Policy Brief

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The Economic Implications of the War in Ukraine for Africa and Morocco

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The Russian-Ukrainian war will have major economic and political repercussions for years to come. In this note, we focus on the war's economic short and long term implications on the African economy. The conflict comes as Africa is still struggling to set its economy on the recovery path, amid global inflationary pressures and volatile financial and commodity markets. While energy exporters will gain from the crisis, others such as Morocco, will be hit hard by soaring energy and food prices. This will add to their external imbalances, and concerns about rising prices and the path of public debt.

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Russia's full-scale invasion of Ukraine on February 24 will have major political and economic repercussions on the rest of the world that will be felt over months and years to come. This note focuses narrowly on the war's economic implications for the 54 countries and 1 billion people of Africa. We devote special attention to Morocco, a lower-middle-income nation that imports over 90% of its energy and half its cereals, and which is among the African nations most exposed to the crisis.

We make the following main points:

- The Russia-Ukraine war is a major event, perhaps the most dangerous international incident since the Cuban missile crisis.
- Its impact is difficult to predict, especially since it comes at a time when the global economy is still in the grip of a pandemic and in the midst of inflationary pressures, which are likely to intensify, especially if the conflict is protracted.
- Even before the crisis, Africa's economic prospects were not propitious. However, the implications of the war for Africa are mixed; while energy exporters will see big gains, energy and food importers such as Morocco will be hurt, adding to their external imbalances and concerns about the size of public debt.

THE ECONOMIC SITUATION AT THE OUTSET OF THE CONFLICT

A conflict between Russia and Ukraine, ranked respectively as the world's 13th and 61st largest economies by GDP, and the world's breadbasket, never comes at a good time. However, the present conjuncture is especially arduous. The global economy is still in the middle of a fourth pandemic wave, and only 11% of Africans are fully vaccinated. Though the world economy is in the second year of recovery and is projected by the World Bank's Global Economic Prospects to grow by 4.4% in 2022, uncertainty remains high because of the pandemic, a surge in prices (as median inflation has increased from 2.2% pre-pandemic to 3%), and the prospect of higher interest rates. In the United States, the world's financial center, prices rose by 7.5% in January 2022 year-on-year, and the Federal Reserve Bank is expected to execute several hikes in its policy interest rate in 2022 and 2023.

Even before the invasion, Africa's economic prospects were not propitious. Africa is still very exposed to the pandemic, and, according to the World Bank (2022), per-capita income in most African countries will remain below pre-pandemic levels at least into 2023. Median inflation was reported at 5.1% y-o-y in late 2021. Africa—especially North Africa—is especially badly affected by high food prices, as food accounts for nearly 40% of the household budget in many countries. Poverty levels—measured at $1.90 a day—have increased from 34% before the pandemic to 39% (African Economic Outlook, 2021). The 43 African countries that are energy importers, according to African Development Bank classification, also suffer indirectly from high coal, gas, and oil prices, since they raise the costs of producing fertilizers and food, both highly energy intensive.

THE IMPACT OF THE WAR ON WORLD TRADE

The two protagonists in the conflict are not systemically determinant powers in the global economy, but they play central roles in specific commodities. With a population of 144 million, the Russian Federation accounts for about 2% of world GDP, about the size of the Belgian and Dutch economies together. Its integration into global value chains (GVC) is limited and consists mainly of providing raw materials in the form of fossil fuels, cereals, and fertilizers. Russia's exports rely only to a very limited extent on foreign inputs. For example, while 24% of Spain's exports consist of foreign inputs, only 9% do in the case of Russia.

The Ukrainian economy, although more diversified than Russia's, is far smaller, accounting only for 0.2% of global output. However, Ukraine plays a critical role in the international food market, supplying 6% of the world's cereal exports, and 10% of vegetable oil and oil seed exports. The share is even more important for wheat, reaching 10% of global exports, and sunflower oil, at 50% of world exports. The Donetsk and Luhansk regions, where military operations are especially intense, are the source of 8% of Ukrainian wheat production and 9% of sunflower seed (IFPRI, 2022). Other important areas of production border Belarus and Russia, from where military attacks have been launched. The harvest season is in summer, and exports occur in the fall. However, disruption of Ukraine's supply capacity and transportation routes over the course of the conflict and beyond it is bound to have a significant immediate effect on the price of these commodities.

Russia and Ukraine together are major players in the energy, food and fertilizers industries (Table 1). Russia plays a central role in energy markets; its exports account for around 11% and 9% of global petroleum and gas imports respectively[1]. Russia accounts for 5% of global cereals imports and 24% of wheat. Russian sunflower oil exports are also critical for the global market, as they represent 23% of world imports of that product. Russia is also the world's largest supplier of fertilizers, accounting for 12.5% of the world imports of manufactured fertilizers and is one of the largest supplier of metals such as palladium, nickel, and aluminum.

