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Commodity prices crash hits Africa

By Kingsley Ighobor

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Just three years ago, most of the world's fastest-growing economies were in Africa, among them Angola, Chad, Ethiopia, Mozambique, Nigeria, Rwanda and Sierra Leone. A middle class was emerging, led by young, tech-savvy entrepreneurs who bought flashy cars, new houses and the latest smartphones.

Image by 123RF

Africa’s impressive average economic growth of around 5%, over the 14 years to 2014, saw economists toasting to the continent’s development potential. Buoyed primarily by high commodity prices and marginal exposure to global financial markets, the African economy as a whole was largely undisturbed by the 2009 global financial crisis. And steady flows of foreign direct investment assured a sustainable growth trajectory.

During that period, China, India, Brazil and European countries scrambled for a slice of Africa’s investment opportunities. The Brookings Institution, a Washington D.C.–based think tank, stated in 2013 that it was a mistake not to “take into account the current realities of the emerging continent” and “leverage the potential that Africa presents as a market for American goods.” Even *The Economist*, a usually restrained UK publication, splashed an “Africa Rising” title on its 11 December 2011 cover, which depicted a silhouette of a child flying a kite of an African map.

Fortune reversal

A precipitous crash in commodity prices is changing that upbeat African narrative. Already, Angola, Liberia, Mozambique, Nigeria, Sierra Leone, and Uganda — the African countries that depend most heavily on commodities — such as oil, gold, diamonds, bauxite, rutile, timber and copper — are in dire straits.

Economists also attribute this sudden reversal of fortune to other factors such as volatile global financial markets, weaknesses in global growth, particularly in China, Brazil and India, rising borrowing costs and severe infrastructure constraints (particularly of electricity supply) in many countries. But it is the plunge in commodity prices that has dealt the most devastating blow.

The price of oil plummeted from $100 a barrel in 2013 to $26 a barrel in February 2016, hovering around $50 a barrel in October. Without sufficient oil earnings, Africa's oil producers, particularly Nigeria, Angola, Equatorial Guinea, Libya, Algeria and Egypt, face serious economic head winds.

For Nigeria and Angola, Africa's largest producers, oil proceeds account for more than 90% of exports and over 70% of the national budget. With low per-barrel prices, economic growth in all of Africa's oil-exporting countries fell from an average of 5.4% in 2014 to an average of 2.9% in 2016. Consider that Angola generated $60.2 billion from oil in 2014 and $33.4 billion in 2015, a significant drop in revenue that mirrors the situation in other countries.

Significant shock

Copper-producing countries have not fared any better as prices dropped to their lowest level since 1998. The World Bank reports that in February 2016, "copper prices declined by almost a third from their peak in February 2011 to $4,595 per tonne."

Tsidi Tsikata, who led an International Monetary Fund (IMF) assessment mission to Zambia in March this year, has issued a bleak report: "The Zambian economy is under intense pressure," he warns, calling for action to regain macroeconomic stability.

More than half of Zambia's copper producers are losing money, and big players in the country such as Glencore, an Anglo-Swiss multinational and Luanshya Copper Mines, a Chinese firm, have shut shops, with thousands losing their jobs. The Zambian economy is currently growing at 3%, down from 7% in 2014. Although some analysts see a rebound in the Chinese economy, in recent years China, which buys up to 40% of copper worldwide, has not been able to afford huge purchases due to economic slowdown.

Sierra Leone is grappling with falling prices of iron ore, even as it recovers from the Ebola epidemic. African Minerals, a London-registered mines company, used to manage the iron ore mines in Tonkolili, northern Sierra Leone, which are worth over $1 billion. Tonkolili has the biggest iron ore deposit in Africa and the third largest in the world.

In 2011 iron ore sold for $191 per tonne, but it fell to $45 per tonne in June 2016. Faced with corruption allegations and huge financial losses, Africa Minerals sold the mines in December 2015 to China's state-owned Shandong Iron and Steel Group. Mining is expected to resume by the end of 2016.

Iron ore is Sierra Leone's economic lifeline. "The iron ore price decline affected macro-financial stability and reversed the country's remarkable positive growth trajectory," maintains the African Development Bank.

