STUDY ON MANAGING SOVEREIGN DEBT IN TIMES OF CRISIS:

Insights from the Covid-19 pandemic and lessons for the future

CHAPTER 1

Economic Impact of COVID-19, Policy Responses and Implications on Debt Dynamics

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FOREWORD

The dark clouds of the COVID-19 pandemic that suddenly descended upon the global economy spared nobody and triggered one of the most devastating global health and economic crises in modern history. The pandemic placed severe strain on the public finances of all types of economies. For developing countries in particular, debt levels that were already high before the pandemic increased further, exacerbating existing debt vulnerabilities at a time when pressure to spend on health and social services became unavoidable.

The IMF noted that the impact of COVID-19 was historic and unusual in its severity as the debt stress it induced exceeded past experiences across a number of dimensions, including the dramatic increase in government borrowing needs, sharp downturn in economic activity, strain in market conditions, and disruption in operations (IMF, 2020).

The pandemic also resulted in the materialisation of a number of operational risks as governments were required to adjust. One of the main challenges of the pandemic to the environment was how to meet increased government borrowing requirements against a backdrop of volatile market conditions, both locally and globally. In addition, the adoption of remote working arrangements changed the overall control environment in which staff performed their roles, thus exacerbating the vulnerability of the Debt Management Offices to operational risks.

As part of efforts to harness a range of lessons and insights emerging from the pandemic, MEFMI, with the support of FSD Africa, commissioned a study to document debt and related policies and practices that countries adopted to manage public debt and support debt markets during the crisis. The study covered four themes: (a) macroeconomic policy interventions, (b) external financing operations, (c) local currency bond markets and (d) governance and operational risk management frameworks for public debt.

In December 2022, MEFMI and FSD Africa organised a seminar to validate the findings and recommendations from the study. The content of the study has now been finalised and has been released as separate chapters, while a study summary has also been produced.

This is Chapter One of the study. It focuses on macroeconomic policy interventions while the pandemic was unfolding, along with the main lessons learnt.

We hope that the findings and lessons from this study will be useful in informing policy makers and debt practitioners of pertinent actions needed in both normal times and in times of crisis.

Readers can access the Study Summary and the other chapters here.

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ACRONYMS

AfDB	African Development Bank
AU	African Union
BOB	Bank of Botswana
BON	Bank of Namibia
BOT	Bank of Tanzania
BOU	Bank of Uganda
BOZ	Bank of Zambia
CBE	Central Bank of Eswatini
CBL	Central Bank of Lesotho
CBK	Central Bank of Kenya
CCRT	Catastrophe Containment Relief Trust
COMESA	Common Market for Eastern and Southern Africa
COVAX	COVID-19 Vaccines Global Access
CIs	Credit institutions
DMO	Debt management office
DSA	Debt sustainability analysis
DSSI	Debt Service Suspension Initiative
EAC	East African Community
EU	European Union
FDI	Foreign direct investment
FSD	Financial Sector Deepening
G20	Group of twenty
GDP	Gross domestic product
GVC	Global value chain
IMF	International Monetary Fund
LCBMs	Local currency bond markets
MDIs	Microfinance deposit-taking institutions
MEFMI	Macroeconomic & Financial Management Institute of Eastern and Southern Africa
MNE	Multinational enterprises
MSMEs	Micro, small and medium enterprises
NBA	National Bank of Angola
NBR	National Bank of Rwanda
OECD	Organization for Economic Cooperation Development
PPE	Personal protective equipment
RBM	Reserve Bank of Malawi
RBZ	Reserve Bank of Zimbabwe
SADC	Southern African Development Community
SOEs	State-owned enterprises
SSA	Sub-Saharan Africa
UNCTAD	United Nations Conference on Trade and Development
VAT	Value-added tax
WB	World Bank
WEO	World Economic Outlook
WHO	World Health Organization

1.
INTRODUCTION

The COVID-19 pandemic resulted in an unprecedented health and economic crisis across the world. Although sub-Saharan Africa has suffered a smaller death toll compared to the rest of the world, the pandemic has led to a sharp economic downturn in the region. As the pandemic spread, MEFMI member states joined the rest of the world in implementing measures to curb the spread of the virus. Such measures included national lockdowns, overnight curfews, border and port closures, social distancing, and greater rigour in hygiene, such as washing of hands and hand sanitisation.

While such measures have saved lives, they have at the same time severely affected economic activity and negatively impacted the livelihoods of millions of people, leading to declines in aggregate demand and output. The services sectors, which include tourism, transport, education, entertainment, sports and restaurants, were the most affected. The economic effects of the pandemic were exacerbated by the presence of a large informal sector, which is prevalent in most MEFMI member states. Besides domestic factors, the region was also affected by a deteriorating external environment, characterised by weak global demand and supply chain disruptions. This affected tourism, exports receipts, foreign direct investment (FDI) inflows and international reserve positions, and led to a shortage of key imports. As a result, COVID-19 led to a decline in GDP growth rates. This in turn affected local revenue collections, in the face of the increased expenditure required in order to save lives and livelihoods.

As elsewhere in the world, MEFMI countries had no choice but to respond to the crisis. The effect of the pandemic on member countries varies from country to country in view of the diversity of the group. MEFMI countries span three income groups. Four countries are classified as low income: Malawi, Mozambique, Rwanda and Uganda; seven as lower-middle income: Angola, Eswatini, Kenya, Lesotho, Tanzania, Zambia and Zimbabwe; and two as upper-middle income: Botswana and Namibia. The structures of the various economies in the group also differ. MEFMI includes mineral-rich and oil-exporting countries such as Zambia, Botswana and Angola, while other countries rely on the export of agricultural produce, manufactured goods and tourism. However, all countries have been negatively affected by the pandemic, to differing extents and through different channels.

Irrespective of the named grouping, MEFMI countries undertook a wide range of fiscal and monetary policies to ameliorate the impact of the pandemic. These policy actions were tailored to member countries' economic characteristics and societal needs, and the mandates of responding institutions. The fiscal policy responses aimed to provide lifelines to households and businesses, restore workers' incomes and preserve jobs. Monetary policy responses, on the other hand, mainly sought to guarantee appropriate market liquidity conditions to support credit markets.

Despite experiencing heightened debt levels before COVID-19, many countries had little choice but to incur additional debt to finance their fiscal responses to the pandemic. This has increased debt vulnerabilities across the region and exacerbated debt sustainability concerns in most countries. Lower GDP growth, higher fiscal deficits, higher borrowing costs, depreciating currencies and deteriorating external positions have combined to create unfavourable debt dynamics in the region.

While international and regional financial institutions, such as the World Bank (WB), International Monetary Fund (IMF) and African Development Bank (AfDB), as well as the countries of the European Union (EU) (both bilaterally and multilaterally), have responded through additional financing, debt relief measures and restructurings, more effort is required to ensure that debt sustainability remains in check in the region.

1.1 Objective

The objectives of this chapter are to:

i. highlight the impact of the COVID-19 pandemic on key macroeconomic variables and the associated public debt dynamics;
ii. map macroeconomic (monetary and fiscal) measures in response to COVID-19 and their impact on domestic debt markets and public debt

[1] See Section 2 in Chapter Two of the study, which reviews in detail the varying nature of support made available by different agencies.

dynamics; and

iii. draw lessons from such policy interventions and practices, including insights into key policy considerations when responding to similar crises in future.

1.2 Methodology

The whole study combines a comprehensive desk review and a structured questionnaire. For this chapter, the desk review documents the impact of the COVID-19 pandemic on key macroeconomic variables and their associated public debt dynamics. Data and information was drawn from different official sources, especially national statistical agencies, ministries of finance, economic development and planning organisations, and central banks. Published information from UN agencies, the World Bank, the IMF, the African Union (AU), the AfDB and the United Nations Economic Commission for Africa (among others) was also reviewed. The structured questionnaire was used specifically to collect information on the interventions of governments and the responses of central banks to the pandemic, as well as the impact of it on domestic debt markets and public debt dynamics. Respondents to the questionnaires included key officials in ministries of finance and central banks in MEFMI member countries.

The rest of the chapter is organised as follows:

- Section 2 highlights trends related to the spread of the virus and the containment measures taken by countries in the MEFMI region.
- Section 3 details the economic impact of the pandemic.
- Section 4 maps the specific policy measures implemented by governments and central banks to reduce the impact of the pandemic.
- Section 5 discusses the implications for public debt dynamics of the macro effects of the pandemic and ensuing responses.
- Section 6 highlights the lessons drawn.
- Section 7 concludes.

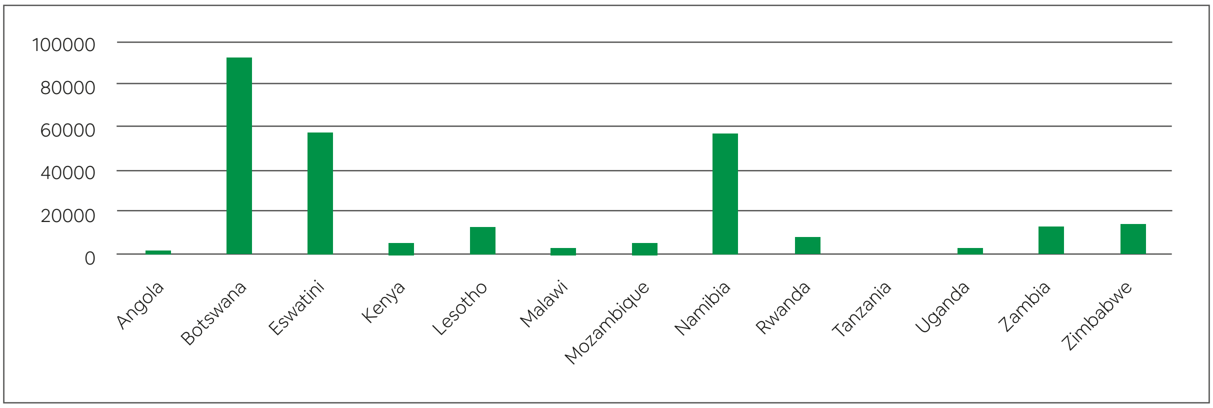
2.

COVID-19 CASES AND CONTAINMENT MEASURES IN THE MEFMI REGION

The COVID-19 virus was first reported in the Hubei province of China in December 2019. COVID-19 quickly spread across the globe and was declared a global pandemic by the World Health Organization (WHO) on 11 March 2020. The first case in Africa was identified on 14 February 2020, but the MEFMI region's first confirmed case was only detected almost a month later, in Kenya, on 13 March 2020. The majority of countries in the region registered their first confirmed cases in the second half of March 2020, while Malawi and Lesotho detected theirs in April 2020 and May 2020, respectively.

The number of new positive cases remained low in most countries in the region with community transmission realised only after a month. The initial spread of COVID-19 cases was unlike that in Europe and the US, where cases were doubling every three days. This may have been due to early adoption of containment measures, although low testing capacity could have masked the true extent of infections. The number of positive confirmed cases, however, increased in the second half of 2020, cumulatively reaching 269,134 for the MEFMI region by 31 December 2020. By country, 96,458 cases were reported in Kenya; 35,216 in Uganda; 23,941 in Namibia; and 20,725 in Zambia (John Hopkins University, 2021). The other countries in the region had fewer than 20,000 confirmed cases as of December 2020. By 31 December 2021, the total number of cases in the region had reached 1,852,137. Despite having low confirmed cases in absolute numbers, Botswana, Namibia and Eswatini had the highest positive cases per million people, as shown in Figure 1.1.

