

Full Length Research Paper

Externalities of global financial crisis and coping strategies among emerging African economies

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The recent global economic recess has far-reaching implications on the stock market, employment of labour and survival of the production sector. Investors are poorly compensated, jobs are lost in thousands and hitherto viable industries are folding up. The African economy is not spared either. Policy makers and technocrats are now being challenged in an attempt to arrive at workable solutions to the current economic quackmire. In this paper therefore, several economic indicators were examined. The implications of the various manifestations of the global financial crisis on the economic indicators of the African economy were investigated. These indicators include the gross domestic product, GDP, foreign reserves, employment opportunities among the active working population and rate of inflation on consumable goods and services, level of exports and interest rates, and so on. Some stop-gap measures put in place by the African countries to circumvent or mitigate the effects of the global crisis were identified and many relevant policy frameworks were suggested for implementation. To avoid an unmanageable economic recession therefore, it was suggested that more attention be paid to the efficiency of resource use and minimization of leakages or wastages in the African economies.

Key words: African economies, coping strategies, economic recession, externalities, policy frameworks.

INTRODUCTION

Following the global financial crisis which reared its ugly head late last 2008, the level of unemployment in the United States and many European countries (particularly Britain, Germany and France) hit all-time high levels (IMF, 2009). The number of people on low wage part-time jobs had spiralled in those countries. Again, there are observable frenzied stock markets and social dislocations in these hitherto booming economies. The general manifestation of this scenario is that there is a negative growth across the various sectors in most developing economies. In addition to this, it is very clear that no African country is safe from the global financial crisis and slowdown in the over- all global economic growth. Given

the inter-linkages in the global economy, policy makers also foresee the global slowdown will invariably reduce the demand for African exports. This has already been reflected in the demand for and prices of commodities in African countries. For South Africa and Egypt, there was an appreciable increase in the demand for exports and non-factor services between year 2000 and 2008 while the story was different for Nigeria and Ghana.

However; there was a general increase in the demand for imports and non-factor services by South Africa, Egypt and Ghana within the same periods (Table 1).

In his paper titled: 'What the Global Financial Crisis Means for Sub-Saharan Africa,' Takatoshi (2009)

Table 1. Africa growth of demand for exports and imports of goods and non factor services.

Country	EGS		IGS	
	2000-2006	2007-2008	2000-2006	2007-2008
	(Average)%	(Average)%	(Average)%	(Average)%
Nigeria	5.2	-6.3	7.8	7.7
South Africa	4.0	10.3	9.0	11.0
Kenya	6.0	7.6	7.9	4.9
Egypt	12.1	23.3	7.6	28.5
Ghana	3.5	1.0	5.4	10.2

Legend: EGS=Exports of Goods and Non-Factor Services. IGS=Imports of Goods and Non-Factor Services. Source: IMF Quarterly Reports, 2009.

Table 2. Africa real GDP growth rates (frequency distribution).

	1990-'99	2000-'05	2006	2007-2008
Negative	5	4	2	3
0-3 %	24	13	11	10
Above 3 to 5 %	15	21	7	14
Above 5%	7	14	32	25
Not available	2	1	1	1
Total	53	53	53	53

Source: IMF Quarterly Report, 2009.

rightly observed that the world's growth was expected to come to a virtual halt, which would require a decisive global policy response. Quite unfortunately, despite wide-ranging policy actions by governments and Central Banks around the world, financial strains remained acute, pulling down the real economy. Given strong policies to stimulate the recovery, it is expected that world's economy will again experience growth in 2014. IMF (2009) noted that even in the second half of the year, many advanced economies are still experiencing their deepest recession since World War 11 (Tella, 2009; World Bank, 2009).

Major emerging economies such as China, India and Brazil are now expected to experience much lower growth than in recent years. This has been dragged down by falling export demand, subdued capital inflows and generally lower commodity prices. Again, unemployment rates, rates of inflation and banks, lending rates have been heightened.

