

# **TITLE: The Situation of Poor Countries after the World Financial Crisis:**

The Case of Ethiopia and Kenya

By

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# Presentation Outline

*The objective of this presentation is to examine*

- *The Situation of poor countries after the world financial crisis, country examples are Ethiopia and Kenya*
- *Description of specific situations of hardship: Examples from daily life of the people and problems for the government*
- *Reasons why situations in these two countries is harder now than it was before the crisis*
- *What the state of implementation of the MDGs is in Ethiopia and Kenya. What is needed there*

# INTRODUCTION

What exactly went wrong?

- The world economy has changed dramatically since September 2008
- What began as a down turn in the US housing sector became a global crisis spreading to both rich and poor economies
- Many believe that this may go down in history as the “worst crisis since the Great Depression of the 1930s”.

Harvest Fast Day 2 October 2009

The financial crisis is **crippling the world's poorest people.**

Time is running out.





Just two years ago, Margaret, from Mathare in Nairobi, Kenya, had a job as a supervisor at a food production company making ice cream and sweets. "I'd worked my way up from the bottom and was earning a good living."



Then her world began to fall apart. Firstly, she was one of 60 redundancies. "The economy was not doing well and factories closed down. They offered us nothing. They didn't even tell us, they just closed the doors."



Weeks later, violence ripped through the streets as hopes of a fair election were torn apart. **In the chaos, Margaret's house was burned to the ground.** With no job and no money, she had to move into a slum area.



Now, although employed as a teacher, Margaret earns next to nothing and is never sure where the next meal will come from. Food prices are out of control, making even basics such as bread too expensive for many.





Margaret says every day is a struggle but her extraordinary courage shines through. "I'm determined. I can walk for any length of time just to find something for my kids. The tougher it gets, the harder I'll work. What do I do, just cry? No, I'll work harder, with God's help."





Around the world, in poor countries, millions just like Margaret are struggling to keep their heads above water. Having spent years working their way out of poverty, they are now being knocked down again by events beyond their control.

# Should Africa , particularly Ethiopia and Kenya Care? Why and How Much?

## Africa in General

On the whole, as would be expected, there were different strands of opinions regarding the likely effects of the financial/economic crisis on Africa but there is consensus on the following:

- 1) Because of Africa's generally **weak financial integration** with the rest of the global economic system, it was believed that the financial sectors of many African countries (except slightly that of South Africa and few countries) would not be directly affected by the crisis

# Africa in General

- *It is argued that, in general, African banking sectors are insulated from foreign finance.*
- *The sectors rely on domestic deposits and lending and does not have derivatives or asset-based securities among their portfolio.*
- *Even though some banks have significant foreign ownership, the parent banks are typically not from the US and the foreign ownership share relatively small – 5% compared to 46% for developing countries.*

# Africa in General

- 2) The economic Effects that were likely to follow (if and when they did) were going to be severe because of the **vulnerability** of African Economies to even minor external shocks.
- 3) The shock to which they were to be transmitted to African Economies is not through the credit crunch and lack of liquidity as observed in advanced countries and emerging economies but through the recession that follows the crisis

# Africa in General

According to the World Bank Chief Economist, Shanta Devarajan, the channels through which the crisis would have an adverse impact on African Economies as recession in developed countries spread would be indirect, which include

- 1) “A slow down in ***private capital flows*** adversely affecting economies that had been relying on these flows to finance much needed investment, particularly infrastructure investment. Already Ghana and Kenya postponed sovereign bond issues worth about \$800 million” he said

# Africa in General

- 2) **Commodity prices** are falling which (because of and as a consequence) hurts exporters and helps importers. He also adds, “Commodity dependent economies are exposed to considerable external shocks stemming from price booms and bursts in international commodity markets”
- 3) **Remittances**, which run about \$15 Billion a year to Africa are likely to decline
- 4) **Foreign Aid**, is likely to be down graded

# Africa in General

**5) *Tourist revenues*** are likely to substantially decline as recession in developed countries deepens

Consequently, as is the case for developed countries, the world bank downgraded the growth prospects of Africa from 7.9% to 0.1% for 2008 and from 6.9% to -1.1% for 2009.