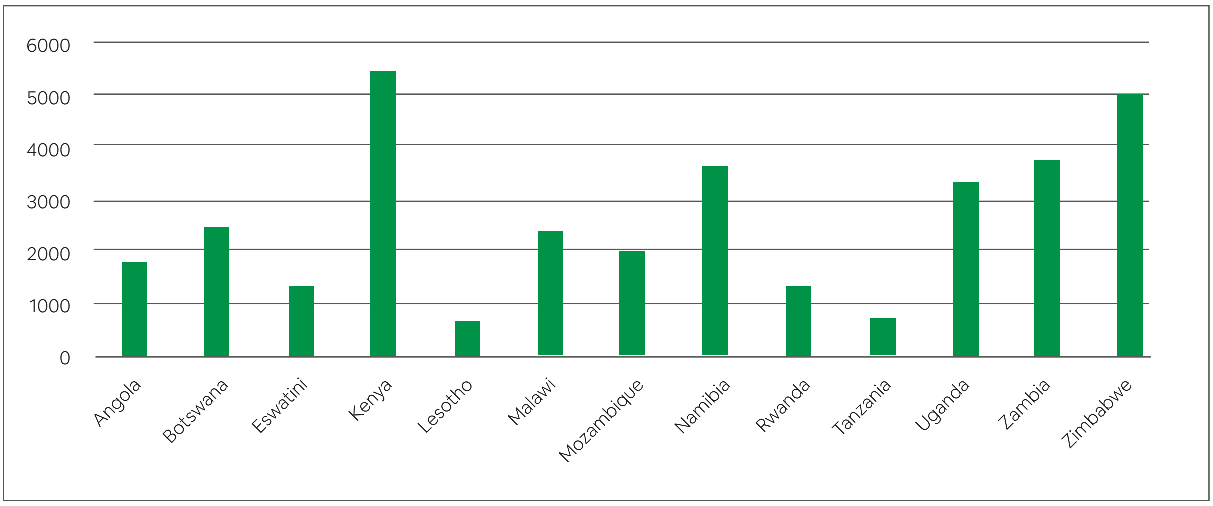
Figure 1.1: Total Confirmed Cases (per Million People) in MEFMI Region, 31 December 2021



Source: Johns Hopkins University, Center for Systems Science and Engineering.

In line with the surge in new cases in the region, the number of deaths also increased. However, fatality rates remained well below global rates. Kenya, Zimbabwe, Namibia, Zambia and Uganda have had the most deaths, while Namibia, Eswatini and Botswana have had the most deaths per million people. Figure 1.2 shows the absolute COVID-19 cumulative deaths in the MEFMI region up to 31 December 2021.

Figure 1.2: COVID-19 Cumulative Deaths in MEFMI Region, 31 December 2021

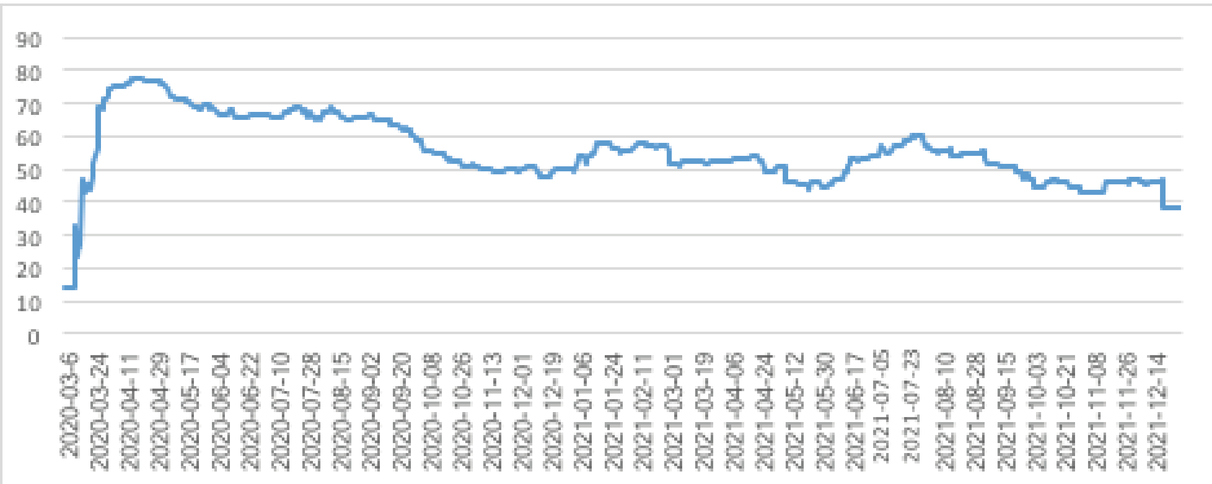


Source: Johns Hopkins University, Center for Systems Science and Engineering

New infections and deaths have moved in waves. For instance, new infections and deaths in most Southern African MEFMI countries surged during the first half of 2021 due to the Delta variant, which was assessed to be 50 per cent more contagious than earlier variants (World Bank, 2021a). As the pandemic spread in MEFMI countries, governments in the region introduced various non-pharmaceutical measures to contain the virus, in line with global best practice. Those measures ranged from testing and tracing systems to near-complete nationwide lockdowns (save for essential services).

Specifically, as infection rates started to rise, most governments in the region declared a state of emergency and instituted strict containment measures including lockdowns, border closures, restrictions on social gatherings, encouragement of teleworking where possible, establishment of isolation facilities, declaration of overnight curfews and limitations on public transportation passenger capacity. These measures were undertaken at an earlier stage of the outbreak than in many advanced economies, with countries in the region benefiting from the hindsight of global experiences. Figure 1.3 shows the stringency of containment measures for the region increasing at the peak of new waves, but then declining significantly, partly due to increased rates of vaccination.

Figure 1.3: Average Stringency Index for MEFMI Region Countries

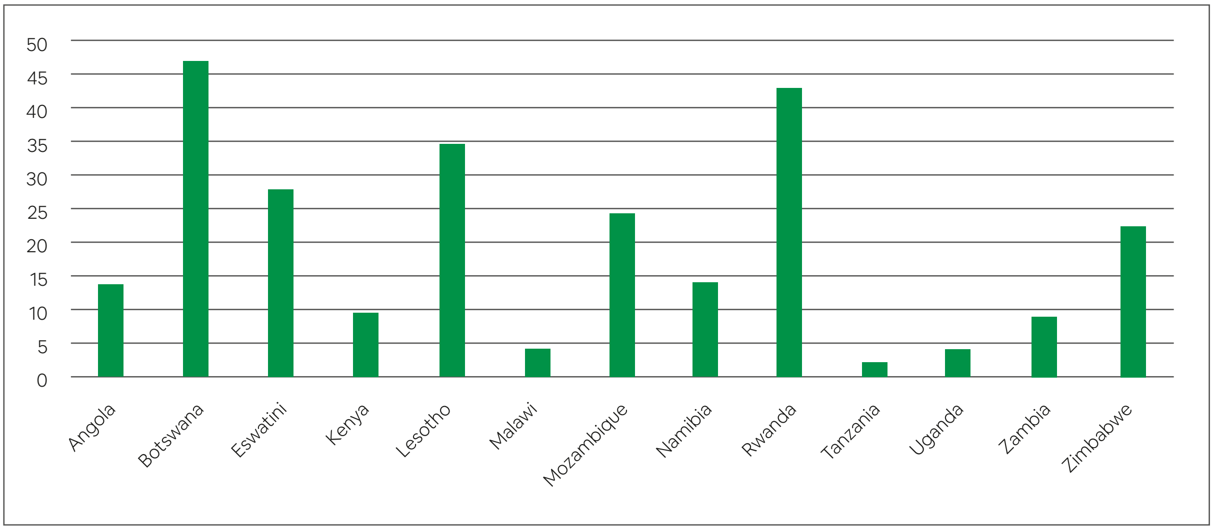


Source: Johns Hopkins University, Center for Systems Science and Engineering

The containment measures, including travel restrictions and workplace closures, initially constituted a supply shock with a negative impact on the productive capacity of economies. This later spilled over to the demand side as it adversely affected aggregate demand due loss of incomes and reduced spending. While they saved lives, the containment measures had a negative impact on economic activity. The IMF (2020b) demonstrated that countries that implemented more stringent lockdowns experienced larger declines in GDP growth. Importantly, stringent lockdowns were found to be correlated with lower consumption, investment, industrial production, retail sales and purchasing managers' indices for the manufacturing and service sectors, as well as higher unemployment rates.

Uncertainty about the future path of the COVID-19 virus continues to have a negative effect on people and economies. A return to normal life will depend on the pace of vaccination in the region, which has lagged most of the world. Within the region, vaccination rates have been highest in Botswana, at 46.8 per cent of population; Rwanda at 43.0 per cent; Lesotho, 34.6 per cent; Eswatini, 28.0 per cent, Mozambique, 24.3 per cent and Zimbabwe, 22.3 per cent. Vaccination rates elsewhere in the region were below 20 per cent at the end of 2021, with Tanzania, Malawi and Uganda below 5 per cent (John Hopkins University, 2021), as shown in Figure 1.4. Further breakdown in terms of COVID-19 vaccinations in the MEFMI region as at 23 January 2022 can be found in Annex 1.1.

Figure 1.4: Percentage of Population Fully Vaccinated as at 31 December 2021



Source: John Hopkins University, 2021.

3. IMPACT OF COVID-19 ON MACROECONOMIC VARIABLES IN THE MEFMI REGION

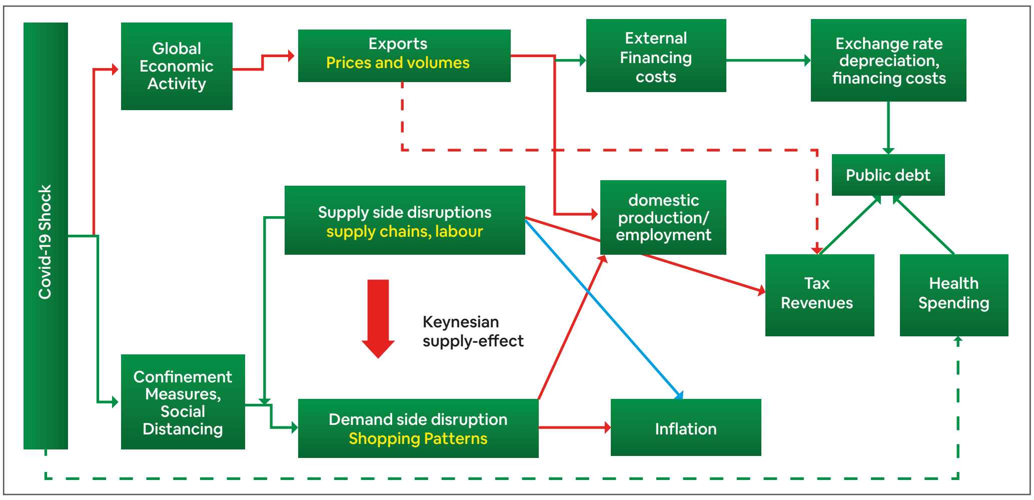
Although the MEFMI region had significantly fewer confirmed cases and fatalities than most regions in the world, the COVID-19 pandemic has taken a severe toll on the region's economies. Restrictions imposed by countries in a bid to curtail the spread of the virus led to a significant slowdown in economic activity.

