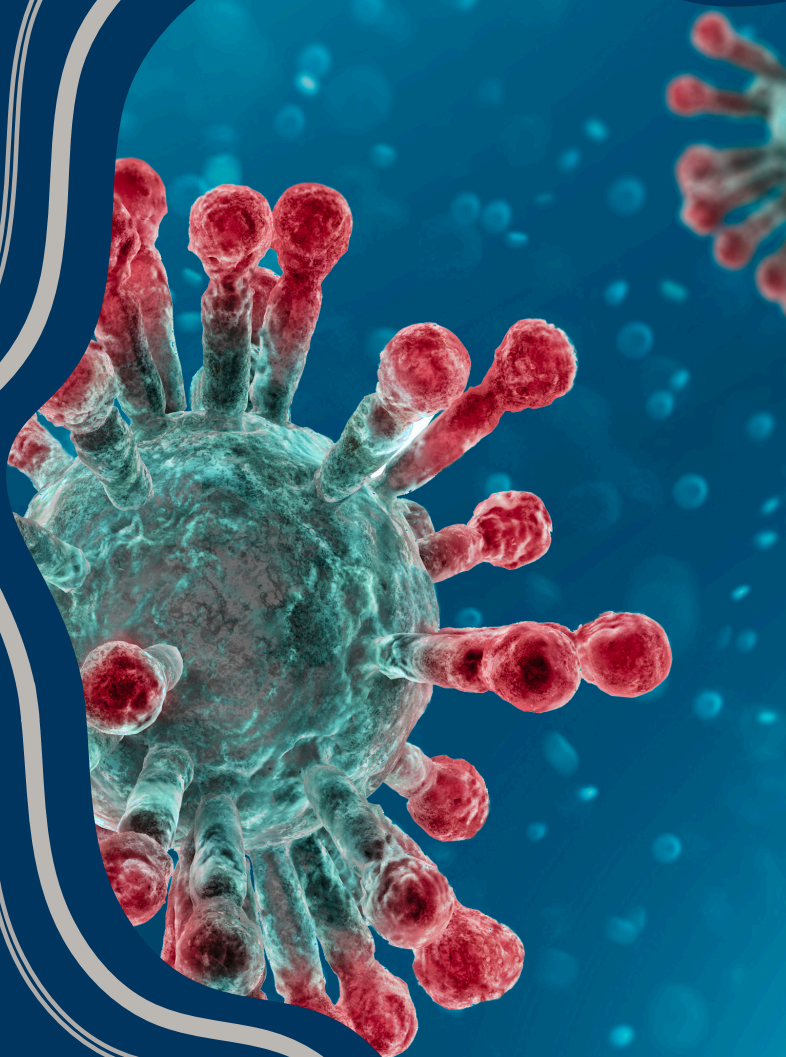




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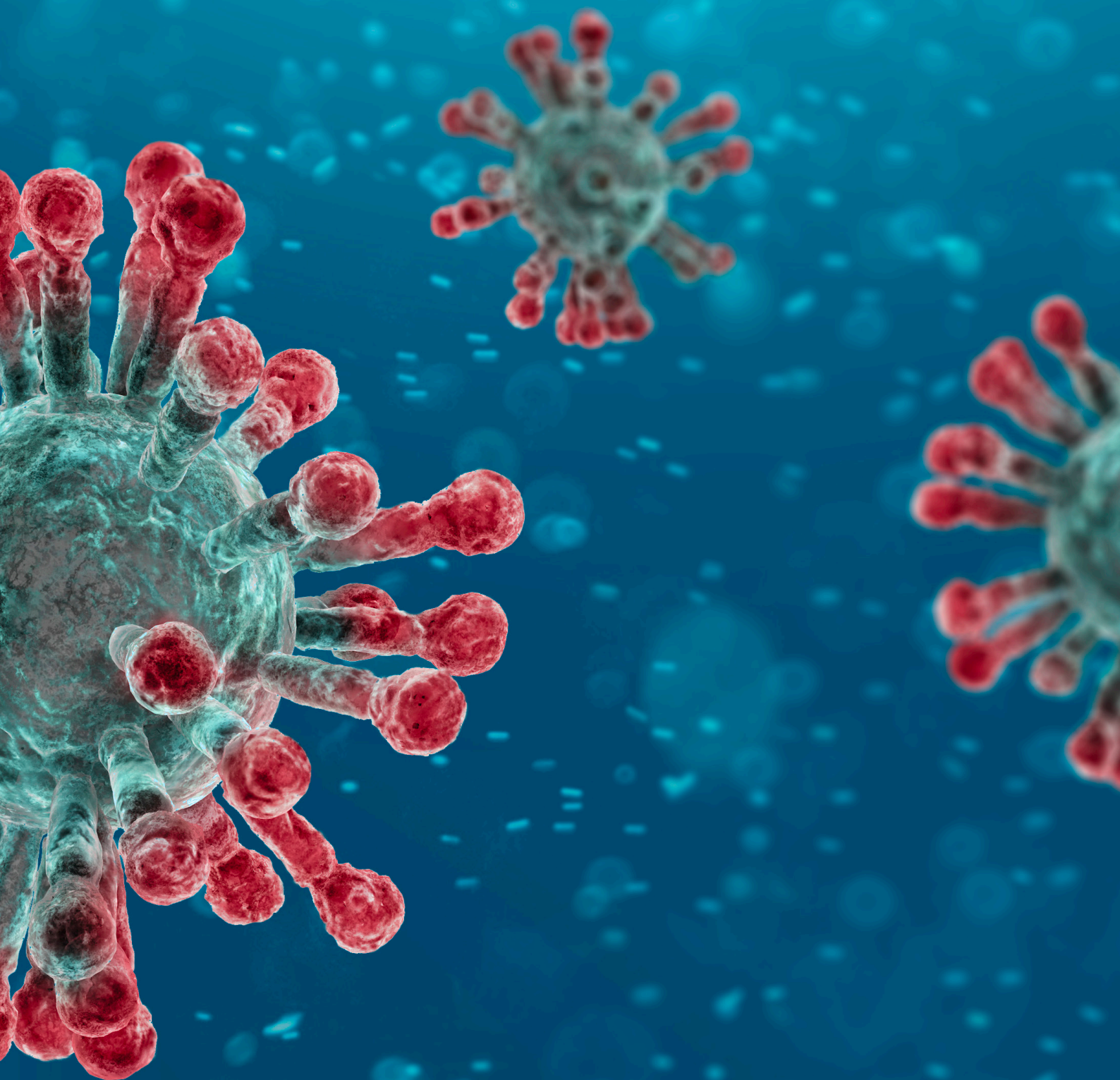