# How adversely did it affect Ethiopia?

**Indirect economic effects:** It affected Ethiopia for the following reasons:

- About one third of the government **budget is donor dependent**
- Ethiopia's **export** declined both in volume and value. As recession spread around the developed economies and the emerging ones, it was expected the **demand for exports** would decrease.
- **Remittances** declined
- **Tourism revenue** had been on the increase, the country got less as the recession deepened

# Ethiopia (Continued)

- For Example, the world price of coffee decreased by a significant margin (about 25 -30%) while volume also decreased by about 5% in October 2009.
- Similarly, according to the 2009 budget, grants were about 28.4 % of total federal government revenue or 4.5% of GDP. Therefore, even a slight decrease in donor support could lead to a sizeable decline in Revenue in Ethiopia. In particular, external loans are about 14% of the total capital expenditure which could constraint completion of Capital projects underway (the electric dams in progress, for instance)

# Ethiopia (Continued)

- Further, according to June 2008 investment figures, 53.1% of the total capital flows was of foreign origin. Hence a decrease in investment activity due to recession abroad has affected both FDI and hence, unemployment, and
- Finally, **remittances** and to a lesser extent **tourism** were becoming an important source of foreign exchange. According to the National Bank of Ethiopia report, remittances from abroad were about \$1 million last year. Both are threatened by the present downturn.

# Ethiopia (Continued)

- Therefore, all the above suggest that even though financial crisis did not affect Ethiopia directly (thanks for its lack of integration to the world) its indirect impact through the channels stated above and others has been unmistakable.
- What we do not know for sure is the exact magnitude and the time frame of the impact.

# Impact of Global Crisis on Kenyan Economy

- The impact on Kenya is both direct and indirect exposure

## ***Direct Effects: Capital Market***

- *Portfolio flows have however adversely affected the stock market, with foreign sales exceeding foreign buys in many counters, as foreign portfolio investors diversify from the market (Kibaara, 2008).*
- *The NSE 20-share index has taken a hit since mid-2008 on the back of the post-election violence and the **global financial crisis**.*
- *In 2008, the NSE-20 index slumped by 35%, 25% since July 2008*

# Impact of Global Crisis on Kenyan Economy

- Indirect effects include **slowdown of the tourism** sector that relies heavily on foreign tourists, **the construction industry** and the **stock market** that benefit from remittances by Kenyans living abroad and foreign institutions e.g. hedge funds
- **Exports**, especially horticulture, lower which impact on foreign exchange earning .

# Impact on Kenya

- Strengthening of US Dollar against other currencies has resulted in **depreciating Kenya Shilling**
- **Foreign Debt Service** is more expensive (more Kshs to pay)
- Implies that **imports** will be more expensive-
- Diaspora **remittances** remains relatively low

# Impact of Global Crisis on Kenyan Economy

- **Falling oil prices** likely to result in lower fuel and energy costs (subject to strength of the Kenya Shilling)
- **Reduced direct investment** in Kenya by developed countries due to foreign investors focus on consolidating their financial position