The pandemic caused both a supply and demand shock, and has affected economies through domestic and external channels (Sawada & Sumulong, 2021). Initially, COVID-19 affected economies in the MEFMI region through disruptions in trade and value chains. Lockdown measures in countries and regions that were major trading partners for MEFMI countries, including China, the EU and the USA, affected the demand for exports from the region, particularly for primary products. Both the global demand and global value chains (GVCs) for oil, minerals, metals and agriculture products were affected, leading also to a fall in international prices of these commodities and affecting the export receipts for most countries in the region. MEFMI countries are vulnerable to the trade channel of transmission of COVID-19 on economic activity, due to strong participation in the commodities global value chain and increased linkage with China.

In addition to disruptions in GVCs, the supply shock worked through the direct health channel where high infections and deaths affected the availability of labour to participate in production. The decline in labour supply went beyond the number of people infected by COVID-19 because of workplace closures and travel bans, though it was partly mitigated by some people being able to work from home.

On the demand side, the disruptions caused by containment and mitigation measures imposed by governments undercut domestic aggregate demand. In addition, the uncertainty caused by the pandemic led to lower spending and investment by firms and households. Businesses cut back on investment spending as the pandemic prompted increased pessimism about future business activity and sales. COVID-19 also affected economies through reduced foreign financial flows into the region, including foreign direct investment, portfolio investments and aid flows (UNCTAD, 2021)

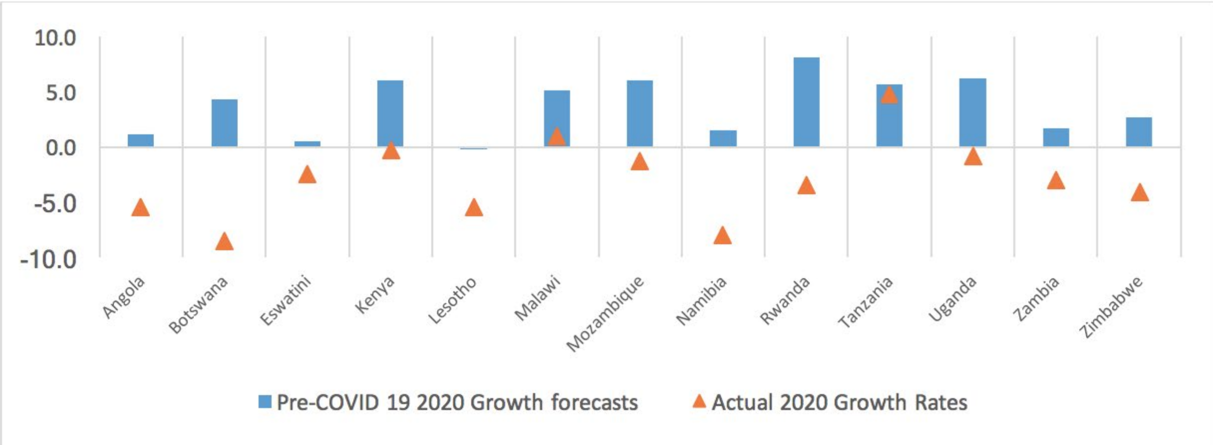
Figure 1.5: COVID-19 Transmission Mechanisms



Source: IMF (2021).
Note: Red arrows signify a decrease and blue arrows signify an increase

Lockdowns, weaker domestic demand and the disruption in supply chains resulted in a significant slump in economic growth in the region in 2020. Average real GDP growth across the MEFMI region contracted sharply to -2.8 per cent in 2020 from 2.7 per cent in 2019, largely because of the pandemic. The decline in growth varied across countries depending on the stringency of restrictions and the sensitivity of major sectors to the pandemic, with tourism- and oil-dependent economies being the most affected in 2020. Although there was some recovery in 2021, most economies remain well below their pre-pandemic growth trajectories.

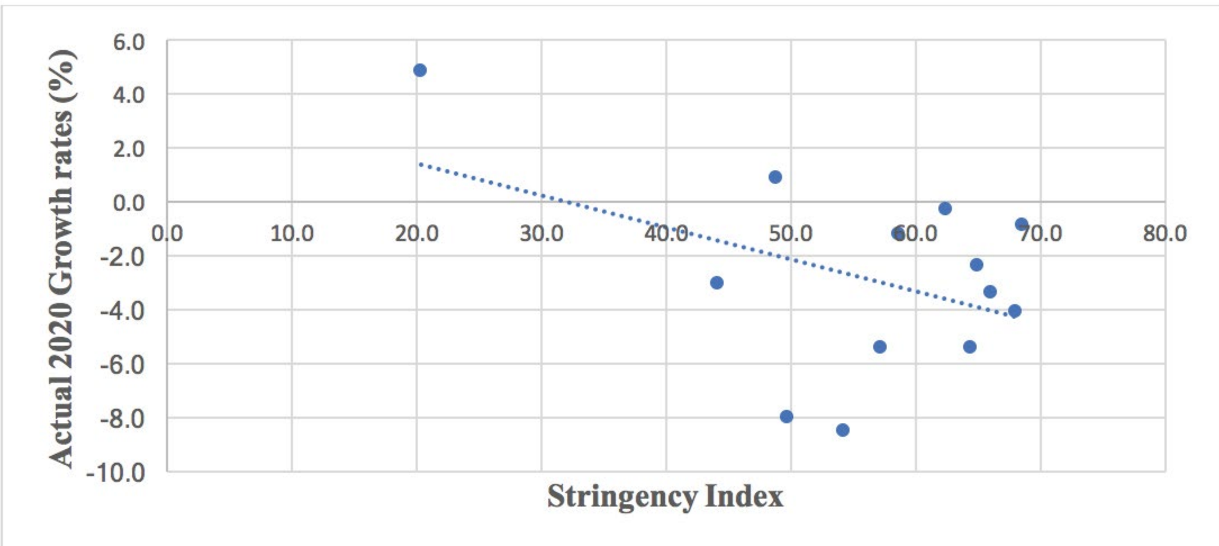
Figure 1.6: MEFMI 2020 Pre-COVID-19 and Actual 2020 Growth Rates



Source: WEO Databases, October 2019 and 2021.

As shown in Figure 1.6, GDP growth in 2020 was well below pre-COVID-19 projections, with only Malawi and Tanzania recording positive growth rates. Tanzania did not impose lockdown restrictions, and the small decline in GDP growth rate relative to pre-pandemic projections was largely on account of travel restrictions in other countries which affected its tourism sector, as well as disruptions in global supply chains. Figure 1.7 shows that those countries that imposed stringent lockdowns experienced major contractions.

Figure 1.7: Stringency Index and Actual 2020 Growth Rates



Source: Authors' calculations using data from IMF World Economic Outlook Database and John Hopkins University, Center for Systems Science and Engineering.

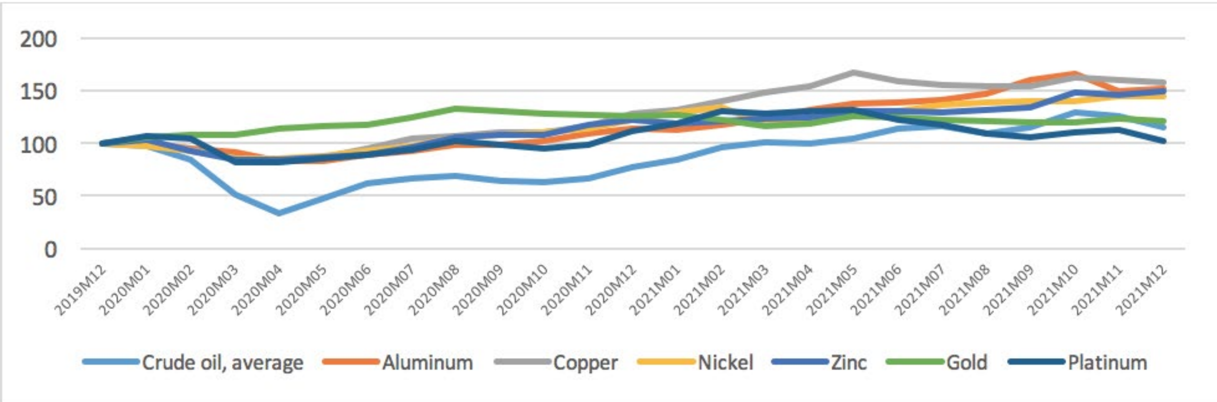
3.1 Commodity prices

The reduction in international commodity prices also contributed to the slowdown in GDP growth in the region. As shown in Figure 1.8, most commodity prices declined in 2020, reflecting reduced demand from advanced and emerging markets as those countries imposed restrictions to deal with the pandemic. As such, commodity exporters such as Angola, Zambia and Botswana suffered significant declines in export receipts.

According to data from Statistics Botswana, the country's merchandise export receipts declined by 13.1 per cent between 2019 and 2020. Earnings from diamonds, which accounted for 90.4 per cent of export receipts in 2019, fell by 15.2 per cent between 2019 and 2020. In Angola, goods export receipts fell by 39.7 per cent between 2019 and 2020, driven by a 41.3 per cent fall in export receipts for petroleum products. Petroleum products accounted for 96.1 per cent of export receipts in 2019, with diamonds accounting for 3.5 per cent. Crude oil prices fell around 33 per cent from pre-pandemic levels in April 2020 and did not recover for much of the year.

The commodity price shock affected revenues and led to a reduced capacity to service debt in several countries. However, the international prices of safe-haven commodities such as gold increased during the COVID-19. Diversified economies with higher levels of intraregional trade, particularly eastern African countries such as Kenya, Tanzania, Uganda and Rwanda, were less impacted by the commodity price shock.

Figure 1.8: International Commodity Indices (December 2019 = 100)



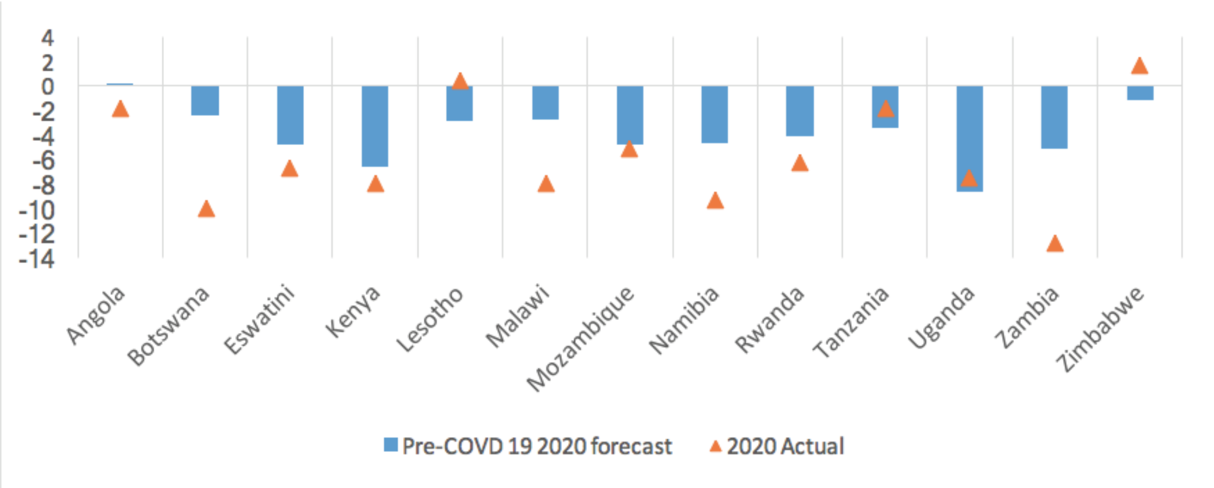
Source: World Bank, Commodity Prices Database, 2022.