AFRICA INSIGHTS

COVID-19 - ECONOMIC IMPACT
ON EAST AND SOUTHERN AFRICA



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Research by Nina Callaghan, Centre for Complex Systems in Transition, Stellenbosch University in collaboration with Bowmans

Foreword

We understand that our clients and other stakeholders may well be inundated with comment and information from professional service firms, including perhaps our own. And no more so than right now, with the global health crisis and its consequent economic fall-out gripping the world.

While we do not want to add to an unnecessary burden of information, we do want to talk to our clients on a regular basis about things that are causes for concern for them, or that are generating optimism or excitement about business opportunities.

To this end, we have entered into a unique research collaboration with the University of Stellenbosch's Centre for Complex Systems in Transition.

At the core of the Centre's work is the drive to find, 'ways of living that sustain rather than destroy the eco-system within which all society is embedded'. This purpose resonates with our vision as an African law firm, supporting our clients and our people, as they seek to unlock opportunity, overcome challenges and realise the hopes that will shape the future of Africa.

Our aim, through this collaboration, is to generate critical analysis of economic, social and

business issues that affect the markets we serve, and to share insights with our clients on a regular basis throughout the year.

This is the first publication in the series.

It is probably no surprise that it contains our early assessment of the unfolding economic fall-out resulting from the COVID-19 public health crisis and in particular the possible economic impact on East and Southern Africa.

We hope that you will find it interesting and useful and that it will provide some insight into the African markets that are our home.

Please look out for subsequent publications in the series. And, of course, we would welcome any feedback you may have.

Robert Legh
Chairman and Senior Partner

Summary

The rate and global spread of infections by the coronavirus (COVID-19) - and the related sense of panic across a globalized financial, political and social architecture - sets this particular pandemic apart from any other in modern times.

As at 23 March 2020 the total number of confirmed infections had reached over 375 000 in 196 countries with 16 362 deaths (WHO). In a matter of two months COVID-19 has reshaped our ideas about being socially connected, economically entangled and existentially unprepared for radical change.

Quarantine and social distancing measures, travel bans and restrictions, closed regional and national borders and health communications have been ratcheted up globally to reduce the chance of exposure as infections and fatalities continue to rise. As China has demonstrated, only stringent aversion behavior is able to control COVID-19's spread. The World Health Organization (WHO) has criticized some governments' slow early response, especially those of advanced economies. They accuse these countries, especially in Europe and North

America, of not understanding the science and the pattern of COVID-19, calling their early efforts at managing a public health emergency 'too little, too late' (Oqubay, 2020). Europe has now become the new epicentre of the virus after China's measures to contain and control its spread show promising signs. Since March 2020, new cases of COVID-19 in China have dwindled to less than 1% (Oqubay, 2020). Italy has now surpassed China's confirmed cases and deaths, reaching 53 578 and 4 827 respectively, as at 23 March 2020.

COVID-19 in Africa

The WHO says just over 1 500 positive cases of COVID-19 have been recorded in 48 African states (WHO, 23 March 2020). Twelve countries in Africa are now experiencing local transmission and with vastly different population demographics, the shape and impact of COVID-19 in Africa could look very different from Europe, Asia and North America.

