KEY NOTE ADDRESS

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- **Distinguished Panellists,**
- **Ladies and Gentlemen**

1. It is a great pleasure for me to address the 2021 NCBA Economic Forum, under the theme "**Regional Economic Outlook 2022: Sustaining growth in an uncertain and volatile environment**". This Forum is being organised at a time when the world is grappling with the COVID-19 pandemic, which has destabilized our healthcare systems, societies and economies in a significant way. On the economic front, we have witnessed significant slowdown in economic growth and at times, economic contractions in many countries, resulting in historically low growth rates. Trade has been disrupted, domestic revenues and foreign exchange receipts have dwindled substantially, while public financing requirements are rising as part of governments' efforts to contain the pandemic and protect the vulnerable groups.

2. My task is to provide a regional macroeconomic outlook and discuss recovery prospects amidst growing vulnerabilities. I will limit my discussion to six (6) countries in the East African Community (EAC) region namely; Burundi, Kenya, Rwanda, South Sudan, Tanzania and Uganda. Five (5) of these are MEFMI member countries. I will divide my presentation into four sections: (i). Recent Macroeconomic Developments; (ii). Medium-Term Outlook, (iii) Risks factors, and (iv). Policy priorities.

A. RECENT MACROECONOMIC DEVELOPMENTS

The COVID-19 pandemic has taken a toll on people's health, safety and global socio-economic development. The year 2020 is described as a year of **"great lockdown"** and IMF referred to COVID-19 as a **"crisis like no other".** For the first time, almost all regions registered negative growth with global growth contracting by 4.9 percent in real terms. Merchandise trade declined by 8.3 percent while trade in commercial services contracted by 21 percent year-on-year. This was mainly driven by the magnitude and persistence of the adverse shocks as the world tried to contain the COVID-19 pandemic.

3. The East African economies also imposed travel restrictions and border closures, together with isolation and quarantine policies. These policies had profound economic implications such as business closures and scaling down of some operations, reduction in labour force, decrease in productivity affecting regional supply chains, vulnerability in both low and high-risk groups of the population, drop in spending, weaker consumer confidence, health crisis, dramatic tightening in global financial conditions, plunge in commodity prices, weaker external demand as well as funding shortfalls.

4. East Africa is the only region in Africa, however, that avoided a deep recession in 2020 due to strong performance in agriculture and

resilience in the services (financial and telecommunication) sector which were the main drivers of economic growth, boosted by sustained public spending on large infrastructure projects. The region registered an average economic contraction of 1.5 percent in 2020 from an average of 5 percent growth between 2018 and 2019. The hardest hit countries were South Sudan and Burundi, where economic activity was already on a weak footing before COVID-19, with output falling by 6.6 and 2.1 respectively. Kenya, Tanzania, and Rwanda registered modest growth owing to the resilience of their financial sector, and quick stimulus packages.

5. Despite high inflation in East Africa, averaging 10 percent in 2020 and the highest on the continent, 5 of the 6 countries recorded single-digit inflation due to stable food inflation, lower energy inflation in the first quarter of 2020 and subdued demand. Factors that affected food supply and added inflation pressures in the region included the disruptions in global supply chains due to COVID-19 and adverse weather events (including drought, floods, and desert locust invasions) in some countries. Currency depreciation has also lifted prices of imported goods, further adding to overall inflation as the main factors weighing on the recovery.

6. Despite widening in 2020, East Africa's fiscal deficit was lower at 6.3 percent of GDP than Africa's average of 8.3 percent. Elevated fiscal deficits in 2020 were mainly due to falling domestic revenues resulting from subdued economic activity, tax measures introduced

to mitigate the socioeconomic impact of COVID-19, import-intensive public infrastructure investment, and sluggish export performance.

7. Public debt in East Africa has been rising since 2011, driven by large infrastructure investments and a relative slowdown in real GDP growth. Public debt increased further to 54.7 percent of GDP in 2020, from 47.4 percent of GDP in 2019, due to substantial nominal exchange rate depreciation in economies with large foreign currency debt, reduced commodity revenue inflows, and borrowing to finance emergency public spending in healthcare.

8. External public debt, like that of many countries in Africa, has become more market-based and less concessional, with the grant element of new external commitments reduced by almost half over the past two decades. This change has increased rollover risks and increased debt vulnerabilities. During the 2019–20 period, Kenya's public debt rose 19 percent, leading to the country's reclassification from a low to high risk of debt distress. Rwanda and Uganda were reclassified from low to moderate risk of debt distress during the same period. By contrast, in Tanzania, where the fiscal position, exports and debt levels remained stable, the risk of external debt distress remained low.

9. East Africa's external current account deficit improved slightly between 2019 and 2020, from 10.2 percent to 7.8 percent of GDP,

but was still higher than Africa’s average of 5.5 percent. Countries that saw their current account balances improve between 2019 and 2020 included Kenya, Rwanda and South Sudan, while the ones most adversely affected included Burundi, Tanzania and Uganda. Kenya’s improved current account position was aided by a sharp reduction in the oil import bill. Most current account deficits in the region were financed by grants and external debt, as other financial flows, including foreign direct investment (FDI) declined.