3.2 Fiscal deficits

The region entered the COVID-19 crisis with countries already facing significant fiscal deficits. From -4.9 per cent of GDP in 2019, average fiscal deficit in the MEFMI region widened to -5.9 per cent of GDP in 2020 before declining to -5.5 per cent of GDP in 2021. Government revenue fell in 2020 in line with subdued GDP growth as a result of the pandemic. Fiscal support measures for the private sector, such as tax exemptions, further weakened government revenues. On the other hand, the additional health spending and fiscal stimulus measures implemented in response to the pandemic resulted in elevated government expenditures. The combination of lower revenues and higher spending inevitably resulted in worsening fiscal balances in most countries.

As can be seen in Figure 1.9, fiscal deficits in 10 MEFMI countries deteriorated in 2020 from pre-pandemic forecasts. Only Lesotho, Tanzania and Zimbabwe performed better under COVID-19 than envisaged prior to the pandemic. Zimbabwe is a special case, in that the country experienced high inflation in 2020 which led to higher nominal revenues. This, coupled with efforts to reduce government spending, resulted in a better-than-forecast fiscal balance.

Figure 1.9: 2020 Fiscal Deficits: Pre-COVID-19 Projections and Actual Outturn

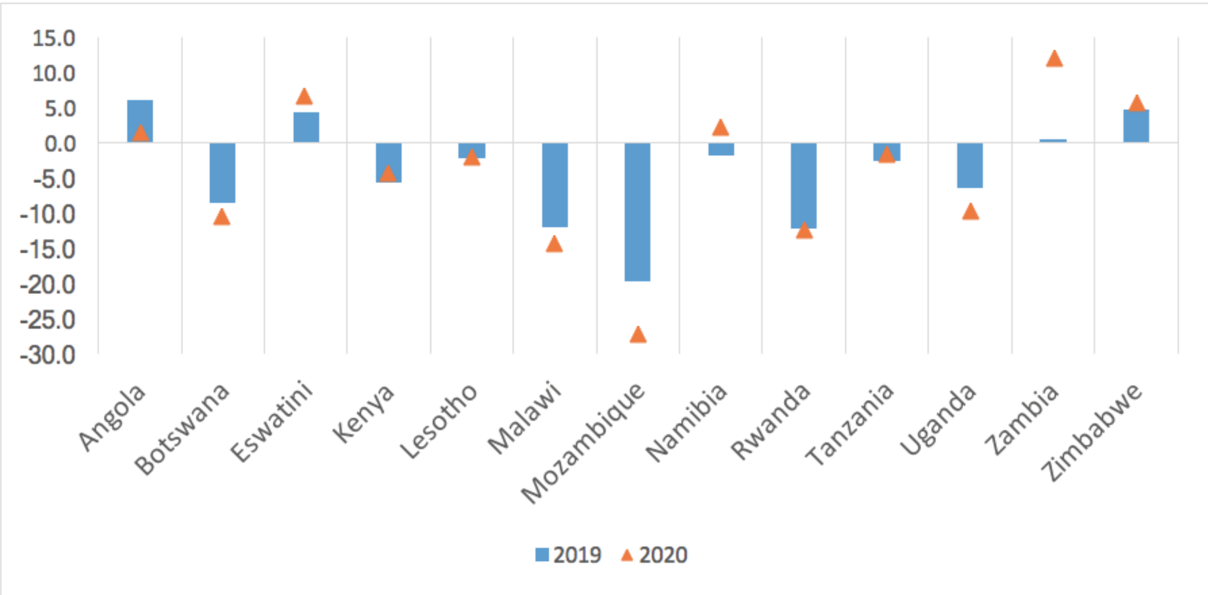


Source: IMF, WEO Databases, October 2019 and October 2021.

3.3 External positions

Disruptions to global trade, weak external demand and low commodity prices combined to negatively affect external positions of MEFMI member countries, particularly during the first half of 2020. This created increased balance-of-payments financing needs. Figure 1.10 shows that six MEFMI countries experienced worsening current account balances in 2020 compared to 2019. Those that incurred improved balance-of-payments positions benefited mainly from increased remittance flows and savings from the Debt Service Suspension Initiative (DSSI).[2] Zambia's current account improved from 0.6 per cent of GDP in 2019 to 12 per cent of GDP in 2020, driven by a decline in imports of 26.4 per cent as a result of the slowdown in domestic economic activity, depreciation of the kwacha and COVID-19-related disruptions to international trade (Bank of Zambia, 2021).

Figure 1.10: Current Account Balance (Per Cent of GDP)



Source: IMF, WEO Databases, October 2019 and October 2021.

[2] The DSSI aimed to help the poorest low- and middle-income countries mitigate the negative impacts of the pandemic by providing a temporary suspension (moratorium) of debt-service payments owed to official bilateral creditors. Further details can be found under Section 3.1.1 in Chapter Two of the study. See also Table 2.6 in that chapter on the extent of relief obtained by individual countries.

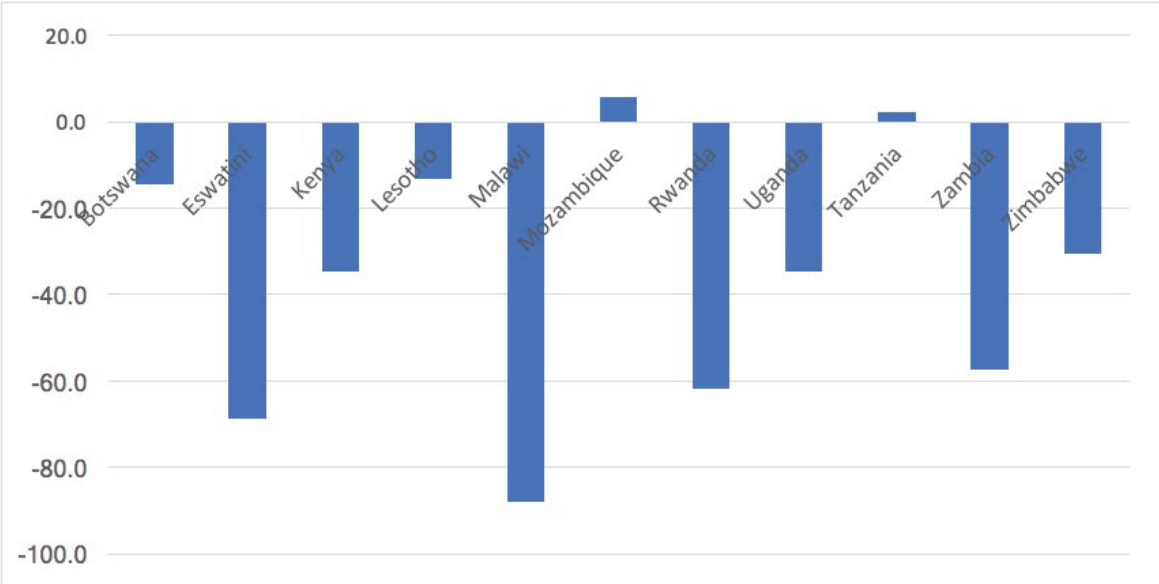
3.4 Remittances

Remittances showed resilience and performed better than expected in 2020. This was despite the recession and higher unemployment in the main source countries, including the United Kingdom, France, Italy, Spain, the United States and South Africa. Remittances also benefited from a shift in flows from cash-based to digital payments, and from informal to formal channels during the pandemic. Excluding Angola, remittance flows to the region in 2020 fell marginally, by 1.6 per cent, although the impact varied widely by country. Countries with diversified sources such as Kenya, Zimbabwe and Zambia recorded significant increases in remittances, as shown in Annex 1.3. Remittances are estimated to have improved in 2021 following better economic performance in most source countries.

3.5 Foreign direct investment

Reflecting the economic uncertainty and falling commodity prices, international capital flows, FDI and other investment flows to the region declined in 2020. As shown in Figure 1.11, FDI inflows declined in all MEFMI countries except for Mozambique and Tanzania. While FDI is estimated to have rebounded in 2021, flows are expected to remain below pre-pandemic levels. In Angola, repatriation of capital by multinational enterprises (MNEs) also slowed by more than 50 per cent in 2020.

Figure 1.11: Change in FDI Flows in MEFMI Countries in 2020

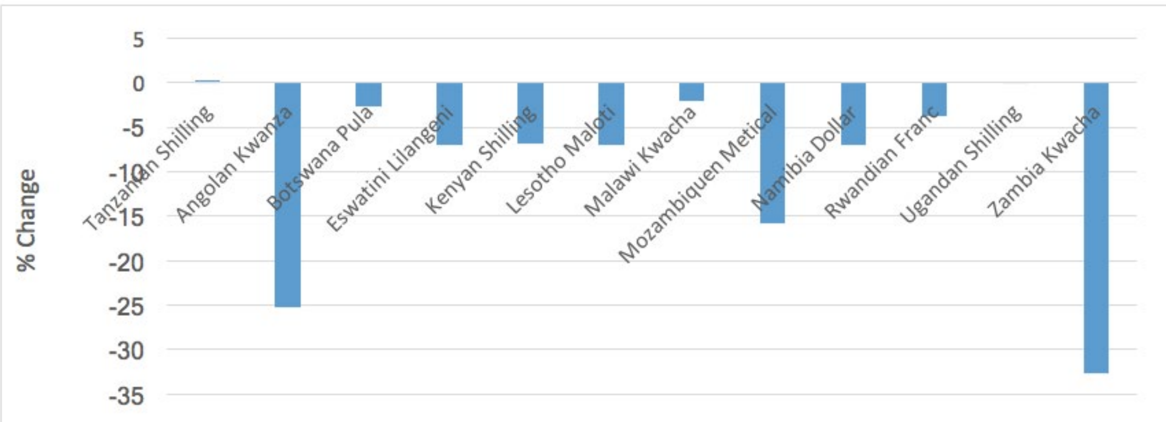


Source: UNCTAD, 2022

3.6 Exchange rates

A combination of large current account deficits and slower capital flows (FDI and portfolio flows) resulted in exchange rate depreciations, particularly where external financing needs were elevated.

Figure 1.12: Currency Depreciation between January 2020 and December 2020

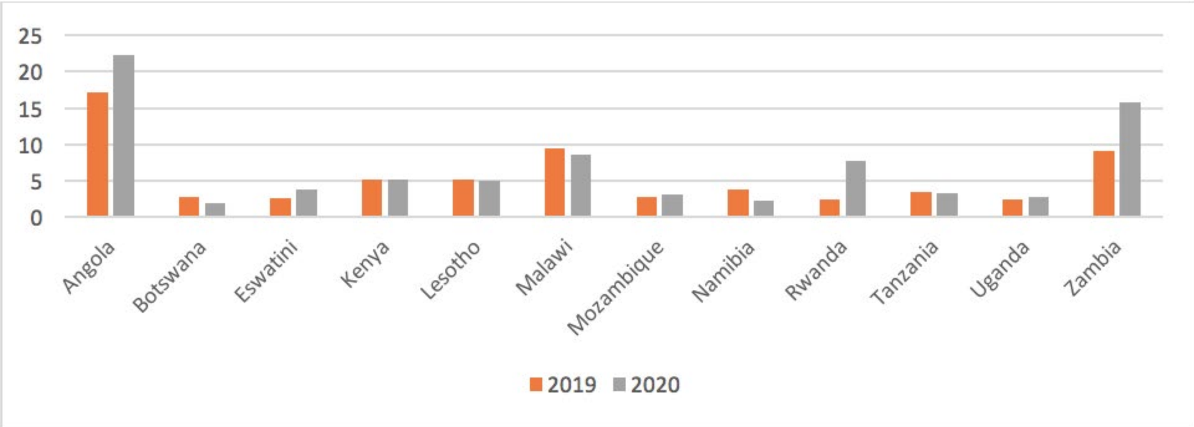


Source: Various MEFMI member central banks, 2022.
Note: Zimbabwe's currency depreciated by 80 per cent in 2020, reflecting higher inflation.