Testing kits and medical supplies have been shipped to several countries on the continent, enabling 45 African nations to now test for the virus, as opposed to just two at the start of the outbreak in January (WHO, 2020).

WHO has also been supporting government health ministries across Africa, training 36 rapid response teams. These trainings aim to improve their surveillance and contact tracing abilities, along with data collection, reporting and diagnosis (Wang, 2020).

AFRICA'S HEALTH VULNERABILITIES

COVID-19 is said to affect the elderly more than other age groups. Africa is a world region that has the youngest population compared to other world regions. However, vulnerability to COVID-19 in Africa is more related to underlying health conditions, of which Africans have a disproportionate share.

The WHO estimates there are 26 million people who are HIV positive in the region, a condition that compromises the body's immunity. Over 58 million children in Africa are malnourished and suffer from stunting, making it entirely plausible that younger people in Africa could be much more susceptible to COVID-19 (WHO, 2020) than other world regions.

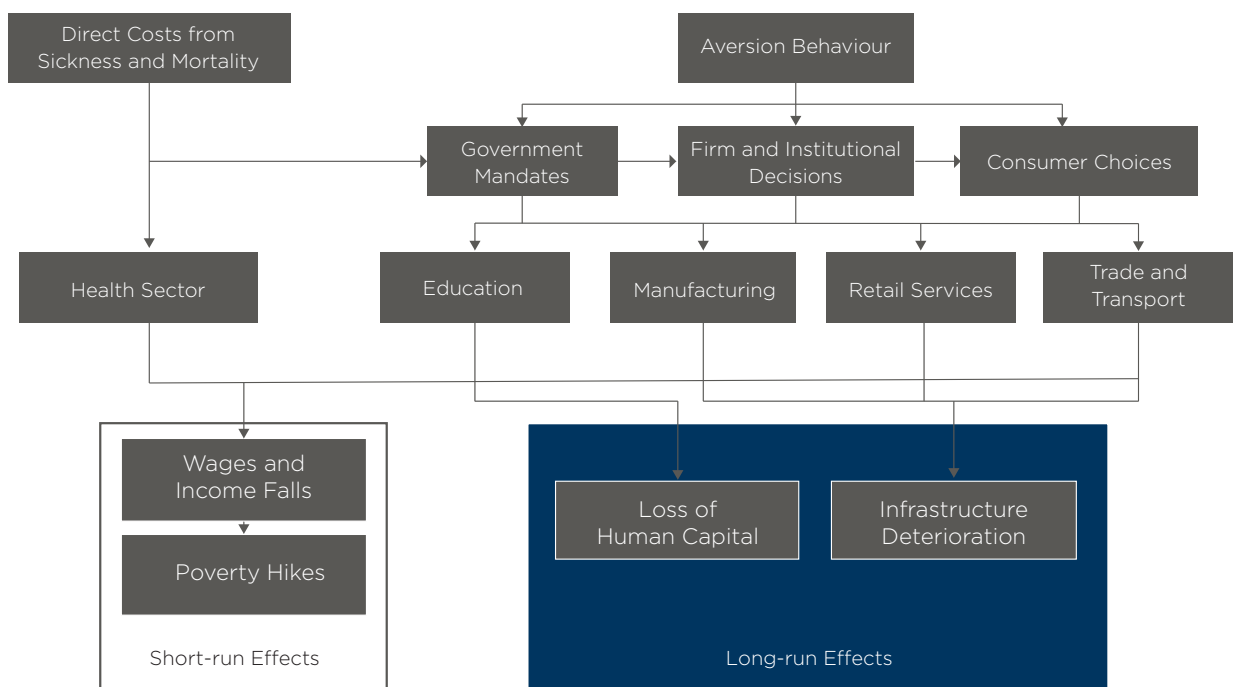
Health systems in Africa are also already stretched in dealing with ongoing disease burdens such as malaria and Ebola. Effects of the Ebola outbreak in 2014-16 in West Africa resulted in fewer resources dedicated to endemic conditions, as well as fewer people seeking treatment for maternal health, hypertension and diabetes (Wang, 2020). Health authorities fear the same trend with regional COVID-19 outbreaks.

Global Economic Fallout from COVID-19

Initially, global leaders imagined a sharp but short hit to the world economy, presuming the Wuhan-originating outbreak would largely be a localized problem for China with some knock-on effects. Now, towards the end of March 2020, a V-shaped recession in the first half, of the year, followed by a recovery in the next half looks unlikely (Elliot, 2020).

The Organisation for Economic Co-operation and Development (OECD) has warned that the virus poses the biggest danger to the world economy since the 2008 financial crisis. Measures to contain the virus, including national lockdowns, social distancing, factory closures and travel restrictions, have crippled supply chains, reduced output, hit commodities and sent confidence on a downward spiral. COVID-19 is a health emergency that is fast becoming an economic crisis, with both a supply and demand side shock.

Channels of Potential Economic Impact of COVID-19



Source: Evans and Over 2020, adapted from World Bank, 2014

There are both long and short-term effects to the pandemic as the diagram on page 7 shows.