"The fall in commodity prices represents a significant shock for the sub-Saharan African region, as fuels, ore and metals account for more than 60% of the region's exports," notes the World Bank.

Ordinary citizens feel the impact in currency depreciation and rising inflation. The value of Nigeria's naira fell from 150 to 450 naira to the dollar between January 2014 and October 2016. The Sierra Leonean currency faced the same fate, declining to 6,500 leones to the dollar, from 5,000 leones a year ago.

Nigeria’s currency depreciation means it has lost the right to call itself Africa’s largest economy. After rebasing (a process of adopting new prices to measure a country’s GDP output) in 2014, the Nigerian economy was reported to be worth $488 billion. With the naira’s depreciation due to a decline in export earnings, the economy has shrunk to $296 billion, according to data released in August by the IMF.

Skyrocketing prices of goods and services without a commensurate increase in earnings could affect prices of food and stoke social unrest across Africa, experts fear.

Austerity measures

Commodity-dependent countries are faced with huge budget deficits, which is why Angola, Ghana and Zambia have received or are intensely negotiating for IMF bailout loans.

Nigeria is overhauling its tax system to increase revenues, aggressively fighting corruption and recovering stolen money stashed in foreign banks, and at the same time intends to borrow money from China and local banks. The country wants to sell off some of its national assets, including energy and oil corporations.

Africa’s most populous nation will “seek a dramatic shift from spending on recurrent expenditures to spending on capital aspects of the budget,” said Udoma Udo Udoma, minister of budget and national planning. It officially declared a recession in August after two quarters of negative growth.

Last March, Sierra Leone announced a 30% cut in recurrent government expenditures, suspended financing for capital projects and the purchase of official furniture, eliminated travel allowances for government officials and began implementing a 50% cut in vehicle maintenance allowance, among other measures.

However, Herbert M’cleod, a leading Sierra Leonean economist, says, “It is bad policies and bad management that have brought us here,” and recommends using proceeds from mining to boost jobs creation and power supply and to construct roads, among other things.

The Ugandan government has scrapped gasoline and diesel subsidies, suspended construction of new roads, banned nonessential foreign travels and stopped the launch of a new airline. Zambia is cutting subsidies on electricity and agricultural inputs.

South Africa, whose largest exports are iron ore, coal, gold and other minerals, is also affected by the fall in commodity prices. While presenting the 2016 budget, finance minister Pravin Gordham said, “There is no doubt that we are in crisis,” before announcing an unprecedented spending cut of 25 billion rand (about $1.7 billion). Liberia, Gambia and other countries are also implementing various austerity measures.

The 2015 study, *The Effect of Commodity Prices on African Economic Growth* by Hangnile Nathalie Olga Tiawara, of St. Cloud State University, United States, found that commodity price changes are linked to the pace of economic growth in commodity-dependent countries. In short, when prices fall, these economies falter.

Good news for some countries

The Economic Commission for Africa (ECA) has over the years been encouraging countries to industrialize by diversifying away from commodities and, at the least, to add value to their commodities. Former ECA executive secretary Carlos Lopes repeatedly spoke about the paradox of countries’ importing Toblerone chocolates from Switzerland when the continent produces 70% of the world’s cocoa, from which chocolates are made.

As oil-exporting countries deal with economic anxieties, low oil prices are good news for oil importers like Kenya, Rwanda and Tanzania. It means these countries spend less and can redirect excess funds into critically needed infrastructure such as roads, bridges and energy. Robust growth in these economies will continue, forecasts the World Bank.

Going forward, mitigating efforts will require good financial management and increases in revenue generation locally, experts say. “As countries adjust to a more challenging global environment, stronger efforts to increase domestic resource mobilization will be needed,” says Makhtar Diop, World Bank vice-president for Africa.

There may yet be a silver lining: experts expect the impact of current belt-tightening policies in Africa to kick in in the medium to long term, providing a cushion for national budgets.

Also, countries will learn the lessons of commodity price movements and will be more inclined to continue diversifying their economies. The World Bank says that agriculture and urbanization are important sectors for investments.

Finally, when earnings are in an upswing, countries must save for the rainy day, experts recommend.

Source: Africa Renewal.