10. Gross foreign exchange reserves have deteriorated in some countries in East Africa but have largely remained within the countries’ thresholds of 3 months of import cover. Still, other countries have precariously low foreign exchange reserves. South Sudan’s reserves, for instance, remain weak and fragile, at 0.4 month of imports cover in 2020.

B. MACROECONOMIC OUTLOOK

Ladies and gentlemen, let me present to you the outlook based on each country policy intervention in the medium term.

11. The global economic activity is estimated to improve to 6.0 percent growth in 2021 and 4.9 percent in 2022. During the same period, the average growth for the East Africa region will also be expected to recover to 5.1 and 5.4 percent, respectively, at the back of improved global control of the pandemic in relation to vaccination, strong domestic activity, particularly in primary

activities (agriculture and mining), resilience of their service sector as well as spillovers from strengthening global activity. Oil and commodity-exporting countries in the region including South Sudan (oil), and Tanzania (gold) are expected to benefit from rising prices during the period.

12. Fiscal deficits are projected at 4.4 percent of GDP in 2021 and 2.4 percent in 2022, a significant improvement from the estimated 6.3 percent in 2020. The projected improvement in the region's average fiscal deficit will be strongly boosted by Tanzania and South Sudan, driven by ongoing and anticipated improvements in global commodity prices. However, Burundi, Kenya, Rwanda and Uganda are projected to have fiscal deficits above 5 percent in 2021 and 2022.

13. East Africa's inflation is expected to ease in the medium term, supported by prudent monetary policies and improved food supplies. But rising oil prices may increase inflation in some oil-importing countries. The region's inflation is projected to ease to 10 percent in 2021 and drop further to 9 percent in 2022 as global supply chains reopen, but rising oil prices are expected to put pressure on non-food inflation. The high average inflation projected for the region is due to projected hyperinflation in South Sudan, due to supply shocks induced by recent floods and desert locust invasions, COVID-19 disruptions, monetization of the 2019/20 deficit, and currency

depreciation, but it will ease progressively due to tight monetary policy. In Tanzania and Uganda inflation is expected to edge up due to the impacts of higher oil prices on non-food inflation. Kenya continues to enjoy low inflation and is expected to remain within the authorities' target band of 5.0 plus or minus percent thanks to prudent monetary policy, favorable weather conditions, and stable demand for non-food items.

14. The region's current account balance, the highest deficit among Africa's regions, is projected to narrow to a deficit of 6.8 percent in 2022, down from 7.8 percent in 2020. Higher exports will help narrow the region's current account deficits, but overdependence on a few commodity exports in some countries is a source of vulnerabilities. Burundi and Rwanda are projected to report double-digit current account deficits in 2021 and 2022, largely because of sluggish recovery of exports and remittances that suppress foreign exchange receipts. Uganda's current account deficit is projected to narrow as exports pick up, reflecting global economic recovery.

C. RISK FACTORS

15. Lockdowns associated with the Covid pandemic reduced physical business interaction. There has been an increase in uptake of digital banking Channels. This has improved on resilience and financial inclusion. At the same time it has also presented growing exposure to cybercrime. Incidents like quality control lapses, identity theft,

hacking of credentials, and other fraudulent activities have exposed the soft underbelly of the new economy.

16. Rising global oil prices are a major downside risk given that most East African countries are net oil importers. Though the anticipated increase in oil prices is good news for the region's few oil-exporting countries, it remains a major risk to the economic recovery for the rest. Forecasts project a consistent increase in global oil prices from US$41 a barrel in 2020 to US$65 a barrel in 2021, and a possible US$66 a barrel in 2022.

17. COVID-19 has exacerbated the region's already worrisome debt situation, with many countries' cost of debt service and risk of external debt distress increasing. Increased budget allocations to debt financing and the drawdown of foreign exchange reserves to meet external debt service obligations reduces the scope for sustained public investments in transformative infrastructure. Given that real GDP growth in several East African countries is driven by public investments, these factors will slow the region's growth prospects and advancements towards Sustainable Development Goals (SDGs).

18. New waves of COVID–19 infections and slow uptake of vaccines remain major risks to recovery in East Africa. The new waves have already led to reintroduction of lockdowns and quarantines in Kenya

and Uganda, and these could expand to other countries in the region slowing or derailing the region's recovery.

19. Conflict-related events and incidents heighten policy uncertainty and dampen investor confidence. Civil unrest in a few countries in East Africa remain a threat to national and regional cohesion and socioeconomic progress.