'Aversion behaviour' is understood to be all the actions taken to avoid infection, be they on a global, national or personal scale. It is the most likely category of actions that will lead to longer term economic consequence, stemming from state restrictions on social and business activities, leading to business and school closures, resulting in lost payment for workers, which eventually translates into less spending

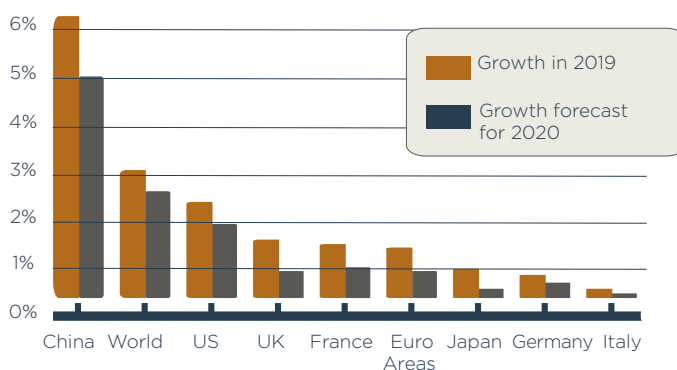
and social activity (Evans and Over, 2020). Economists and analysts calculate that the long-run effects will lead to reduced global growth.

In the figure below, the OECD has downgraded growth forecasts to hover around 1.5% – 2% which is half the projected rate before the COVID-19 pandemic (OECD, 2020). This low growth would erase USD 1 trillion off the value of the world economy (Hutt, 2020).

Volatile world markets have compounded aversion behaviours since the COVID-19 outbreak in Wuhan, China in December 2019. It has caused oil and stock prices to tumble with several historic levels recorded in March 2020.

OECD downgrades growth forecasts

Economic growth (GDP expected to slow down in 2020)



Source: OECD, 2020

Oil

China is the world's biggest oil importer. With much of the country still in lockdown and several other countries now enforcing lockdown and states of emergency to contain COVID-19, the International Energy Agency (IEA) has predicted the first drop in global oil demand in a decade (Hutt, 2020).

The IEA's monthly report for March 2020 puts the year-on-year slump at 90kb/d. The current price of oil, USD 22.43 a barrel, as at 23 March 2020, is close to the record lows during the Asian financial crisis in 1998/9 (World Oil, 2020). Analysts have predicted that the price war between Russia and Saudi Arabia has been catastrophic for OPEC, the world's most successful cartel.

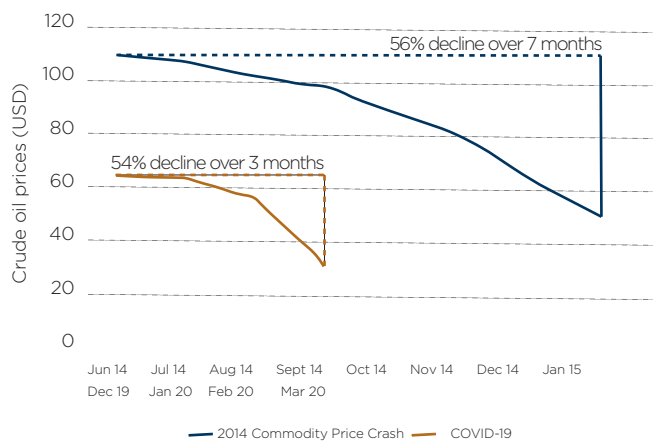
In March 2020, the Saudis abandoned their 2017 output agreement, flooding the market with cheap crude oil. The move was in response to Russia's refusal to effect deeper production cuts to help prop up prices in the face of declining demand due to COVID-19 (Fortune, 2020).

Oil price volatility has deep impacts for African oil-producing and exporting countries such as Libya, Algeria, Nigeria, Angola and Ghana. The oil price drop in 2014 impacted significantly on the continent, which saw a decline in GDP growth for the Sub-Saharan region from 5.1% in 2014 to 1.4% in 2016 (Brookings, 2020). Compared to 2014, the oil price fallout during the COVID-19 pandemic has plummeted over a shorter time, declining 54% in just three months.

African oil-producing countries rely heavily on oil earnings to fund national budgets. They have pegged national earnings on a much higher oil price of around USD 60 per barrel (Bloomberg, 2020). Ghana's hopes of earning at least USD 1.5 billion off new oil discoveries this year have been dashed, not to mention Nigeria's and Angola's projections, the continent's first and second biggest producers and exporters respectively. China is Angola's largest oil importer and with demand low, Angola's economic resilience to weather a global economic recession is

poor; this at a time when it is experiencing its fourth year of recession (SET, 2020).

Fragile and volatile markets look to be the order of the day, with key indices decidedly down on 23 March 2020. Uncertainty around when the pandemic disruptions would cease has prompted investors to sell even good stocks with fundamental value (Bloomberg, 2020). The big winners are those who anticipated the crash and bid short.



