markets, i.e. the **real exchange rate** will remain constant. This represents a conservative assumption, for the expected strong productivity gain would indeed allow local currencies to appreciate in real terms. This is joined by the terms-of-trade effect already mentioned above which, with commodity prices high, generates additional purchasing power and bolsters demand.

With an increase of the magnitude mentioned above, the region might well manage to keep pace with the other developing regions in the next 10-15 years and catch up economically. Assuming growth of this kind, the **glaring prosperity gap** between South Africa and most of the other countries could shrink somewhat, given that South Africa's potential growth is certainly lower than the average of the sub-Saharan African countries due, among other things, to the relatively low formation of capital there and the already advanced development level.

As already described above, the economic development within the region has always differed greatly. This development pattern will continue to accompany us in the next 10 to 15 years solely in view of the drastic differences in political stability from one country to the next as an indispensable pre-condition for economic momentum. The key question is therefore **which countries** will record continuously **high economic growth** in future. Countries with serious minority conflicts and civil wars are therefore unlikely to rank among the top group. However, this should not rule out the possibility of countries with still fragile political and economic structures finding their way towards more political stability and prosperity over the altogether long projection period. **Zimbabwe**, currently battered by appalling political and economic conditions, could be a case here, particularly considering the country's well-educated population. Generally speaking, positive developments serve as an **example worth copying**: The more countries are successful

[6] This effect is described in detail in the publication „China's long-term outlook", Allianz Global Investors: Analyses and Trends, January 2008, Authors: G. Joseph and R. Schäfer.

[7] The International Monetary Fund determines slightly lower growth rates in its published "World Economic Outlook" for the years up to and including 2013. Generally, the above-mentioned rates must be understood as annual average rates. However, from year to year strong fluctuations in real GDP can come about. A rate we project for the next 15 years would lead to a nominal GDP in USD terms approximately equivalent to Italy's in 2007.

at generating high and stable economic growth, the greater the likelihood of others following this course at a later point in time.

Stable political background conditions are the precondition for healthy economic development. Among the countries with especially high growth potential are those already able to look back on a fairly stable political phase. This is joined by the fact that **foreign investors** whose investments serve so to speak as the ignition key for economic momentum generally prefer **highly populated countries**. This is because thanks to the **higher economies of scale** the fixed costs of an operation are not felt so strongly. Finally, countries well-endowed with **raw materials** are particularly attractive for foreign capital. Naturally enough, a promising future lies ahead for those countries with readily exploitable **oil and gas resources**.

From this perspective, the countries listed below can be expected to record above-average economic growth in the next 15 years and during this phase break out of the group of developing countries and rise up to the ranks of the emerging markets.

2008-2022 TOP PERFORMERS IN AFRICA

WEST AFRICA AND CENTRAL AFRICA

NIGERIA

Oil and gas sector will continue booming. Economic success steadily spilling over into other sectors. The service sector (telecommunication, financial intermediation) currently recording growth rates (real, p.a.) of over 13 %.

CÔTE D' IVOIRE

Strong agricultural sector; world's largest cocoa producer. The export revenues resulting from this as well as the rising income from oil extraction are helping to boost the current account surplus. However, the country must still recover from the long years of civil warlike conditions.

GHANA

Politically stable. Second largest cocoa producer in the world. Besides cocoa, the country also generates the most export revenues from gold. Strong domestic market. The sectors finance, construction, telecommunication and transit transport are currently booming.

SOUTHERN AFRICA

ANGOLA

With the long years of civil having come to an end in 2002, Angola is the most dynamically growing country in Africa. The main export products are oil and diamonds. Within the domestic economy, the building trade and telecommunications are particularly booming. Attractive business possibilities opening up for foreign investors in nearly all areas.

MOZAMBIQUE

The market economy-style reforms initiated since 2004 are steadily bearing fruit. Mega projects (largest aluminum smelting works in the world, 900 km long gas pipeline to South Africa, coal and titanium extraction) will place the country on an increasingly stronger economic footing.

SOUTHERN AFRICA

ZAMBIA

Politically stable. Huge copper reserves. The drop in the price of copper plunged the country into a deep crisis. But since copper prices have rebounded, the “copper belt“ has attracted many foreign investors investing in new mines with new technology. In some cases, copper pre-processing already takes place within the country.

EASTERN AFRICA

KENYA

Largest and best-diversified economy in eastern Africa. Strong tourism sector. Coffee, tea and cut flowers are the main export products. The country is currently hoping for a new political beginning.

TANZANIA

Politically very stable for years. Economic growth rates of an average 7 %. Good climate for foreign investors. Booming mining industry (above all gold). High current account deficit at the moment, mainly thanks to import of capital goods for mining.

ETHIOPIA

Domestic economy growing strongly again after a severe drought in 2003, in particular in the sectors telecommunications, construction, mining. Main export products are coffee and cut flowers. Relatively well educated urban population.

SUDAN

Sudan‘s rapid economic development with growth rates of 9 % is attributable to oil which has been extracted since 1999. Investments, above all from the Arabian region, are continuously flowing into the sectors construction, telecommunications and transport. Current EU embargo due to Dafur crisis.