# Impact on Kenya

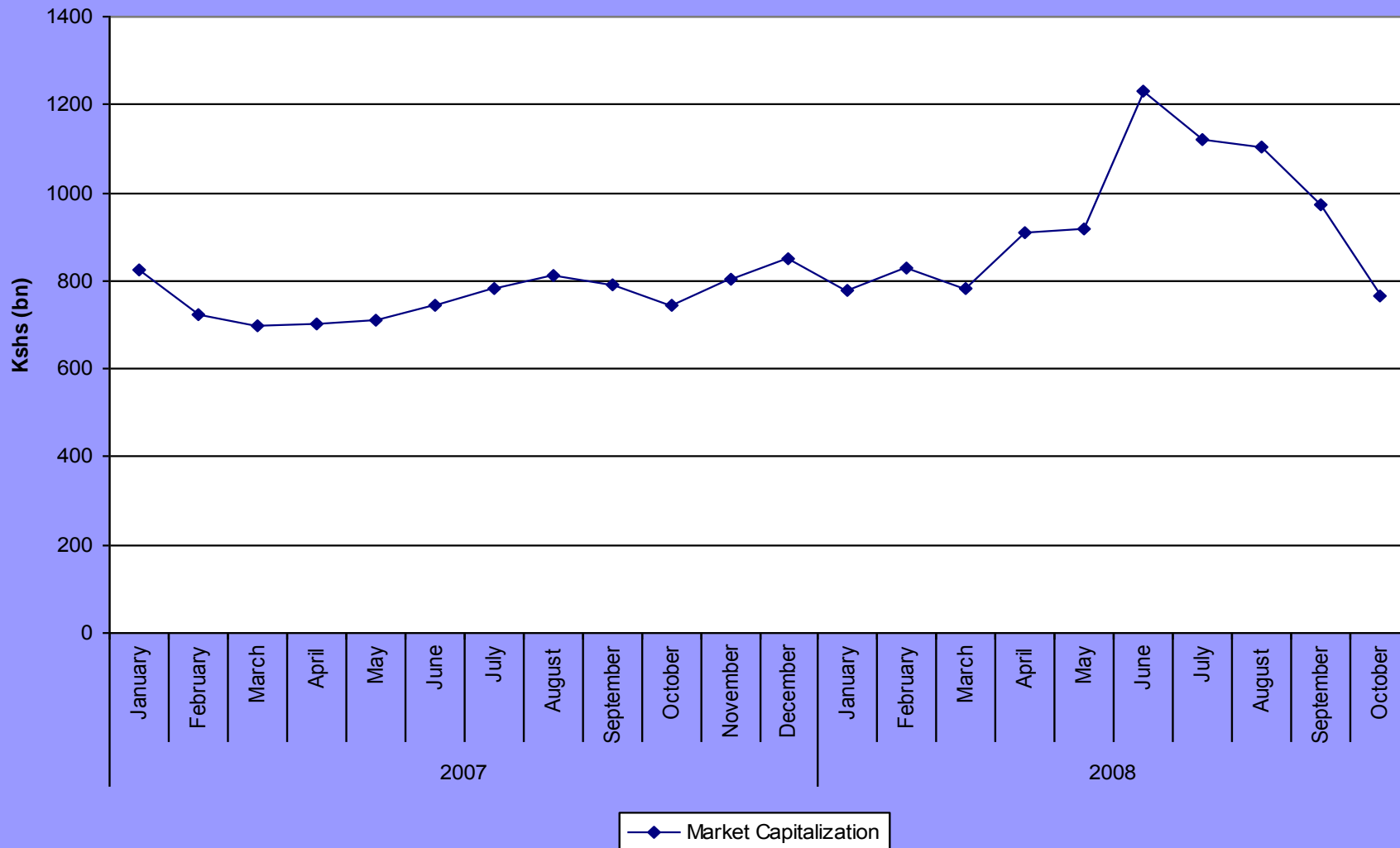
## NSE Market Capitalization Trends 2007

<b>Year</b>	<b>Month</b>	<b>Market Capitalization (Kshs bn)</b>
<b>2007</b>	<b>January</b>	<b>824.3</b>
	<b>February</b>	<b>723.7</b>
	<b>March</b>	<b>697.3</b>
	<b>April</b>	<b>702</b>
	<b>May</b>	<b>709.7</b>
	<b>June</b>	<b>743.9</b>
	<b>July</b>	<b>780.7</b>
	<b>August</b>	<b>813.2</b>
	<b>September</b>	<b>791.7</b>
	<b>October</b>	<b>745.5</b>
	<b>November</b>	<b>804.1</b>
	<b>December</b>	<b>851.1</b>