Drop in crude oil prices in 2014 vs COVID-19

Source: IMF Primary Commodity Price System

The Africa-China Connection

Since 2009, China has overtaken the US as Africa's biggest trading partner. Now, during this time of virus-induced panic, analysts are looking to China first for indicators of knock-on economic impact. China's cities are still in lockdown, its production sectors have slowed dramatically, travel internally and to the rest of the world has all but ground to a halt, and commodity prices have plunged.

A decelerating super-power means that low- and middle-income countries dependent on trade and tourism with China will feel the sting of the virus, even if COVID-19 infections in those countries do not spike on the global graph.

Beijing's Belt and Road Initiative has funded a range of infrastructure projects across the Eurasian continent and beyond, from roads and railways to power plants.

Construction on the 2 000km crude-oil pipeline and the almost-complete Lagos-Ibadan railway has ground to a halt, the Chinese workforce not having been on site since just before the Chinese Lunar New Year in February 2020 (Kitimo, 2020).

AFRICA-CHINA TRADE AND COMMODITIES

Besides oil, Africa's other commodities are also closely linked to China's fortunes. Depreciations in industrial commodities are hitting resource-dependent economies hard. The Congo's commodity exports amount to 70% of GDP with exports to China accounting for 50% of total GDP (Smith, 2020).

Copper prices are down by 7% which in turn will lower the value of exports from major suppliers - Zambia, the Republic of Congo and the Democratic Republic of Congo (SET, 2020). Africa's copperbelt region produces 70% of the world's cobalt and supplies a large percentage

of global demand for lithium and other rare minerals. China is the biggest importer of cobalt and rare minerals, being the world leader in the production of mobile phones, electric car batteries and hi-tech components (Smith, 2019). China also has significant investments in mines in the copperbelt region, exercising its control over value chains in the mining sector. With the overall downturn in China, investments in these ventures have also slowed.

Chrome, manganese and iron ore make up two thirds of South Africa's total exports to China. Less demand for these metals has caused listed shares of mining companies to tumble (Times Live, 2020).

Soft commodities such as coffee, tea, rose flowers and cocoa are also suffering due to subdued Chinese demand. The slowdown affects Rwanda, Ghana, Ethiopia, Kenya and the Ivory Coast (Okoth, 2020). South Africa's fisheries industry took a knock after China stopped all animal imports in January; 95% of the country's rock lobster harvest is usually sold to China.

According to researchers at SET, the estimated lost revenue of Sub-Saharan exports to China could reach around USD 420 million. Angola, Congo, Sierra Leone, Lesotho and Zambia have been named as the most economically exposed through exports and tourism (SET, 2020).

SUPPLY CHAINS

China's record of favourable pricing and efficient logistics has made it a critical player in global demand and supply chains. Many African states have become dependent on Chinese imports such as textiles, electronics and household goods.

Kenya's port of Mombasa has become a regional transport and supply chain hub, receiving goods bound for Uganda, Rwanda, Burundi, Democratic Republic of Congo and South Sudan (Okoth, 2020). Since February 2020, Mombasa has recorded its lowest arrivals of cargo ships to date, with

37 cancellations and a further 104 scheduled dockings still uncertain – most of them from China.

This has sent ripple effects across borders and down the supply chain, impacting the rail freight service that operates from the port (Kitimo, 2020).

Thousands of small to medium-sized enterprises on the continent have been forced to shut down after disruptions to supply chains and an inability to store large stocks.

China is Kenya's biggest source market, accounting for up to 40% of all imports. The Kenya Importers and Small Traders' Association says it has lost USD 300 million since the COVID-19 outbreak (Kitimo, 2020). A fourth of all Ugandan imports come from China, as well as 60% of all South Africa's clothing and textiles (Evans and Over, 2020).