It should be added that the major economic indicators which manifested positive development in the industrialized economies are now redressed at all-time low levels. These indicators include the gross domestic product, GDP, buoyant foreign reserves, high employment opportunities among the active working population and low rate of inflation on consumable goods and services. Others include high level of exports and moderate interest rates, and so on. For instance,

between 1990 and 1999, only 39 out of 53 African countries had real GDP growth rate of 5 % and below while just 25 of these countries had above 5 % between 2007 and first quarter of 2009 (Table 2).

MATERIALS AND METHODS

Purely secondary data were used for this study. These data were obtained from various World Bank and IMF reports/bulletins (all published), Statement of Accounts of the Central Bank of Nigeria (CBN), textbooks, published journal articles and so on. Data used for the study covered some 18 years that is 1990-2008. Information was collected on national GDP levels, rate of inflation, interest rates, growth rate of the economy, employment rates, money supply levels, import and export levels, among others. Descriptive statistics such as mean, median, mode, frequency tables and other measures of central tendencies were used to analyse the data.

RESULTS

According to the IMF (2009), Africa's aggregate GDP at current market prices increased to US \$1,232.6 billion in 2007 from US\$ 1,083.51 billion in the previous year. This figure later dropped to US\$ US\$1,034.2 billion in the first quarter of year 2009 (CBN, 2009). The IMF (2009) added that, for some emerging economies, the GDP at current market prices in 2007 stood at US\$273 billion (for South Africa), US\$124 billion (for Nigeria) and US\$30.0 and US\$129 billion for Kenya and Egypt, respectively. On the whole, the Africa's rate of growth of inflation ranged between 7.0 and 10.3 % between year 2000 and 2007 while the rate of growth of money supply was between 17.5 and 26%. In the same vein, the contribution of net foreign balance to GDP growth (1990-1999) averaged 0.2 while it sharply dropped to -2.3 and -2.8 in 2007 and first quarter of 2009 respectively.

For the same period, the contribution of exports of goods and services averaged 1.5% between 1990-1999 rose to 2.6% in 2007 and then dropped to 2.4% in the first quarter of 2009. Between 2000 and 2007, the average consumer price inflation (%) for Nigeria, South

Africa, Kenya, Egypt and Ghana stood at 12.7, 6.2, 9.2, 6.0, and 18.7, respectively. The situation became worse between 2008 and the first half of 2009 due to the global financial crisis.

The exchange rate indices such as the nominal exchange rate and real exchange rate indicated a general decline in the strength of the local currencies. This development has a negative implication on the purchasing powers of many Africans and indeed those of their entire households. To avoid an unmanageable global economic recession therefore, it is important that more attention be paid on the efficiency of resource use and minimization of leakages or wastages.

DISCUSSION

Externalities of global financial crisis and African economies

Towards the end of the year 2008, there were insinuations by key policy makers in African countries to the effect that the rampaging global financial crisis would not affect African continent. They were however proven wrong within the first quarter of year (2009) when many Africans working in many of the developed countries such as the United States, Canada, Britain and Germany started losing their jobs in thousands. This negatively affected their remittance to home countries. Indeed, there is a growing pressure on these workers to return home due to the crisis in the employment markets in their host countries overseas. In addition to this, Nigeria, Ghana, South Africa and Kenya, among others, had by April 2009, experienced sharp drop in stock exchange, market capitalization, reduced budgetary revenues, falling external reserves and general market depreciation (Balogun, 2009). Except one tries to pretend, which is no longer possible, the global financial meltdown is having an excruciating effect on the African economies.

Generally, speaking, weaker financial linkages with the rest of the world may have limited the impact of the systematic banking sector crisis in advanced economies in Africa. The continent will however be hard hit by the effects of the ensuing slowdown in global economic growth. For example, according to Takatoshi (2009), the harsh reality of lower global growth reduces the demand for African exports, pushes commodity prices downwards and curtails the flow of remittances from abroad. It was also noted, World Bank, (2009), that the tightening of global credit had reduced capital inflows and pegged down the availability of trade finance. This could cause donors to reduce their aid to Africa. In addition, the economic slowdown may affect the quality of the credit portfolios of financial institutions and impose losses on other financial assets.

