THE IMPACT OF GLOBAL FINANCIAL CRISIS AND ECONOMIC DOWNTURN ON SMALL AFRICAN STATES

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INTRODUCTION

Over the past 10-15 years, the world economy has enjoyed unprecedented stability and growth;

• High FDI flows and High savings and investments
• High growth rates and Export sector growth
• Achievements of MDGs
• Achievements of Macroeconomic stability
• Effective monetary policy by central banks

Today, 2008/09, the global economic crisis or recession is the worse in 80 years since 1930.

About 40% of small states highly dependent on export sector yet the World demand for export is declining. What will be effect on foreign exchange flows?
Nature of the Problem

Questions that are frequently asked since the beginning of the crisis include the following:

How are the developing countries such as Lesotho, coping with the current global economic crisis?

How will the crisis affect capital flows into developing countries’
- portfolio capital flows
- direct foreign investment flows (FDI)
- remittance flows
- foreign aid flows

Effects on Infrastructure Development
Challenges facing small states include
• The thread of a growing poverty likely to reverse MDGs
• Lack of institutional capacity and policy framework to mitigate impact
• Lack of safety net, unemployment benefits,
• Increasing fiscal pressures
The Purpose of the Presentation

• To examine how the five SACU/SADC small states have been affected by financial crisis

• SACU small states include Lesotho, Botswana, Namibia and Swaziland (SADC include Zambia, Malawi, Seychelles)

• The presentation focus on direct and indirect effects of global financial crisis on small states of SACU and SADC

• The impact of world economic downturn on foreign exchange income of small states in SACU and SADC

• The Impact on migrant remittances

• The impact on foreign aid flows
• The small states in SACU and SADC have developed a highly integrated financial system due to a long history of regional integration with South African economy

• The financial sector seem to have not been severely affected by global financial crisis due to exchange controls, strong regulatory and supervisory systems

• The insurance sector operates off sure investments and therefore have been affected
Spread of Financial Crisis on SACU Small States

- SACU small states have a dual currency system with RSA which permits capital flows within the region.

- Large number of commercial banks owned by RSA parent companies:
  1. Botswana and Namibia have a diversified banks ownership including some from U.K.
  2. Lesotho and Swaziland have 100% banks from RSA parent companies.
  3. All SACU countries have stock exchange except Lesotho.
  4. All SACU banks practice dual banking supervision and harmonized regulatory systems.

- All SACU member states have similar monetary policy.
- RSA experienced no exposure or spread of financial crisis.
- SACU member states have experienced no liquidity shortages but there is a problem of loss of confidence, hence credit crunch.
- Sources of banks incomes is placement with parent companies in RSA.
The impact of credit crunch in Lesotho

- Global credit crunch affected textile sector, mining sector and money markets (off-shore investments)

- Lack of Trade Finance in Lesotho, Cash-flow problem
  - pre-shipment requirements for procurement of fabric material

- post-shipment – manufacturing period - credit required/working capital
- export credit – inward LCS, imports - DCC – credit certificates
- Government of Lesotho taking equity M30 million - importance of bail-out program

- Establish trade finance facility to the value of $60m to support credit guarantee scheme

- Restructure the textile industry – diversify products, internal production of raw material diversify the market - U.S. – AGOA, European, SADC, Other region
5. IMPACT OF RECESSION
Declining incomes, repossession of vehicles and houses
Factory closure, e.g. copper mines, diamond mines, except gold and platinum prices, export industry collapse, oil prices fall
Tourist industry collapse
Motor industry
Case of Lesotho
diamond mines – Liqhobong and Kao
SADC revenue falling
5.1 Fiscal implication

- Government expenditure rise
- Government revenue declines – tax revenue falls
- Foreign aid falls – donor community fail to deliver on commitment
- Foreign exchange inflows falls

**Budget Deficit**

6. GOVERNMENT RESPONSE – G20, IMF/World Bank, National Government
- Stimulus packages
- Government bail-out important firms, motor industry through subsidies, agricultural subsidies
- Stimulate consumption expenditure
- tax rebates
1.1 Reserves Currency Composition (%)

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<th>Months</th>
<th>USD</th>
<th>GBP</th>
<th>EURO</th>
<th>CHF</th>
<th>ZAR</th>
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From the graph, it is observed that the percentage composition of reserves has remained relatively stable over the months from March 2006 to September 2008, with USD, GBP, and Euro holding a significant portion of the reserves.
1.2 Reserves Allocation By Institution

- **Sovereign**
- **Private**

**Months**
- Q1-06
- Q2-06
- Q3-06
- Q4-06
- Q1-07
- Q2-07
- Q3-07
- Q4-07
- Q1-08
- Q2-08
- Q3-08
- Oct-08

0.00% - 100.00%
3.1 EURO PORTFOLIO ALLOCATION BY INSTITUTION

- Sovereign
- Private

TIME

- Q1-06
- Q2-06
- Q3-06
- Q4-06
- Q1-07
- Q2-07
- Q3-07
- Q4-07
- Q1-08
- Q2-08
- Q3-08
- Oct-08

Oct-08
4.1 RAND PORTFOLIO ALLOCATION

TIME

Sovereign
Private