



## **African Fiscal Forum: Fiscal Policy Challenges in Africa 9- 10 November, Townhouse Hotel and Conference centre, Cape Town**

### **Opening address by Nhlanhla Nene, Deputy Minister of Finance, South Africa**

Good morning ladies and gentlemen. It is with great pleasure that I welcome you all to the inaugural African Fiscal Forum, jointly hosted by the National Treasury of South Africa and the International Monetary Fund (IMF), with the support of the Collaborative African Budget Reform Initiative. The forum brings together representatives from Ministries of Finance from 14 African countries, the IMF, World Bank, OECD and African Development Bank to discuss fiscal policy challenges facing the economies and governments on the continent.

Over the next 5 years, seven of the 10 fastest growing countries are expected to be in sub-Saharan Africa. And as uncertain economic conditions continue to prevail in the developed markets of Europe and America, as well as in emerging markets, it is important for us to focus on medium- to long-term considerations in order to sustain the continent's economic expansion and growth.

Fiscal policy is generally recognised as one of the best tools available to policymakers to ensure macroeconomic stability and long-term growth. And the 2008-2009 financial crisis illustrated the importance of fiscal buffers in managing an economic downturn. Most macroeconomic policies in Africa remain supportive of growth and the fiscal stimulus measures implemented during the global downturn continue to spur growth in the region. This ensures countries in the region continue to expand close to their highest growth in many years.

As the continent navigates its way through the next few years, fiscal authorities need to strike a balance between addressing the challenges of strong, inclusive growth through sound fiscal management of spending and revenue, and the potentially

adverse effects of another global downturn. The programme over the next day and a half aims to provide a broad range of perspectives and sharing of lessons from the crisis and ideas for the next phase of fiscal development and management.

Africa continues to find itself in the fortunate position of still being able to access debt and grant funding, as the continent is seen by many developed and emerging countries as a safe haven for excess savings and investment. The diminishing availability of financing in developed countries, and the risk of overheating in emerging markets could mean this inflow of budget support and foreign savings may not always exist. The conference will therefore focus on issues around managing the commodity price cycle, macroeconomic risks to the budget, fiscal policy priorities and sustainably financing development. The forum will also address how countries can prepare for the next crisis, while continuing to meet fiscal policy priorities.

The development of fiscal space prior to 2008 meant countries were able to respond to the global downturn by maintaining expenditure priorities, despite any slowdown in revenue collections. Provided global growth continues to recover, albeit slowly, countries should work towards rebuilding these fiscal reserves in order to respond to future crises when they arise. Fiscal space can be developed in several ways.

Firstly, the improvement of revenue management and collection provides a big opportunity for countries in Africa to increase fiscal reserves and reduce dependency on foreign aid. By expanding the tax base in countries, governments will be able to continue to sustainably manage expenditure priorities and debt over the long term. Secondly, where aid financing is available, targeted programmes to improve investment will assist countries in reaching their growth potential and lower the cost of doing business on the continent. Thirdly, the availability of debt financing and the willingness of investors to provide finance at reasonable interest costs, will also determine the ability of countries to continue to finance fiscal priorities and infrastructure. Finally, and probably most importantly, the management of expenditure has an increasingly prominent role to play in the development of fiscal space. The lessons from the current problems facing the euro zone and US provide Africa and the developing world with an opportunity to address the composition and efficiency of government expenditure. Are current expenditure plans optimal to the continent's goals for expansion and growth? And most of all are they sustainable? By addressing the efficiency and effectiveness of government spending, governments can improve the quality of fiscal deficits by focusing on areas of spending with the biggest multipliers for economic support, macroeconomic stability, and inclusive growth.

In addition to the risks associated with rebuilding fiscal space, policymakers face additional challenges in determining what events in the economic environment relate to cyclical fluctuations in the business cycle and revenue performance, and what are structural or permanent changes in the environment in which they operate. African

countries also face inflationary risks from rising fuel and food prices, as well as the potential for overheating. The coordination of monetary and fiscal policy management can assist in mitigating these risks.

The IMF foresees fiscal deficits remaining at higher levels in many countries over the next 2 years, despite the generally strong growth environment. In many of the countries in the region, this reflects the once-off exogenous shock to public finances in response to the financial crisis. In others, however, it reflects faster spending growth. If the economic growth outlook declines, there may be a need for fiscal deficits to temporarily widen further in order to continue to support aggregate demand. This is, obviously, dependant on the availability of financing and country-specific debt sustainability considerations.

The key to sustaining Africa's expansion is to remain focused on medium-term issues of sustainability, stability and growth, rather than short-term gains. Governments across the continent should manage their public finances with a focus on maintaining planned spending initiatives, while automatic stabilisers operate on the revenue side. The consideration that needs to be made is whether the increases in expenditure can be absorbed and spent efficiently. If the global slowdown persists and indicates a change in the structural level of growth, spending plans and tax policies should be adjusted in line with lower growth and financing forecasts. For commodity exporters, specifically oil, the improved terms of trade conditions provide additional opportunities to build reserves and buffers to counteract future price volatility and fiscal pressures.

Traditional trading partners in the US and Europe continue to account for almost half of sub-Saharan Africa's exports. While there has been an increase in the volume of trade with emerging market partners, such as China and India, the trade with developed countries remains a crucial source of official financing as well as a source of remittances and investment flows. Any further revisions to the growth outlook in these countries would therefore likely affect the performance of Africa over the next 2 years. Previously, the slowdown in trade between Africa and the US and euro zone in 2009 – 2010, was mitigated by continued strong demand from emerging market trade partners. This helped to support continued economic expansion in Africa. Over the next few years, however, it is expected that economic activity in countries like China and India, as well as other major emerging markets will likely decelerate as they adjust policies to counter overheating.

The IMF, however, sees that "the positive response of the region's exports to the recovery in world trade from the global financial crisis augurs well for external viability and growth." Regardless of the outlook for global economic performance, African countries need to work at addressing fragilities in their own fiscal management. Governments need to shift public finances from the expansionary stance taken during the downturn in 2008 – 2009 to a more neutral stance consistent

with debt sustainability. Should the downside risks in the global economy emerge, the space for additional discretionary fiscal stimulus is limited.

The focus on improved fiscal management and sustainability will place countries on a sound footing for further growth and development over the medium to long term. Failure to manage dependence on aid financing and growing debt stock will ultimately lower the growth potential of countries and reduce their ability to respond to future fiscal challenges and economic crises. Issues of political risk, governance and regional integration must be managed in conjunction with fiscal considerations. The coordination of monetary and fiscal policy will support the management of commodity price volatility, inflationary pressures, stabilise interest and exchange rates and aid growth and development. The continued improvement in budget management systems, the development of medium-term expenditure frameworks, accountability, transparency and institutional capabilities for budget management and governance will also work towards strengthening authorities' ability to face challenges in the fiscal environment as they arise.

Over the next one and a half days, these issues will be discussed and debated at great length. It is my hope that this forum provides participants with the opportunity to share experiences, ideas and build relationships that will only benefit the development of fiscal institutions and capacity in governments to deal with fiscal challenges that arise in future.

In closing I would like to thank US AID for the funding they have provided in order for National Treasury and the IMF to host these important discussions. In addition, thank you to the team of people from the fiscal policy unit in the Budget Office of the National Treasury, the Fiscal Affairs Department and Africa Department of the IMF and the staff from CABRI for all their hard work and efforts in pulling this event together. All the best for the forum and I hope that this will be the first of many forums of this nature to take place on the continent.