3.7 Inflation

The region's annual average inflation rate (excluding Zimbabwe) is estimated to have increased from 5.3 per cent in 2019 to 6.8 per cent in 2020, and remained elevated in 2021. Zimbabwe's annual inflation rose significantly in 2020, to above 500 per cent, driven by the unstable exchange rate as the country transitions from full dollarization. Increased inflation in Angola and Zambia in 2020 mainly reflected pass-through from currency depreciations. Food inflation surged as lockdowns put pressure on food prices. Inflation picked up in other categories too, including housing and utilities. However, some countries like Botswana, Lesotho, Namibia and Tanzania recorded declines in inflation, as shown in Figure 1.13.

Figure 1.13: Annual Inflation, 2019 and 2020



Source: IMF, WEO Databases, October 2021.

4.

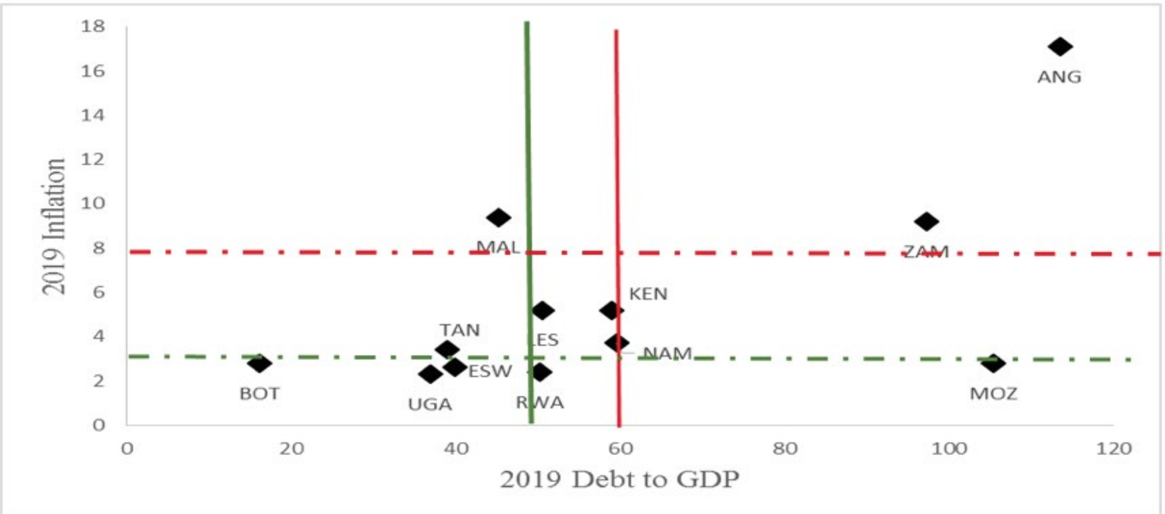
FISCAL AND MONETARY RESPONSES TO COVID-19 IN THE MEFMI REGION

As in most parts of the world, fiscal and monetary authorities in the MEFMI region responded to the pandemic by implementing a number of measures aimed at minimising its negative impact on livelihoods and improving economic resilience. The size, composition and duration of these support measures varied between countries, depending on their monetary and fiscal space. Whereas relatively low inflation afforded most countries the space to conduct countercyclical monetary policy, fiscal authorities generally had less room due to high debt levels in many countries. Debt levels in most countries were already elevated in 2019, with Zambia assessed as being at high risk of debt distress and Mozambique and Zimbabwe already in debt distress.

Based on data from the IMF's World Economic Outlook database, average public debt as a share of GDP for the MEFMI region in 2019 was 63.6 per cent, more than twice the 2013 level of 30.9 per cent.

Figure 1.14 shows the space available to MEFMI countries to undertake countercyclical fiscal and monetary policies, based on their end-of-2019 debt-to-GDP ratios and the average 2019 headline inflation rates. To gauge the fiscal and monetary space available to countries, thresholds for debt and inflation were imposed. For public debt as a share of GDP, a lower bound of 50 per cent is adopted, with the upper band set at 60 per cent.[3] The thresholds for annual inflation of 3 per cent and 8 per cent are based on the lower- and upper-bound macroeconomic convergence targets for SADC, COMESA and EAC, to which the members belong. For both public debt and inflation, countries below the lower bound are assessed as having 'substantial' space for policy intervention. Countries between the lower and upper bound had 'some' space, while countries above the upper bound had 'limited' space for policy intervention.

Figure 1.14: Inflation and Public Debt in MEFMI Countries



Source: Author's calculations from WEO 2021 Database.

[3] The lower bound of 50 per cent is derived from the MAC DSF, which uses this value to differentiate between lower and upper scrutiny countries. The upper bound of 60 per cent is derived from the SADC convergence criteria.

Figure 1.14 shows that Botswana, Eswatini, Mozambique, Rwanda and Uganda had substantial leeway to implement monetary policy, as their average inflation for 2019 was below 3 per cent. Kenya, Lesotho and Tanzania had some space, while Angola, Malawi and Zambia had limited room to manoeuvre. On the fiscal front, Botswana, Eswatini, Malawi, Tanzania and Uganda had substantial fiscal space to intervene. Kenya, Lesotho, Namibia and Rwanda, having debt levels between 50 and 60 per cent of their respective GDPs, had some fiscal space to intervene. Angola, Mozambique and Zambia had limited space, given that their debt-to-GDP ratio was above 60 per cent.

Botswana, Eswatini and Uganda had substantial space for both fiscal and monetary policy interventions. On the other hand, Angola and Zambia were above both the monetary and fiscal upper bounds and were therefore limited in their capacity to intervene. Zimbabwe (not reflected in Figure 1.15) had triple-digit annual inflation in 2019, reflecting rising food prices due to successive weather shocks, exchange rate pass-through and monetary deficit financing prior to 2018, severely constraining the country's ability to respond with monetary policy.

4.1 Fiscal responses

Due to limited fiscal space, the stimulus packages undertaken by countries in the MEFMI region were only about 2.6 per cent of GDP on average, compared to 7.2 per cent in advanced countries (World Bank, 2021b). Survey results from countries in the region, including Mozambique and Tanzania, indicated that increased fiscal spending on health came at the expense of reallocations from areas deemed non-priority and capital expenditures.

Nevertheless, MEFMI member countries implemented discretionary fiscal easing measures targeted at the most-affected households and sectors in order to mitigate the impact of the pandemic. These measures included both tax and expenditure measures.

4.2 Tax measures

The common tax measures implemented by MEFMI member countries included VAT/duty exemptions on health equipment, pharmaceutical products, food, essential goods and COVID-19 donations; deferment of tax filing; and fast-tracking of VAT refunds. These measures are shown by country in Table 1.1.

In Mozambique, the government also extended VAT exemptions on sugar, vegetable oil and soap, while Rwanda introduced VAT exemptions on construction materials under the Manufacturing and Build Recovery Program. In most instances, deferments for filing taxes were initially set at three months, although this was later extended in most cases. Eswatini, Zambia and Zimbabwe also waived tax penalties and fees on outstanding tax liabilities resulting from COVID-19.

Table 1.1: COVID-19 Tax Measures Implemented by MEFMI Members

Specific	Ang	Bot	Esw	Ken	Les	Mal	Moz	Nam	Rw	Tan	Ug	Zam	Zim
Duty/VAT exemptions on Pharmaceutical products, food, Humanitarian Aid & Donations	X	X		X		X	X		X	X		X	X
Deferred or Delays on filing taxes	x	x	X		X			X	X		x		X
Fast Tracking VAT refunds		X	X	X					X		X		
Waiver of penalties and interest for older tax debt			X									X	X
Tax refunds for SMEs paying tax obligations & retained employees													
Reduction of the turnover tax rate on small business													
Reduction of the turnover tax rate on small businesses				X									
Reduction of the standard VAT rate/income and PAYE				X								X	
PIT Exemption for teachers, tourism & hotel employees									X			X	

Source: Survey of MEFMI member countries and IMF/WB Policy Tracker/IMF Fiscal Monitor.

In addition, tailor-made tax measures were undertaken depending on country circumstances. For instance, Kenya reduced the standard VAT rate from 16 to 14 per cent, corporate tax and top PAYE rate from 30 per cent to 25 per cent, and turnover tax rate on small businesses from 3 to 1 per cent. Rwanda also exempted private school teachers, tourism sector staff and hotel employees from personal income tax.

4.3 Expenditure measures

Reflecting the severity of the pandemic, all countries in the MEFMI region increased health expenditure to improve public health and testing capacities, establish emergency response plans and purchase medical supplies. Most countries also established quarantine centres as a higher number of hospital beds were made available. In Malawi and Zimbabwe, governments postponed moratoria on employment to hire additional health workers. In addition, Botswana, Namibia and Eswatini also raised spending on health-related expenditures, including provision of water and sanitation services, given the importance of these interventions in slowing the spread of the virus.

Expenditure measures also aimed at providing temporary income support to poor and vulnerable households, including workers laid off during the pandemic. Most countries introduced and expanded social protection measures, including cash transfers and food assistance. As reflected in Table 1.2, survey results show that cash transfers and food assistance were introduced and expanded in all MEFMI countries. In Lesotho, the government expanded cash transfers directed to existing beneficiaries under the Child Grants Program and to destitute families under the Public Assistance Program. To enhance food security, the Lesotho government also provided food parcels to vulnerable households and food stamps to vulnerable Basotho living in South Africa. In addition, social protection was extended to support survivors of gender-based violence, athletes and early pre-primary/primary school-going vulnerable children. Kenya allocated KSh 10 billion (almost US$100 million) for cash transfers to cater for the elderly, orphans and other vulnerable people. The disbursement of cash transfers through mobile money was found to be effective even during the peak of the pandemic, as it had a broader reach, including rural populations and the informal sector.

Governments in the MEFMI region also expanded social protection to address the plight of those people being laid off due to COVID-19. In Namibia, the government provided a one-off payment of N$750 (about US$50) to workers who lost their jobs in the formal and informal sectors. Eswatini also established a revolving fund to cater for newly laid off workers. In Tanzania, the treasury increased social security schemes to meet the increased demand for benefits as a result of becoming unemployed.

A total of six countries also extended credit guarantees to save businesses and jobs. In Botswana, the government established a loan guarantee scheme for businesses that were tax compliant for a period of 24 months. Kenya also provided credit guarantees and a new youth employment scheme as part of the economic stimulus package while Lesotho provided a 75 per cent partial credit guarantee to businesses. Namibia gave guarantees to support low-interest loans for individuals, SMEs and agricultural businesses. Rwanda, under the Economic Recovery Fund, offered to support affected businesses through credit guarantees and subsidised loans from commercial banks. Government guarantees and subsidised loans were used to address liquidity issues and preserve employment. Payment of domestic supplier arrears and prevention of the accumulation of new ones was a key policy in Botswana, Tanzania, Uganda and Namibia, to avoid cash flow problems for businesses (particularly SMEs).