## NSE Market Capitalization Trends 2008

<b>Year</b>	<b>Month</b>	<b>Market Capitalization (Kshs bn)</b>
<b>2008</b>	<b>January</b>	<b>777.1</b>
	<b>February</b>	<b>830.6</b>
	<b>March</b>	<b>781.7</b>
	<b>April</b>	<b>908.2</b>
	<b>May</b>	<b>916.8</b>
	<b>June</b>	<b>1230.7</b>
	<b>July</b>	<b>1122.2</b>
	<b>August</b>	<b>1102</b>
	<b>September</b>	<b>972.27</b>
	<b>October</b>	<b>764.98</b>

Trends in NSE Market Capitalization for period covering Jan 2007-Oct 2008

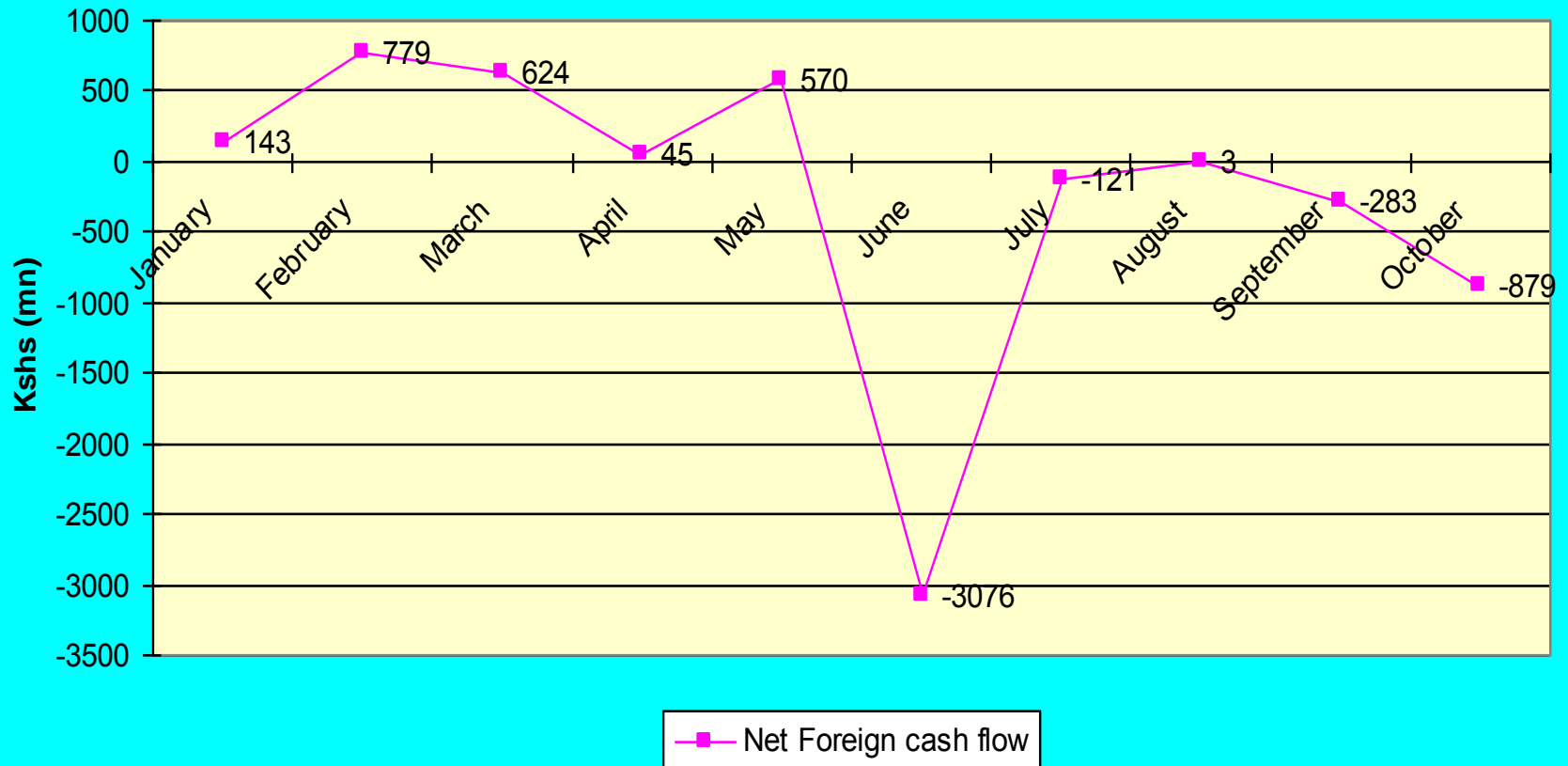


# Impact on Kenya

<b>2008</b>	<b>Foreign Investors (Net Outflow Kshs Mn)</b>
<b>January</b>	<b>143</b>
<b>February</b>	<b>779</b>
<b>March</b>	<b>624</b>
<b>April</b>	<b>45</b>
<b>May</b>	<b>570</b>
<b>June</b>	<b>-3076</b>
<b>July</b>	<b>-121</b>
<b>August</b>	<b>3</b>
<b>September</b>	<b>-283</b>
<b>October</b>	<b>-879</b>

# Impact on Kenya

## Net Foreign cash flow activity for the period March-October 2008



# Impact on Growth

- *All these effects have adversely affected the **Kenya** growth rate.*
- *In 2007, the country experienced a growth rate of 7%, the highest growth in over two decades.*
- *In 2008, the growth was expected to be 4% (IMF) due to the post-election violence in the first quarter of the year, drought and the **global financial crisis**.*
- *In 2009, growth is expected to be about 3% (AIG).*

# Policy Issues

- *Kenya has set up a Task Force to look into ways of cushioning Kenya's economy from the effects of the **global financial crisis**.*
- *It is comprised of officials of the ministry of finance and planning as well as the central bank.*

# ***Some suggested solutions:***

- Lower interest rates. CBK has already lowered the cash ratio from 6% to 5% and the Central Bank Rate from 9% to 8.5% , although some contend these actions are not enough to significantly reduce interest rates.*
- Expand Expenditures e.g. acquisition of shares by the government or its agencies to shore the stock market*
- Facilitate and lower the cost of remittance costs which are currently quite high.*