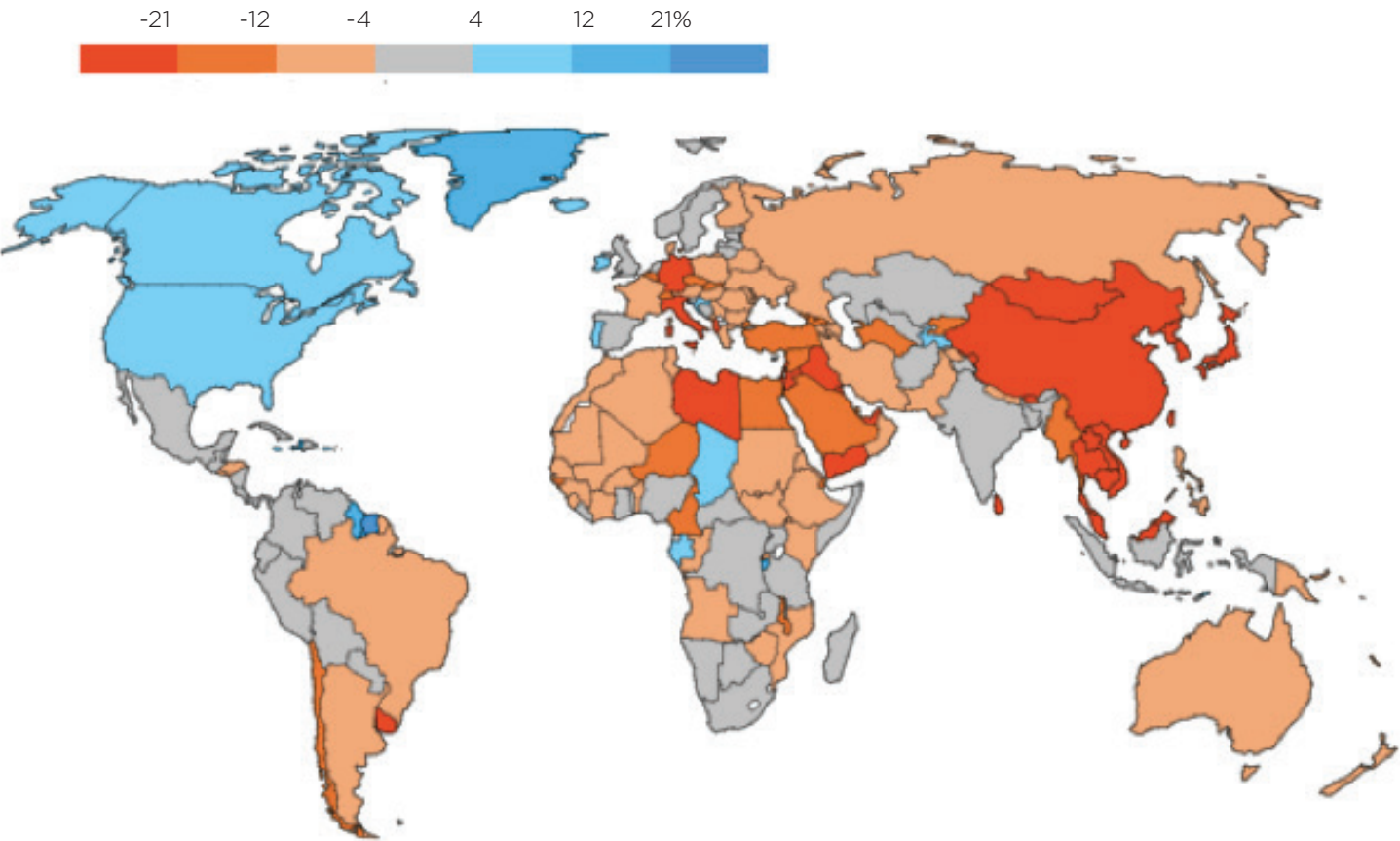
Several state-owned Chinese industries are returning to work after COVID-19 cases drastically reduced, but it is privately-owned industries and smaller companies that are really China's economic engine. They produce toys, textiles and consumer goods and have not regained momentum, with workers still idle due to lack of materials and enduring quarantine measures (Evans and Over, 2020).

TRAVEL

The airline industry has been a major COVID-19 casualty, decimating business across the globe due to containment measures. At the start of the outbreak much of the loss was attributed to the diminished Chinese tourist market, but the global spread of the virus, with Europe now the epicentre, has collapsed all demand in the sector.

COVID-19 has erased up to 15% of global airline capacity, prompting all carriers to take drastic measures just to stay afloat (Bloomberg, 2020).

The graph on page 13 indicates airline capacity, illustrating just how much travel has been curtailed in certain regions, mirroring the aviation regulations countries have put in place to stop COVID-19 infection rates.



No-fly Zone

The COVID-19 outbreak has reduced global airline capacity by 15% since the pandemic began.

The following is a list of the draconian measures global airlines are taking:

- Deutsche Lufthansa AG, Europe's biggest carrier, will ground 700 planes and cancel 95% of seats.
- State-owned Dubai airline, Emirates, will ground most of its passenger fleet, reducing destinations from 145 to 13, and cut wages to half.
- British Airways is set to cut back 75% of operations over the next two months.
- Australia's carrier, Qantas Airways, will stop all international operations in March, slash domestic operations by 60% and temporarily lay off up to 30 000 staff.
- Delta Airlines in the US is reducing its operations by 70%.
- Abu Dhabi-based Etihad is grounding its Airbus A380 fleet along with an entire premier class of service called 'The Residence'.
- Virgin Atlantic is to reduce 80% of its flights and has requested staff take eight weeks of unpaid leave.
- Irish carrier Ryanair has cut capacity by 80% and is considering grounding its entire fleet.

(Bloomberg, 2020)

On the African continent, airlines have taken similar measures to avoid bankruptcy. The sector has already lost USD 4.4 billion in revenue since the start of the pandemic. According to data from the International

Air Transport Association (IATA), there has been a 20% decline in international bookings and a 15% drop in domestic travel in Africa for March and April 2020 is projected.