Table 1.2: COVID-19 Expenditure Measures Implemented by MEFMI Governments

Specific	Ang	Bot	Esw	Ken	Les	Mal	Moz	Nam	Rw	Tan	Ug	Zam	Zim
Additional health spending including COVID-19 vaccine	X	X	X	X	X	X	X	X	X	X	X	X	X
Expanded social protection transfers (cash)	x	x	X	X	X	X	X	X	X	X	x	x	X
Introduced/expanded food assistance			X	X	X			x	X		X		X
Credit guarantees		X		X	X			X	X				X
Reallocation of expenditure towards health			X										
Wage subsidies, waiver on training levy		X						X					
Grant/subsidies to SMEs including tourism			X		X		X	X	X				X
Improved access to water and sanitation		x	X					x					
Relief fund for laid off workers			X					x		x			
Expedition of payment arrears/obligations				X							X	X	
Youth employment schemes				X							X		X
Agriculture subsidy – inputs subsidy					X			X	X		X		X
Expanded public works programme									X	X	X		X
Price reduction of strategic prices including fuel subsidies		X				x			X				

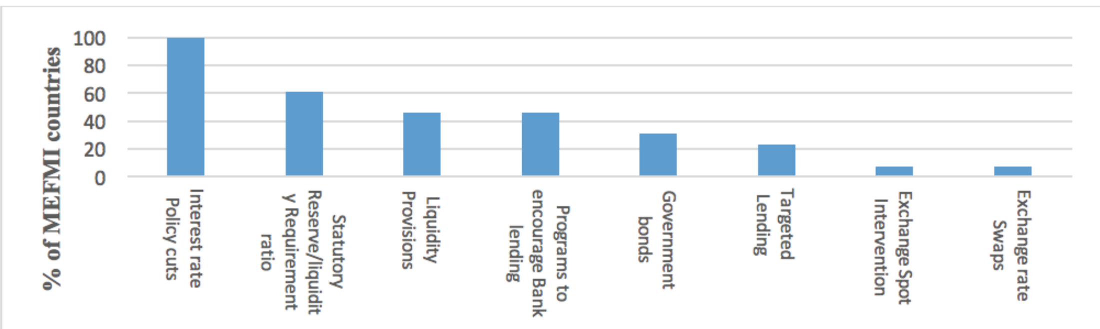
Source: Survey of MEFMI member countries and IMF/WB Policy Tracker/IMF Fiscal Monitor.

4.4 Monetary and macro-prudential responses

4.4.1 Monetary measures

Central banks in the region intervened in the monetary and prudential domains to mitigate the economic downturn. Key policy measures, which were largely aimed at increasing liquidity and boosting aggregate demand, included cutting monetary policy rates, reducing statutory reserve targets, targeted lending, increased foreign exchange flexibility and use of swaps to manage exchange rate fluctuations. Figure 1.15 shows the monetary policy responses by central banks in the region during the pandemic.

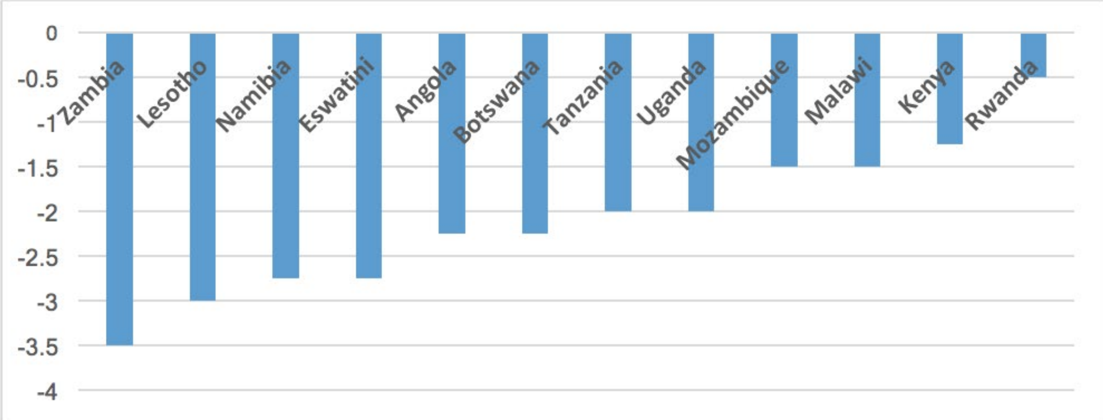
Figure 1.15: COVID-19 Monetary Policy Measures Implemented by MEFMI Members



Source: Central Bank Surveys and IMF/WB Policy Tracker

Figure 1.16 shows that all the central banks in the MEFMI region cut policy rates. Countries with the largest cuts compared to the end-2019 position included Zambia (350 bps), Lesotho (300 bps), Namibia (275 bps), Eswatini and Botswana (225 bps) and Uganda (200 bps. Zimbabwe, despite having no space for countercyclical monetary policy, reduced the policy rate from 35 per cent to 15 per cent in March 2020 before revising it to 70 per cent within three months. Interest rate cuts were also reversed in Angola.

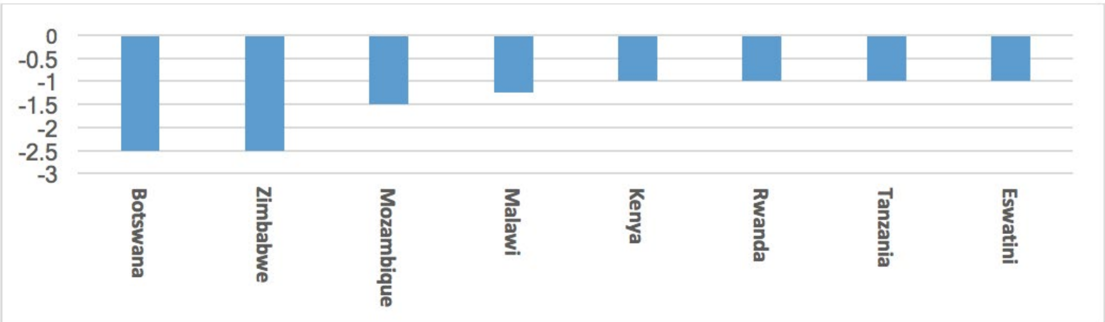
Figure 1.16: Changes in Policy Rates in 2020



Source: Central bank surveys and IMF/WB Policy Tracker

One of the main monetary responses implemented by the central banks in the region was the reduction in statutory reserve requirements, in a bid to inject additional liquidity into the market. This was particularly the case in Zimbabwe and Botswana (250 bps), Mozambique (150 bps), Malawi (125 bps) and Eswatini, Kenya, Rwanda and Tanzania (100 bps).

Figure 1.17: Changes in Statutory Reserve Requirement Ratios in 2020



Source: Central bank surveys and IMF/WB Policy Tracker

Central banks in the region introduced other tailored measures to increase liquidity in the financial system. These included the Emergency Assistance Framework instituted by the Reserve Bank of Malawi to support local commercial banks in the event of worsening liquidity. Similarly, the Bank of Tanzania reduced haircuts on government securities from 10 per cent to 5 per cent for treasury bills, and from 40 per cent to 20 per cent for treasury bonds. The measure increased the ability of commercial banks to borrow from the Bank of Tanzania with less collateral than before.

Four central banks in the MEFMI region also put in place government bond purchase programmes as part of liquidity support measures. The National Bank of Rwanda (NBR) reviewed the existing Treasury Bonds rediscounting window. The NBR offered to buy back bonds at the prevailing market rate and the waiting period if it was not possible to sell the bond at the secondary market was reduced from 30 days to 15 days. The Bank of Uganda embarked on a programme for purchases of treasury bonds held by microfinance deposit-taking institutions and credit institutions to ease liquidity pressures. Further, the Bank of Zambia undertook a bond purchase programme worth ZK8 billion (about US$44 million) to provide liquidity to the financial sector. A bond purchase programme was also implemented by the Bank of Angola (BNA).

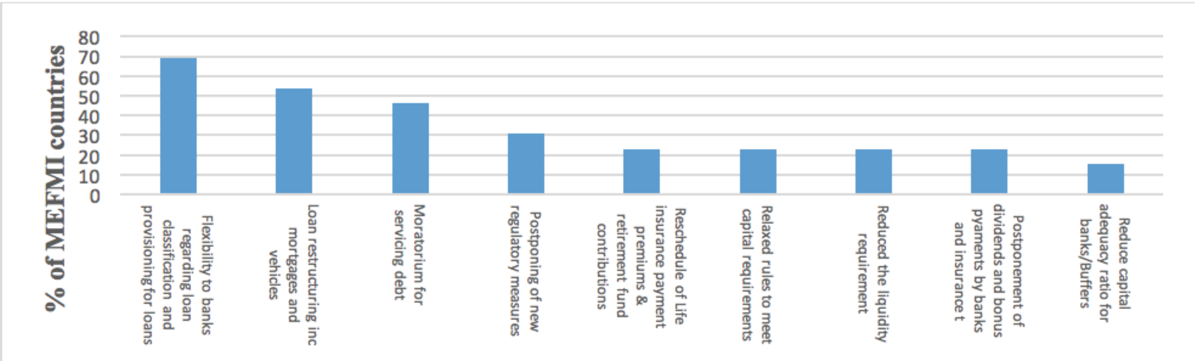
Sixty-nine per cent of central banks in the region also put in place measures to boost banks' lending operations through liquidity provisions, programmes that enhanced lending, and targeted lending frameworks to support credit to strategic and vulnerable sectors. The BNA increased the minimum bank credit allocation to producers of priority products and also directed banks to provide credit in local currency to assist importers of essential goods. In addition, the BNA reintroduced the Permanent Overnight Liquidity Provision facility to provide banks with liquidity. The Bank of Botswana (BoB) reduced overnight rates and broadened access to repo facilities by extending collateral for banks borrowing from the BoB to include corporate bonds and traded stocks. The Reserve Bank of Malawi (RBM) introduced an Emergency Liquidity Assistance framework to support banks in liquidity crisis.

The National Bank of Rwanda extended a lending facility worth RWF50 billion (0.5 per cent of GDP) to liquidity-constrained banks. The Reserve Bank of Zimbabwe (RBZ) also put in place a facility of Z$500 million to finance micro, small and medium enterprises (MSMEs), which was accessed at about half the market interest rate. The RBZ also expanded the Medium-Term Bank Accommodation facility, a window that allowed banks to access liquidity for lending to productive sectors. This was increased from Z$1 billion to Z$2.5 billion. The Bank of Tanzania set aside TSh 1 trillion (approximately US$450 million) to lend to the agricultural sector during 2021/22. Responses to exchange rate movements were more varied. Initially, Zimbabwe fixed the exchange rate at Z$25 to US$1, which was well below the market clearing rate. In June 2020, it moved to a Dutch Auction system, meant to ensure market determination of the exchange rate. Angola moved to increased exchange rate flexibility in order to reduce the parallel market premiums and engender market price discovery. Malawi used currency swaps to reduce exchange rate fluctuations.

4.4.2 Macro-prudential responses by central banks

In addition to accommodative monetary policies, MEFMI central banks relaxed regulatory and macro-prudential standards to support the provision of credit. The measures undertaken are summarised in Figure 1.18

Figure 1.18: COVID-19 Macro-prudential Measures Implemented by MEFMI Members



Source: Central bank surveys and IMF/WB Policy Tracker.

As shown in Figure 1.18, central banks in the MEFMI region put in place measures that included flexibility to banks regarding loan classifications and provisioning, loan restructuring and grant moratoria for debt service to businesses and individuals. Other measures focused on softening regulatory capital and liquidity requirements to allow banks to temporarily operate below required capital and liquidity levels. Such measures included relaxing rules to meet capital requirements, postponement of new regulatory measures, reducing capital adequacy ratios, and buffers. In three countries –Lesotho, Rwanda and Uganda – these measures were combined with restrictions on dividend and bonus distributions to preserve capital positions and shore up liquidity.