These include deposits with troubled foreign correspondent banks or capital repatriations by troubled parent banks, which are often foreign -owned.

The slowdown in trade has again reduced government revenues; thereby worsening the fiscal position in many countries. Fewer resources would mean that African governments would be unable to meet the heightened expectations of their populations for progress in reducing poverty and investing in infrastructure. With the expectation of a more pronounced global downturn, weaker commodity prices and higher pressure on capital flows, the level of growth in the economies of the African countries slid from about 5.25 percent in 2008 to about 3.25 percent in 2009 (IMF, 2009). With significant uncertainties at the global level, risks to growth of the economies of African countries remain tilted to the downside. For many African economies, major determinants in both the fiscal and external accounts are anticipated. This development does not augur well for a meaningful economic growth in the continent. It is now clear that no African country is safe from the global financial crisis and slowdown in the overall economic growth. Recently, the major stock and foreign exchange markets on the continent are having the worst of their business life. This development has forced shareholders to dispose off their shares, thus leading to devaluation in the real estate market.

Moreover, there is a concern over the capital inflow into the African economy and limited availability of trade financing arising from global credit crunch. To this end, the more the African countries appreciate the magnitude and implications of the present economic realities, the more the need to look for the necessary solutions. Specifically, the recent reports by the Central Bank of Nigeria and Ministry of Finance on the assessment of the Nigerian economy in the first quarter of 2009 revealed that oil price collapsed to average of USD 40.00 per barrel, (CBN, 2009). Government revenue also declined by 32 percent for the same year compared to the projected income.

The interest rate and inflation rate rose to all time high levels while the non-oil receipts fell. Only 22 percent implementation of 2009 budget could be achieved (for the first half of the year) and there was a marked reduction of credit levels to private sector. Rate of unemployment also increased further as government spending on workers' recruitment was cut down. In Ghana, as pointed out in the World Bank Report (2009), the current global financial crisis has brought about the fuel and food crisis. The situation has again been exacerbated by the droughts and floods in the Northern parts of the country. In South Africa, growth in demand for credit by private sector slowed more than expected to 14 per cent year-on-year in December 2008. The expansion of demand for credit dropped from 15.3 percent in November 2008 to 9.5 percent in March 2009 (World Bank, 2009). There has also been a sharp decline in both consumer and producer price inflation. The growth in credit aggregates has come off quite sharply. This just supports the case for an aggressive rate cut.

Coping with externalities of global financial crisis in Africa

The devastating effects of the global financial crisis cannot be allowed to continue unabated. As a result, different stop-gap macro-economic measures have been put in place by African countries in an attempt to at least cushion the effects of the crisis. For example, the World Bank (2009) suggested that Nigeria, whose economy is largely dependent on oil, should urgently device other aggressive sources of government revenues. This suggestion becomes necessary in view of the unprecedented decline in the market price of crude oil to all-time low level of USD 38.5 per barrel in March 2009. This situation fairly improved to USD 60.23 per barrel in July, 2009.

Again, the banking regulatory authorities, the Central Bank of Nigeria (CBN) and the National Deposit Insurance Corporation (NDIC) are mandated to urgently strengthen their supervisory roles to guarantee banks' transparency in whatever assets they declare on their balance sheets.

Another device by the Nigerian government to protect the economy from further hurt was the slashing of the salaries of the public office holders. Under this dispensation, for example, senators and members of House of Representatives have their constituency allowances slashed from 250 to 125 percent and 150 to 75 percent, respectively.

The Nigerian government also sought and obtained USD 59 billion loan from the World Bank to help her overcome some of the teething economic problems occasioned by the recent global financial slowdown. The latest effort by the Central Bank of Nigeria to address the crisis in the financial sector was the reduction in the lending rates to banks (monetary policy rate) from 8.0 to 6.0 percent: a 200 basis point reduction.