- Etc*



# Millennium Development Goals

1. Eradication of Extreme Poverty and Hunger
2. Universal Education
3. Gender Equality
4. Child Health
5. Maternal Health
6. Combat HIV/AIDS
7. Environmental Sustainability
8. Global Partnership

# Millennium Development Goals

- According to UNDP, mixed progress within regions demonstrates that MDG progress is country specific. Sub-Saharan Africa, for example, has seen volatile fluctuations in poverty: falling in Ghana between 1999 and 2006, but increasing in Uganda between 2000 and 2003, despite comparable GDP growth.
- Performance varies even among fragile states: poverty has fallen in Ethiopia and Cambodia, but risen in Niger, Nigeria and Zimbabwe. The mixed performance on MDGs reflects a complex combination of specific country contexts.

# Millennium Development Goals

## MDGs and the global economy

- The global economy can support achievement of MDGs by facilitating economic growth in particular countries, but the extent to which this reduces poverty depends on context.
- In Ethiopia, two dimensions of Poverty identified: Income and non-income; Trends in rural and urban poverty
- According to UNDP the decline in rural poverty is substantial, key objective of the government is food self sufficiency

# Implementing MDGs

## A Development Emergency

- "In Africa, where most people are self-employed, unemployment takes on the face of a woman who grows vegetables for market and finds that people are no longer buying them," said Joy Phumaphi, Vice President, Human Development, at the World Bank.
- "This woman is forced to make difficult choices—to pull her children out of school, to wait until a child is very sick before going to the clinic, to feed her family a poor-quality diet without the meat or vegetables they need."
- While individual families struggle with increased needs and shrinking incomes, the financial crisis is also deeply affecting the capacity of low-income country governments to meet public needs in critical areas.