Central banks also put in place measures to promote cashless payment, particularly through the waiving or reduction of mobile money charges. This happened in Kenya, Lesotho, Malawi and Uganda. In Tanzania, the daily transaction limit for mobile money was increased.

4.5 International COVID-19 responses

Finally, broad-based support from development partners was essential in helping countries prepare health systems and raise much-needed financing. The support was provided mainly in the form of targeted financial assistance and also included debt relief measures and loans. A more comprehensive review of this international response can be found in Chapter Two of the study (see Section 3: 'Response of the International Community and Commercial Lenders'). Debt relief measures were in the form of the G20's Debt Service Suspension Initiative and the IMF's Catastrophe Containment Relief Trust (CCRT). The loans mostly came from the IMF under its various lending instruments,[4] including the Rapid Credit Facility, the Rapid Financing Instrument, the Extended Credit Facility and the Extended Fund Facility.

[4] A detailed description of IMF lending instruments is available at: https://www.imf.org/en/About/Factsheets/IMF-Lending.

5.
COVID-19 AND IMPLICATIONS ON PUBLIC DEBT DYNAMICS

As with much of sub-Saharan Africa, public debt in the MEFMI region was rising even before the onset of the pandemic. The comprehensive review of the debt portfolio and its evolution in the MEFMI region carried out in Chapter Two of the study shows that the pandemic did lead to acute acceleration in the pace of debt accumulation.

5.1 Key trends in explosion of debt levels in the MEFMI region

A number of key pointers from the growth in debt levels are worth reiterating here:

- The average debt-to-GDP ratio for the MEFMI region rose from only 28 per cent in 2011 to 63.4 per cent in 2019, before increasing further to 70.6 per cent in 2020 (Figure 2.4, Chapter Two).

- The increase in debt mainly reflects the decline in GDP growth rates and increase in fiscal deficits to meet increased expenditures against lower revenue and partly depreciating exchange rates. Due to limited fiscal space, countries in the region had to resort to increased borrowing to acquire additional doses of coronavirus vaccines. In addition, the pandemic has worsened the balance sheets of state-owned enterprises, resulting in contingent liabilities.

- The region has also seen a gradual shift away from multilateral to bilateral and private debt. The latter is typically commercial in nature and includes Eurobonds. Consequently, multilateral debt, which tends to be highly concessional, decreased from 62 per cent of external debt in 2012 to 54 per cent in 2020. Over the same period, bilateral debt increased from 27 per cent to 31 per cent of external debt, while private debt increased from 11 per cent to 14 per cent (Figure 2.6, Chapter Two).

- In tandem with the increase in public debt, there has been a rapid increase in the spreads of Eurobonds issued by countries in the region (Table 2.2, Chapter Two).

- There has also been a deterioration in risk ratings across the MEFMI region over recent years, which was accelerated by COVID-19 in 2020 and 2021 (Table 2.3, Chapter Two).

5.2 Debt-carrying capacity

In a few of the countries, debt-carrying capacity has also deteriorated during the pandemic. This has contributed to worsening ratings of these countries' risk of debt distress. A confluence of negative factors due to COVID-19, including subdued outlooks for medium-term global and domestic growth and reduced reserve coverage, have conspired to diminish the debt-carrying capacity of most countries in the region. As such, many countries have had their debt-carrying capacity downgraded, as shown in Table 1.3.

Table 1.3: Evolution of Debt-Carrying Capacity Ratings in the MEFMI Region

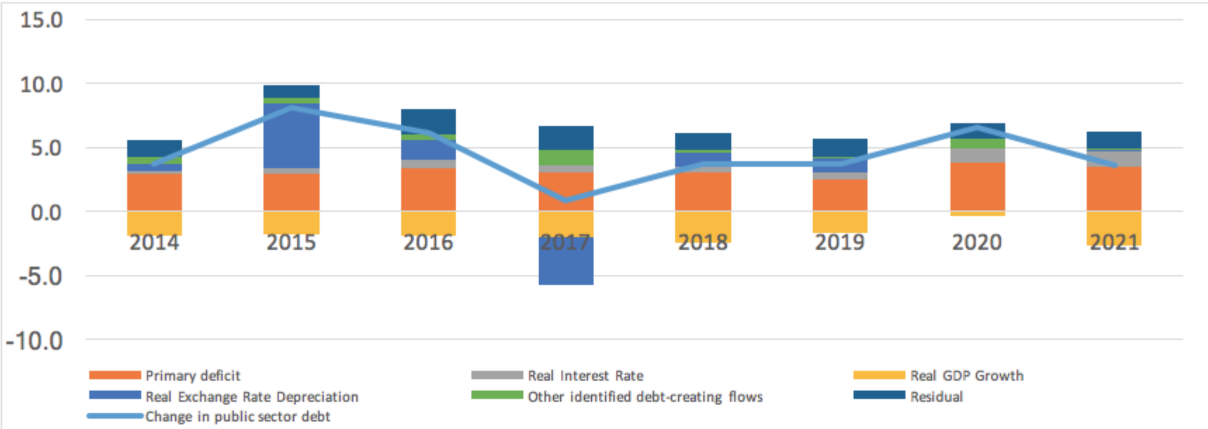
	2018	2019	2020	2021
Kenya	Strong	Strong	Strong	Medium
Lesotho	Medium	Medium	Medium	Medium
Malawi	Weak	Weak	Medium	Weak
Mozambique	Medium	Weak	Weak	Weak
Rwanda	Strong	Strong	Strong	Strong
Tanzania	Strong	Strong	Strong	Medium
Uganda	Strong	Strong	Strong	Medium
Zambia	Medium	Weak	Weak	Weak
Zimbabwe	Weak	Weak	Weak	Weak

Source: IMF/World Bank DSA Reports.

5.3 Drivers of Public Debt in the MEFMI Region

During the pandemic, additional fiscal stimulus, lower-than-expected growth, rising borrowing costs, realisation of contingent liabilities and currency depreciation caused by external pressures have conspired to affect debt dynamics significantly. The increase in public debt in the MEFMI region since 2014 has been mainly driven by additional borrowing. Figure 1.19 shows primary deficit as the main variable driving debt upwards throughout the period, with this becoming more pronounced during 2020 and 2021 because of additional borrowing to meet increased expenditure in response to COVID-19. Previously, real GDP growth has played a key role in mitigating the increase in debt. However, the onset of the pandemic in 2020 significantly affected GDP growth, which also contributed to a sharp rise in public debt across the region. The real interest rate also gained prominence in 2020 and 2021 as one of the major factors exerting upward pressure on the debt-to-GDP ratio. This points to a general increase in the cost of debt as countries in the region increasingly turn to non-concessional debt to finance their budget deficits.

Figure 1.19: Drivers of Public Debt in the MEFMI Region



Source: IMF/World Bank DSA Reports.
Note: This figure represents the average for MEFMI countries assessed using the LIC DSF.

There has also been a deterioration in risk ratings across the MEFMI region over recent years, and this accelerated due to COVID-19 in 2020 and 2021.

In the medium term, public debt in the MEFMI region will depend largely on the future path of COVID-19 and its impact on fiscal positions and macroeconomic variables, including GDP growth, real interest rates and exchange rates. What is clear, however, is that COVID-19 worsened debt positions in the region and countries should quickly embark on fiscal consolidation to put debt back on a sustainable path as soon as the pandemic situation allows. In addition, any available buffers (including special drawing rights) should be carefully deployed in a manner that promotes economic recovery and improves debt-carrying capacity.

6.

LESSONS LEARNT FOR PANDEMIC MANAGEMENT AND RESPONSES

Governments in the region took policy actions to cope with the COVID-19 pandemic and its adverse impacts. This section discusses the key lessons learnt from the responses of governments in the MEFMI region. Such lessons can shape policy making before or during future pandemics or other shocks that lead to severe economic downturns. Among the key lessons are:

I **Ensure that debt is sustainable.** This will provide countries with space to borrow in times of crisis. Countries with high debt levels may find it difficult to access international credit markets or even multilateral/bilateral creditors due to the high credit risk. Botswana, Eswatini, Malawi, Tanzania and Uganda were the MEFMI countries whose debt-to-GDP ratio was below 50 per cent in 2019. These countries utilised their fiscal space to borrow in 2020, as shown by their relatively high fiscal deficits for that year.

II **Countries should also build fiscal buffers** in times of high economic growth or high commodity prices, as these are critical in implementing countercyclical fiscal policy during a crisis. For commodity-dependent countries, the establishment of sovereign wealth funds cannot be overemphasised.

III **The pandemic has showed the importance of building capacity in debt management,** particularly through improved debt data quality, risk analysis of debt instruments, processes and institutions. Contingent liabilities pose a risk, and debt management offices need to monitor, assess and manage them carefully.

IV **Low and stable inflation provides room for monetary policy response.** Although high inflation can lead to a significant fall in the real value of government domestic debt, rising price levels could be detrimental to the growth prospects of the private sector and the economy at large. When inflation is low and expectations well anchored, monetary authorities have the space to respond to a shock such as the COVID-19 pandemic. In countries where inflation was low before the start of the pandemic, monetary authorities were able to reduce policy rates and leave them at lower levels for an extended period to enable pass-through of the policy change to other interest rates in the economy. In countries where inflation was high, such prolonged policy changes were difficult for central banks to sustain.

V **International cooperation remains critical to fostering rapid and effective responses to shared threats.** Many developing countries are not able to deal with large shocks without external assistance. Most countries in the region were able to access resources from the IMF, although this differed by country. The most notable recipients of IMF loans during the pandemic were Kenya and Uganda, which agreed financing and policy surveillance programs with the Fund, while Angola requested additional resources under a pre-existing financing programme. International cooperation was also evident in the implementation of the DSSI, which provided much-needed liquidity for a number of countries in the region. MEFMI countries also benefited from international efforts to avail vaccines under the COVAX facility, as well as bilateral donations. The international community also donated testing kits, masks, personal protective equipment and other medical supplies needed in the COVID-19 fight.

VI **Reforms to domestic revenue mobilisation efforts.** The pandemic illustrated the importance of having robust tax systems that can enable countries to raise sufficient domestic revenues to combat economic shocks. Many countries needed urgent international assistance to help finance their pandemic response because tax systems were beset by years of underperforming and could not raise much-needed revenues. Reforms that create a broader tax base and make the tax system more progressive will yield important resources with which countries can build economic resilience and deal with future economic shocks. Many tax systems in the region are characterised by illicit resource outflows, which are enabled by domestic governance failures and corruption, including tax evasion, mis-invoicing, profit shifting and transfer pricing. Curbing illicit flows is central to the development financing challenge for the continent, since they deprive countries of resources that could have been used to access a debt sustainability path (Heitzig, Ordu and Senbet, 2021). Moreover, countries in the region should explore ways of taxing digital transactions, given that such transactions are expected to take up an increasing share of trade in future.

VII **Public financial management reforms should be expedited.** In addition to tax reforms, areas such as transparency and accountability in the use of public finances need to be given more attention. Having a track record for transparency and accountability builds domestic and international confidence in a country's economy and government. Budgets should become more efficient, with more resources allocated to social and development investments rather than increasing the size of government.