South African Airways (SAA) has cancelled all international flights until the end of May 2020 in response to the Government declaring a state of disaster in South Africa as COVID-19 cases surpassed 400. A further 124 regional flights were also grounded (Omarjee, 2020). The beleaguered South African state-owned airline was placed under business rescue in December 2019 to avoid bankruptcy after years of mismanagement and corruption that accumulated a USD 1.6 billion loss. Kenya Airways was also facing a battle for survival before the COVID-19 impact, after years of escalating debt (Kuo, 2020).

Royal Air Maroc, Air Tanzania, Air Mauritius, EgyptAir, RwandAir, SAA and Kenya Airways have all suspended flights to and from China. On the other hand, for Africa's most profitable carrier, Ethiopian Airlines, it is business as usual for its China routes. The airline countered calls to suspend its 35 weekly flights to China, arguing that the measure would not slow the spread of COVID-19 (Logupdate Africa, 2020).

Hand in hand with a collapse of travel go tourism, hospitality and entertainment. Cancelled national celebrations, sporting events, cultural and religious practices, art, music and literary festivals and conferencing are decimating these industries, which face large-scale job losses.

Economic Vulnerability Indicators

It is clear that curtailed investment, trade and freedom of movement will result in a global slowdown and will render economies vulnerable. But vulnerabilities are also dictated by other internal or national factors. Should the pandemic reach high infection rates in African countries and should there be a high degree of community transmission (viral infections from and between local persons), local productivity and local value chains across sectors will be further impacted. The health of national coffers, the level of debt and the state of currency reserves are all internal factors that add to this economic vulnerability.

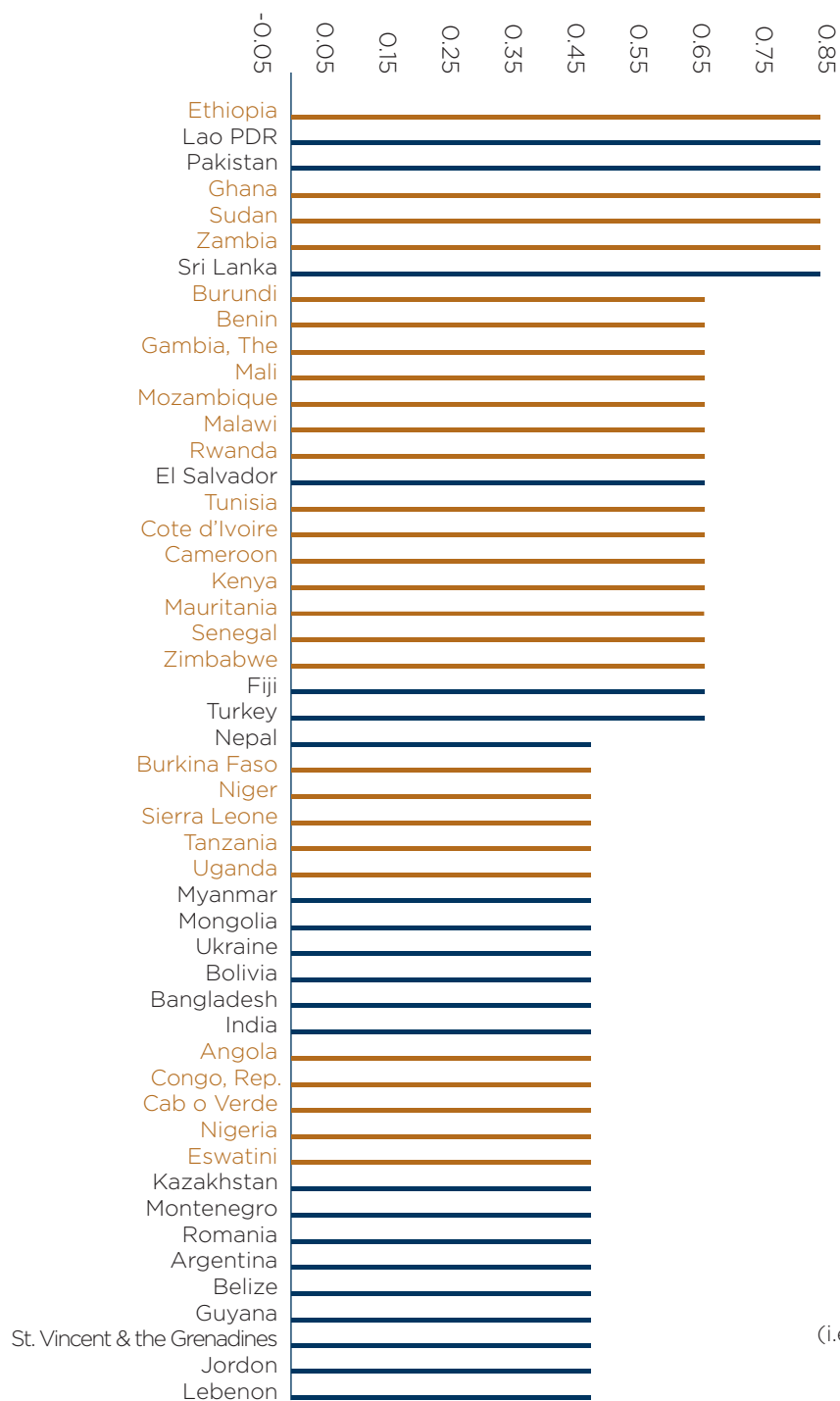
From this understanding, SET (2020) has compiled an index with several measurable indicators that helps to evaluate a country's status. Among the 10 most significant indicators are:

- Confirmed COVID-19 cases
- Reduction and cancellation of flights by key airlines
- Travel restrictions
- Total trade with China as percentage of GDP (both exports to and imports from China)
- Inbound Chinese tourism

- Foreign direct investment (as net inflows in % of GDP, as well as China's outward FDI)
- External debt in % of GDP
- Current health expenditure as % of GDP
- Healthcare access and quality
- Migrants as % of population

Many of these indicators are drawn from slow-changing variables and can be fairly reliable over the course of time. Confirmed infection rates and changes in travel restrictions are perhaps two of the more volatile indicators and subject to more drastic changes. These could significantly affect the weighting of indicators and the placement of countries on the graph on page 17.

Drawing from the SET methodology, Ethiopia, Ghana, Sudan, Zambia and Burundi are the five African countries least resilient to the economic impacts of COVID-19. These countries top the list because they have less fiscal capacity to buffer the impacts, along with poor-quality health systems and poor access to them (SET, 2020). Out of the 50 least resilient countries listed on the graph, half are in Africa.



Countries that are least resilient
 (i.e. may confront challenges to doing
 something about the impacts)

Remedies

Creative combinations of monetary and fiscal policy measures will need to make up a multi-faceted response to the economic impacts of COVID-19.

Central banks across the world and in Africa have taken unprecedented measures to reduce interest rates in a bid to arrest a downward economic spiral. But many analysts agree that rate cuts are just a plaster on a gaping wound. Several Sub-Saharan African states are in a technical recession. Three of the region's bigger economies, Angola, South Africa and Nigeria, are particularly vulnerable. Combined with COVID-19 impacts, slumping markets and rising unemployment, rate cuts are considered merely reassuring measures that could cushion the blow.

What has been called for is a targeted response, with measures to help businesses deal with the short-term crisis and cash flow. Targeted relief is being extended in hard-hit countries such as Italy, Denmark, China and the US. Several African countries have also extended economic support packages, especially for small and medium enterprises that are being affected. South Africa has announced that a Temporary Employment Relief Scheme will be made available for companies in COVID-19 distress. This scheme is meant to pay salaries directly to employees to avoid retrenchments while reserves in the Unemployment Insurance Fund are also on standby to supplement loss of income for companies unable to foot their wage bill (Chothia, 2020).

Several tax regulations have also been relaxed for compliant SMMEs across several African countries. Mauritius, Kenya and South Africa will expediate value-added tax refunds in the next few months, as well as delay categories of tax payments to their respective revenue services without penalties. Banks across these countries have been instructed to suspend and extend loan repayments for affected businesses with existing facilities, as well as allow for higher borrowing limits (Chothia, 2020, Reuters, 2020, Central Banking, 2020).

Stimulus packages have the potential to boost the economy and provide funding to cover the rising costs of the pandemic which include boosting health expenditure.

For many African countries, stimulus packages are not affordable but that does not mean fiscal responses are entirely off the cards. Economists suggest redirecting funding from existing budget line items rather than increased borrowing (Krugel and Viljoen, 2020). This measure would support additional health resources and other containment measures. This is one of the routes several African nations are taking, but the more economically vulnerable countries such as Kenya predict they will not be able to cope. Kenya is now seeking emergency assistance of USD 350 million from the IMF, much of it to be directed towards the national budget. Kenya has already approached the World Bank for USD 60 million to support its health sector to better respond to COVID-19 (Reuters, 2020).

Deep cooperation between global leaders and the financial services industry is a prerequisite to stem the human and economic cost of COVID-19. What is significant is the sense of agency that governments and powerful global institutions have been forced to exercise. Relaxing regulations and punitive conditions around tax, banking and debt has allowed governments greater freedom in making economic decisions in the interests of their citizens. Neo-liberal orthodoxies have traditionally limited government interventions and prioritised market interests. The COVID-19 outbreak has catalysed a crisis that is reshaping this condition to more fully embrace labour, competition regulations and the price of essential goods and services.

United Nations chief Antonio Guterres has warned that a global recession is likely. 'This is a moment that demands coordinated, decisive and innovative policy action from the world's leading economies. We are in an unprecedented situation and the normal rules no longer apply.'

In the case of COVID-19, no country is safe until every country is safe - a fact of our deeply interconnected and interdependent realities. This pandemic is going to require the reset of rules thought previously immutable, especially economic ones that have over a long period sustained or maintained deep structural inequality.



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