# Millennium Development Goals

## Achieve Universal primary Education

### What has worked

- Burundi, DRC, **Ethiopia**, Ghana, **Kenya**, Malawi, Mozambique, Tanzania and Uganda have abolished school fees which has led to a surge of enrolment, e.g. In Kenya 1.2 million additional pupils in 2003, by 2004 climbed to 7.2 Million of which 84% were of primary school age. Challenges in providing sufficient school building and teachers

# Millennium Development Goals

## Achieve Universal primary Education

- Although aid directed to basic education for low income countries increased from \$1.6 billion in 1999 to 5 Billion in 2006, it is still well below the estimated \$11 billion in aid required annually to reach universal primary education by 2015.
- The aid was further affected by the Global financial crisis. For example, in both Kenya and Ethiopia the budget had to be adjusted given the reduction in government revenue.

# **Kenyan Ministry of Education delegation impressed with Sauri's school meals program**

- It is possible! That was the key message from Margaret Ndanyi, the Director of the school health, nutrition and meals Unit at the Kenya Ministry of Education, after touring schools in the Sauri Millennium Villages Project (MVP). She was there to experience firsthand the School Health, Nutrition and Meals programs supported by the Project in the Gem District of Nyanza Province, Western Kenya. Mrs. Ndanyi was part of a delegation of senior Ministry officials on a learning visit to projects such as the MVP, before they finalize the Ministry's draft national strategy on school health, nutrition and meals

# Millennium Development Goals

## Achieve Universal primary Education

- In Ethiopia, (UNDP report) during 2007/2008 total primary enrolment reached 15, 341,121 pupils which brought up the Gross Enrolment ratio (GER) to 96.7% from its level of 91.6% in 2006/2007.
- During the same period 1,992 primary schools have been constructed which brought total number of primary schools in the country to 23,235. Progress supplemented by the fact that 80% of the constructed schools are located in rural areas and with improved awareness of the community towards girl education.



# Improving aid effectiveness to reach the MDGs

- Aid effectiveness is at the centre of the aid debate. The 2005 Paris conference aimed to resolve problems around aid effectiveness, but results are limited.
- The priority is to improve, and demonstrate, the effectiveness of aid. Firstly, it is known that channeling aid to projects in poor countries make little sense in some circumstances, and that aid is better channeled as budget support.
- Nevertheless, aid continues to go to projects (increasingly MDG-related). The question arises: “If we do not trust this government enough to give it budget support, why would project finance produce the intended results?”

# Improving aid effectiveness to reach the MDGs

- Finally, there has been little progress on results-based aid, with disbursements linked to progress on targets agreed in advance. While results take time to materialize, recipient countries need aid money to launch programmes.
- The result-based aid contract should start by giving governments the benefit of the doubt, before aid becomes conditioned on a set of indicators, while policy choices should be left to recipient country governments.
- Steps in this direction include the Poverty Reduction Strategy (PRSP) process, and the European Commission programmes whereby aid disbursement includes fixed and variable components, the latter linked to progress towards specific targets.

# NEW PARTNERSHIP FOR AFRICA DEVELOPMENT (NEPAD)

- The Government of Kenya is committed to the principles of the NEPAD and has already appointed a focal point within the Ministry of Finance and Planning to focus specifically on NEPAD. As a result of high-level lobbying, Kenya is beginning to play a bigger role in the NEPAD in the sub-region in promoting its principles.
- There is also a possibility that Kenya's role might even be bigger, perhaps at the highest level not excluding the steering committee. The location of NEPAD in the Economic Planning Division in the Ministry of Finance and Planning demonstrates its commitment to integrate the Government's priorities into NEPAD, particularly in linking NEPAD to the national planning process (PRSP) as well as with other global commitments such as the MDGs which are getting integrated in the same way.

# Conclusions

- *We need more policy coherence, not more goals*
- *Donors must deliver on promises*
- *Policies within developing countries are crucial*
- *Social protection and insurance need more support*
- *Fragile states need a special agenda*
- *We need to look beyond 2015*
- *The European Union has a special role*

- ***THANK YOU FOR LISTENING***