VIII **Less diversified economies are more vulnerable to commodity price shocks.** Countries that rely heavily on one or two commodities can be severely affected when prices fall. Examples in the region include Botswana (diamonds), Angola (oil) and Zambia (copper). These countries suffered significant falls in export receipts when the prices of their main exports fell during the pandemic. Countries that rely on tourism were also affected by international restrictions on travel. Countries should diversify their economies by expanding manufacturing and service sectors and decreasing reliance on extractive industries. One principle consideration is that structural transformation strategies must contribute to growth in productivity, focusing more on value-added 'sophisticated' tradable sectors that are essential to creating better-paying jobs.

IX **Digitalisation of the economy enables faster and more effective interventions.** Digitalisation has helped in rolling out fiscal support such as cash transfers, which were key in ensuring that social protection was more targeted. In addition, digitalisation is critical in enhancing industrial performance, even during the pandemic, as it allows free flow of communication and home working (Rhee & Svirydzenka, 2021). As such, policies to scale up digital transformation in MEFMI countries by attending to issues such as e-commerce regulation, electronic payments and regulatory measures to protect consumer data, are critical in building resilience to shocks. It is also important to increase trade facilitation through trade digitalisation and the development of paperless and contactless trade. Governments should invest in broadband connectivity to make internet access ubiquitous and affordable.

X **Targeting of interventions achieves better, faster results**. Given the limited fiscal space, countries need to implement targeted measures to ensure that public resources are channelled to the most vulnerable firms and households. Targeting allows a larger share of transfers to reach their intended targets. While many countries extended little assistance to the most vulnerable in the informal sectors, Eswatini and Lesotho stood out in targeting their interventions. Eswatini subsidised the cost of COVID-19 tests for informal cross-border traders, while Lesotho extended grants of LSL500 per vendor in the informal sector. Informal economies are the engines of employment creation in most MEFMI countries. However, informal workers are often not covered by health and unemployment insurance and other benefits. Informal workers are also concentrated in sectors hit hardest by COVID-19, including hospitality, retail, tourism and transport.

XI **There is a need for continued policy intervention, as economic recovery will be slow.** Although economic output in advanced economies will return to pre-pandemic trends in 2022, developing countries (excluding China) are projected to remain 5.5 per cent below pre-pandemic forecasts in 2024 (IMF October 2021 WEO). This shows that most developing countries will continue to require some form of fiscal stimulus for the next few years. Countries with the fiscal space to provide assistance to the private sector should continue to do so. Unfortunately, a number of countries in the MEFMI region, including Angola, Mozambique and Zambia, lack such space due to elevated debt levels and a high debt service burden. Nevertheless, the pandemic has highlighted the importance of having a healthy fiscal position. After economies recover in the medium term, countries would do well to improve their fiscal positions by making efforts to improve domestic revenue collections as well as improving expenditure efficiency. A number of countries also have fiscal rules to which they should adhere. Rules agreed to in regional blocs such as the SADC and EAC should also be taken into account in the design of fiscal policy.

7.
CONCLUSION

The unprecedented health and economic crisis resulting from the COVID-19 pandemic led to a wide range of fiscal and monetary responses by countries across the globe, including in the MEFMI region. Countries in the region instituted COVID-19 policy responses despite entering the crisis with limited fiscal space. Debt vulnerabilities, which were significant before the pandemic, have been exacerbated. Debt-carrying capacity has been eroded and the risk of debt distress heightened. The slowdown in economic growth makes fiscal consolidation difficult, due to tax revenue shortfalls and increased need for fiscal stimuli. Nonetheless, it is important to reform public financial management with a view to increased efficiency in the use of available resources as well as returning to fiscal sustainability in the post-pandemic world.

Premature consolidation, however, may stall economic recovery, while delayed or incomplete consolidation can lead to increased risk of debt distress with serious adverse economic consequences. As such, overcoming the increasing debt sustainability challenges requires that MEFMI countries not only invest in health and social protection systems but also embed long-term sustainability into stimulus packages and recovery policies, in order to strengthen resilience to future shocks. Importantly, international support remains critical as countries in the region face the likely trade-off between sustainable debt and sustainable development in the post-COVID period.

The lessons from the pandemic, especially the need to maintain fiscal and monetary space, should not be forgotten as they will serve the region well in the event of a future pandemic or another large economic shock. Importantly as argued by the IMF (IMF, 2020a), crisis response policies are temporary and should be implemented transparently, with effective communication to assure stakeholders that the increase in fiscal deficits and public debt will be reversed after the crisis. Such an approach will ensure that the region stays on track to meet its medium-term objectives, which include building resilience, restoring growth to create jobs, and achieving other sustainable development goals. In this, spirit, resilience to climate change should be built, with particular focus on coping and mitigation measures.

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Annex 1.1: COVID-19 Vaccinations in the MEFMI Region as at 23 January 2022

Country	Doses administered	People fully vaccinated	% of population fully vaccinated
Angola	12,690,132	4,308,880	13.54
Botswana	2,210,690	1,079,089	46.84
Eswatini	440,245	321,392	27.99
Kenya	11,542,128	5,082,976	9.67
Lesotho	698,383	735,610	34.61
Malawi	1,864,968	763,510	4.10
Mozambique	17,031,660	7,388,072	24.33
Namibia	759,685	354,975	14.23
Rwanda	13,892,895	5,435,180	43.04
Tanzania	2,431,769	1,359,225	2.34
Uganda	12,430,501	1,809,627	4.09
Zambia	2,258,222	1,582,151	8.86
Zimbabwe	7,506,786	3,267,249	22.31

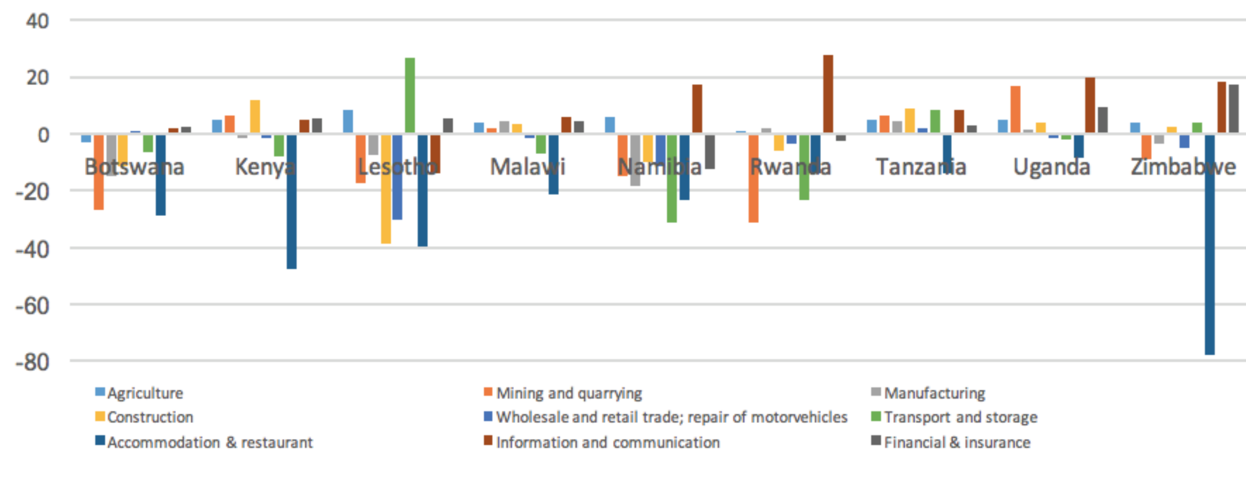
Source: John Hopkins University, https://coronavirus.jhu.edu/.

Annex 1.2: GDP Sectoral Performance in MEFMI Countries in 2020

Box 1: GDP Sectoral Performance in MEFMI Countries in 2020: Production Approach

Most countries in the region recorded negative GDP growth rates because of the pandemic. While COVID-19 affected virtually all sectors of the economy, service sectors were hit disproportionally. These include transport, hospitality, tourism, leisure, retail and wholesale.

Sectoral Growth Rates for Selected Industries in some MEFMI Member Countries



Source: Various national bureaus of statistics.

As shown, all MEFMI countries suffered significant declines in 2020 in the accommodation and restaurants sector, reflecting the impact of COVID-19 on tourism. The major declines in the accommodation and restaurants sector were recorded in Zimbabwe (78 per cent decline), Kenya (47.7 per cent) and Lesotho (39.6 per cent). The decline in this sector was caused by a reduction in tourist arrivals due the closing of borders, and stringent requirements such as the need for PCR tests and quarantining of passengers. International tourist arrivals declined by 72 per cent in Kenya, 70 per cent in Uganda, 69.7 per cent in Rwanda and 64.9 per cent in Tanzania (Muoki, 2021). Prior to the outbreak of COVID-19, the travel and tourism sector had been a major source of revenue and jobs for many countries in the MEFMI region. The decline in international arrivals reduced international tourist receipts by about 70 per cent on average for the four countries mentioned above and reduced jobs in the tourism industry in these countries by 50 per cent. Similar trends were also noted in Zimbabwe and Namibia, where international arrivals declined by 83 per cent and 79 per cent, respectively.

Tourism contributes significantly to GDP and export receipts in some of the MEFMI member countries. In terms of export receipts, tourism contributes 27 per cent in Tanzania, 25 per cent in Rwanda, 18 per cent in Uganda and 15 per cent in Kenya, while it contributes more than 10 per cent of GDP in Namibia, Lesotho, Tanzania, Botswana and Kenya (World Bank, 2020a). Considering the importance of international tourism receipts to most MEFMI countries before the pandemic, the sharp decline in international visitors had a devastating economic effect on these economies. The decline in the tourism sector had negative spill-over effects through industry linkages and led to job losses mainly in the MSMEs that had catered to tourists or related industries. The emergence of more contagious variants of the coronavirus, such as Delta and Omicron, has led to increased uncertainty regarding when international travel is likely to return to pre-pandemic levels.

The wholesale and retail trade sector also suffered huge losses in 2020, reflecting the impact of curfew, fear of contracting disease and reduce incomes. Other sectors with significant declines include transport and storage as a result of travel restrictions and closer of borders and manufacturing activities due to disruptions of global value chains and closure of companies.

The only sector that registered positive growth rate in 2020 across all countries in the region was the Information and Communication sub sectors benefiting from tele-commuting, online conferences and training, among other activities.

Annex 1.3: Remittance Flows into the MEFMI Region in 2016–2020 in US$

Country	2016	2017	2018	2019	2020
Angola	3,988,048	1,418,196	1,579,247	3,445,473	8,053,051
Botswana	24,622,502	38,956,561	44,309,897	59,360,104	35,615,908
Eswatini	98,421,044	144,415,394	125,737,322	118,702,082	112,495,380
Kenya	1,744,642,661	1,962,264,726	2,720,366,061	2,838,192,215	3,100,000,000
Lesotho	453,529,595	549,810,084	581,803,816	543,706,904	470,565,620
Malawi	39,053,133	78,392,830	180,578,523	217,457,944	189,021,274
Mozambique	93,372,690	257,936,772	296,070,199	299,567,589	348,813,813
Namibia	66,479,265	48,292,447	53,670,691	65,593,517	64,026,883
Rwanda	172,516,841	215,292,395	260,511,616	260,710,295	241,000,000
Tanzania	402,531,458	403,305,722	412,910,078	433,498,219	409,138,394
Uganda	1,146,050,427	1,165,739,411	1,338,053,925	1,424,508,663	1,051,170,000
Zambia	38,464,441	93,644,095	106,965,626	98,259,121	134,864,832
Zimbabwe	1,856,034,931	1,729,883,817	897,902,104	921,726,525	1,209,718,045

Source: World Bank, 2021.

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