The CBN also reintroduced the interest rate corridor of plus or minus 200 basis points, with the rate on the standing lending facility at 8 percent and the rate on the standing deposit facility at 4 percent with immediate effect. It is expected that this measure will help close the gap between the inter-bank rates and the monetary policy rate. On foreign exchange, the CBN reversed to Wholesale Dutch Auction System (WDAS) in place of Retail Dutch Auction System (RDAS). It equally removed all other restrictions on trade and increased banks' net open position from 2.5 to 5.0 percent.

As a way out of the present global financial imbroglio, the Ghanaian government applied for and secured USD 535 million from the World Bank. The situation was brought about largely by the fuel and food crisis that resulted from the global financial and economic mess. Again, the IMF (2009) has canvassed that all African countries must set aside more money for the IMF to buoy the Fund's resources so that it can always come to the rescue of member nations at times like this. The present

global economic challenge has again provoked, particularly in Nigeria, the establishment of small scale entrepreneurship and microfinance schemes to empower domestic economic operators. This exercise will surely increase the aggregate domestic output and household income levels.

To further increase the activities of the entrepreneurs therefore, governments of African nations must, as a matter of urgency, address and ease all forms of regulatory obstacles to business like barriers to entry, convoluted taxation, property registration and licensing. Again, credible insurance corporations should be capitalized to be able to absorb the financial shock in the African economies.

However, it must be emphasized that there is no single recipe for the financial and economic crisis as it affects African countries since each economy has its own peculiarities and priorities.

CONCLUSION AND POLICY RECOMMENDATIONS

Conclusion

The global financial crisis is here with us in Africa. People can no longer pretend about this. But there is the need for the African governments to channel ways by which to overcome it. This is a mandate for the African leaders to suppress the devastating effects of poverty, malnutrition and other social maladies confronting the African countries. Some stimulus may however, be needed from the governments of those countries that have the economic wherewithal. This, if provided in good time and quantities, will produce the expected stop-gap devices to neutralize the effects of the financial mess. Though there is no single recipe to adopt as a general solution to the global financial cum economic problem, good supervisory and regulatory roles by the banks will ensure a better financial discipline in the banking sectors of the African economies. Aggressive drives by African leaders in finding solutions to the current socio-economic mess is necessary as it will prevent this continent from sinking deeper into brutal economic recession.

Policy recommendations

Since the circumstances differ across African countries, there is no single recipe to overcome the effects of global financial crisis. However, the following policy challenges have been found relevant by the IMF to all African countries.

This becomes necessary in order to protect the hard-won improvements in economic fundamentals that is, more sustainable debt levels, lower inflation, liberalized trade and structural reforms. The following few principles could guide the economic policies of African nations particularly

at a time like this:

1. Exchange rates should be used to rebalance the economic growth:

In countries where the terms of trade deteriorated, real exchange rates will have to depreciate to preserve macroeconomic stability. Countries with exchange rate flexibility should let the nominal exchange rate depreciate while keeping fiscal and monetary policies sufficiently tight to avoid devaluation –inflation spiral.

2. Need for Judicious use of the fiscal space

Fiscal responses should be tailored to specific country circumstances. There may be scope for a fiscal stimulus in some countries but, in many other countries, this option may not be available due to already weakened fiscal positions and concerns regarding fiscal sustainability. In some countries, there may even be a need for fiscal consolidation. In all cases, spending plans should be cast in a medium-term context, with targeted measures to protect the most vulnerable.

3. Need to monitor the balance sheets of financial institutions

Governments of African countries should identify the vulnerabilities of the banking system and plan how they will react should a banking crisis erupt. The liquidity and usability of reserve assets, the status of non-performing loans in the banking sector and the availability of trade credit deserve some particular attention.

4. Focus on Medium-term goals

The gloomy environment puts an even higher premium on keeping African economies in a stable form. It is now important to make every effort to move ahead with the

planned structural reforms. The current crisis should be seen as an opportunity to foster domestic consensus for urgently needed reforms in Africa.

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