20. Weather-related shocks and invasions of locust swarms threaten agricultural production in East Africa. Some countries in the region were invaded by desert locusts in 2020, and a second wave of invasion is already being experienced in Ethiopia, Kenya, and Somalia. This is likely to remain a significant risk to the region's recovery because agriculture employs about 60 percent of workers, contributes more than a third of GDP, and accounts for over 60 percent of merchandise exports in the region. In addition, unpredictable weather conditions pose a major risk to the region's agricultural production, given the recent history of frequent droughts and floods.

D. POLICY PRIORITIES

Allow me to conclude by proposing priority policies and reforms needed to get East African economies back on the path of strong economic growth and structural transformation.

21. The Cyber risks should be addressed using a three pronged approach as follows:

a. Taking a system wide approach to cyber risk management, assessing system interconnectedness and attack vulnerability.
b. Strengthening partnerships between private and government sector entities to deal with emerging cyber risks. The goal should be to use cyber resilience to enable business growth.
c. Continuously maintaining a culture of trust, flexibility and transparency, supported by a regular pulse check (feedback loop).

22. In 2020, several East African governments instituted fiscal and monetary policy measures to cushion their economies from the impacts of COVID-19. To cement the gains achieved with the stimulus packages, the **measures should be withdrawn gradually, in a phased manner.**

23. Faster recovery in East Africa will depend on **how quickly large portions of the population can develop immunity against the virus through vaccinations.** The authorities should take bold steps to procure more doses of the vaccines and encourage people to take them. These efforts should involve **public health education and awareness campaigns to debunk the conspiracies surrounding the vaccines.**

24. Though the development needs of many East African countries remain enormous, the resources available to meet those needs have declined due to COVID-19. To maintain reasonable fiscal space, countries must **reprioritize recurrent spending and reschedule nonpriority development projects.**

25. Containing further waves of the pandemic and avoiding harsh lockdowns will require beefing up health systems in almost all of East Africa. More resources should be directed towards strengthening heath infrastructure and human resource capacity to curb further spread of the virus. In addition, public awareness campaigns should promote adherence to public health protocols for containing the virus.

26. **To restore fiscal stability, accelerating domestic resource mobilization remains a priority in the region.** Domestic tax collection efforts remain low in many East African countries relative to Southern African peers. Though low tax effort does not necessarily imply the need to raise taxes, it signals the potential for increasing tax revenues by making tax administration more efficient and broadening the tax base.

27. Many East African countries have increased their debt to bridge the financing gap caused by COVID-induced weak revenue performance. But this debt has significantly increased debt vulnerabilities in many countries. Part of the short-term solution lies in **debt restructuring, debt rescheduling, and debt service suspension.**

28. East Africa has the potential to boost private investment to help its countries tap the benefits of formality, such as ease of access to credit. Governments should put more effort into identifying firms that could broaden their tax bases in, say, agriculture. This would also ensure that informal businesses are registered and have access to formal credit facilities as they become more productive and can extend social protection to workers.

29. Several East African countries heavily rely on public financing of development projects and rarely tap into the diverse array of private sector financing sources. Governments can promote the use of several innovative non-sovereign financing mechanisms to bridge the public financing gap. These include blended finance, and public-private partnerships (PPPs).

30. The broader issue of strengthening public financial management remains at the core of streamlining public spending in many developing countries, including those in East Africa. One of the main concerns about public financial management in these countries

is the lack of proper investment planning. In some countries, especially where governance challenges abound, public investment decisions, particularly on big projects, are still based on political considerations rather than economic and financial viability.

31. East African countries should work closely with development partners and other stakeholders to strengthen their capacities to manage public debt. These efforts should include developing capacity to devise contingency plans for refinancing external and domestic debt.

32. East African countries remain exposed to external shocks, so there is a need to build mechanisms to absorb them. Some of the region's countries that were most severely affected by COVID-19 are those that are least economically diverse. Building resilience in such countries will require diversifying the economies and the export base. East Africa's exports should be oriented towards other emerging markets, including those covered by the African Continental Free Trade Area (AfCFTA).

33. The goal of these proposed strategies is to preserve livelihoods in the short term while maintaining debt sustainability in the medium term and building economic resilience in the long term.

34. Ladies and gentlemen, challenges we face for economic recovery from COVID-19 depend on how quickly the disease can be brought

under control, how quickly consumer and investor confidence can be restored, whether companies are able to find substitutes for parts of their supply chains that are disrupted, and the effectiveness of actions taken to support workers and companies to prevent widespread bankruptcies, extended job losses, and system-wide financial strains. But more importantly, we need to guard against the recurrence of new waves and variant.

35. When considering prospects of our policy challenges, two issues must be carefully analyzed; one - the need for fiscal policy to support aggregate demand including vaccination policies; two - the need to evaluate the duration or withdrawal of containment fiscal support as economies recover. The regional fiscal outlook has brightened significantly, with deficits forecast at 4.4 and 2.4 percent of GDP in 2021 and 2022, respectively. Let us use the improved economic conditions to rebuild economic buffers and strengthen ou resilience to future shocks.

36. **Ladies and gentlemen**, I thank you for listening to me.