Table 1:

Main Ukrainian and Russian exports and their shares of global trade

TOP 10 UKRAINIAN EXPORTS	SHARE OF GLOBAL IMPORTS (%)	SHARE OF UKRAINIAN EXPORTS (%)	TOP 10 RUSSIAN EXPORTS (%)	SHARE OF GLOBAL IMPORTS (%)	SHARE OF RUSSIAN EXPORTS (%)
Vegetable oils	6.7	9.3	UN Special code*	14.2	13.0
Cereals	6.0	20.0	Manufactured fertilizers	12.5	2.0
Oil and fruit seeds	3.1	5.0	Coal/coke/ briquettes	11.6	4.0
Iron and steel	2.3	18.8	Petroleum and products	10.9	45.5
Animal feed	1.8	3.0	Gas Natural &manufactured	8.7	6.8
Metal ores/ metal scrap	1.1	8.3	Cork and wood	8.4	1.5

1. Numbers can differ from other sources following the trade nomenclature used.

Meat & preparations	0.5	1.4	Non-ferrous metals	5.3	4.4
Railway & tramway equipment	0.2	1.5	Cereals	5.2	2.0
Electrical equipments	0.1	4.8	Iron and steel	4.7	4.5
Industrial equipments	0.1	1.4			
			Metal ores/ metal scrap	1.7	1.5
Total exports by country in billions of $		**50.1**			**426.7**

Source: WITS

*Mainly arms

OTHER EFFECTS ON THE GLOBAL ECONOMY

The sanctions on Russia declared so far are not of a kind to cripple the Russian economy. They do not, for example, envisage – at this stage at least - preventing completely the use of SWIFT to make bank transfers, and nor do the sanctions include stopping imports of oil, gas, cereals, and aluminum from Russia, simply because such measures are more likely to hurt Western consumers—especially Europeans—rather than Russia, which has low debt and large foreign currency reserves. Russia can also divert many of these exports towards China, with which it has increasingly close ties. The suspension of certification of the Russian gas pipeline to Germany, NordStream2, which is complete but not yet operational, and the announcement of sanctions against its shareholders by the United States, could reduce Europe's expected gas supply by 10%-15%. This means that gas could remain in short supply in Europe in coming years, requiring a search for alternative sources of gas and of energy, raising prices.

Even though the Russian economy will suffer a hit from the war, including sanctions on some of its banks and individuals, and the large devaluation of the ruble that will hurt the purchasing power of Russians, and even if the war devastates the Ukrainian economy, the direct effects on world GDP will be small because of the economies' modest shares of world output. This is especially the case if the conflict is of short duration, as many expect in view of Russia's overwhelming military advantage.

The main effects of the war are already evident in the volatility in financial and commodity markets and will be seen in weeks and months to come in inflation aggregates, complicating the calculus of central banks already bent on tightening monetary policy. Over the last fortnight or so, as the perceived risk of invasion increased, and was then confirmed, oil prices increased from $88per barrel to $98/barrel, and wheat prices increased from 759 US cents per bushel to 878 US cents per bushel. Over the same period, stock values markets in Europe and the U.S. have declined by 8% and 5.7% respectively. The yield on the 10-year U.S. Treasury bond increased by 18 basis points, and the price of the largest high-yield bond exchange-traded funds (ETF), such as HYG[2], has lost 2.1% of its value since February 1. However, equity indexes have rallied in recent sessions, in part because announced sanctions on Russia were less severe than expected.

Figure 1:

Wheat and Brent prices evolution in 2022

Source: Wall Street Journal

The increased uncertainty will affect consumer and investment demand across the world. A useful measure in this regard is the economic policy uncertainty index[3] for the United States. It has shown a significant increase since early December 2021, coinciding with rising tensions in Ukraine and massing of Russian troops on its borders. The climate of uncertainty will be aggravated by the effect on inflation aggregates of higher oil and food prices. For example, analysts have predicted that the effect might be to raise consumer inflation by 1%-1.5%. Loss of confidence and higher energy prices point to slower growth. Oxford Economics, for example, estimates that global GDP will slow by about 0.2% in 2022 relative to the previous baseline, with Europe seeing a deceleration of around 0.4% which will persist over the next two years. Russia will be the most affected, though the impact will be moderate—a deceleration in the region of 1% over the next two years. Central Banks will have to factor into decisions to raise interest rates both this higher inflation and the increased risk of a sharp slowdown due to the uncertain environment. Higher inflation increases the probability of a hard landing of the global economy, and even of a prolonged economic slowdown as policy interest rates are raised.

2. HYG is one of the most widely used high-yield bond ETFs (Blomberg).

3. The indicator is available on a daily basis but released every week. it reflects the frequency of articles in 10 leading US newspapers that contain the specific words. the index spikes near tight presidential elections, Gulf Wars I and II, the 9/11 attacks, the 2011 debt-ceiling dispute

THE EFFECTS ON AFRICA

Of Africa's 54 countries, 11 are large energy exporters and the rest are net energy importers, or in approximate self-sufficiency. To illustrate the effects of the war on Africa, we focus on six large economies. Three are energy exporters: Algeria, Angola, and Nigeria. Two are close to self-sufficient in energy: Egypt, and South Africa. And Morocco is heavily dependent on imported energy and food. These six economies together account for over 60% of African GDP.

The oil exporters will see big gains from the rise in oil and gas prices of recent weeks, since Algeria's oil exports amount to 18.9% of GDP, Angola's 36.5%, and Nigeria's 10.3%. For example, a 20% to 30% increase in the price of oil and gas, in line with what was seen in recent months, if sustained, will add about 4% to 6% to Algeria's national income. Though these countries are also dependent on food imports to a differing degree (Nigeria is the least dependent), the additional cost of higher food prices would be dwarfed by their gains on energy exports.

The effects of the war on African energy importers, which also tend to be food importers, is strongly negative. Morocco is the largest African economy most likely to suffer a big adverse shock from the war since Morocco's imports of oil, gas, and coal equaled 6.4% of GDP in 2019, about twice the shares of Egypt and South Africa, which also have significant energy exports. Morocco is also a large importer of cereals. The cost of imported cereals as a share of GDP was 1.4% in 2019, but because of an expected bad harvest in 2022, imports could be 50% larger, or three times larger than 2021's imports. This means that the combined effect of higher oil and cereal prices could cost Morocco between 1% and 2% of national income this year, if sustained.

Besides the impact on Morocco's external balance, the surge in oil and food prices will add to the high budget deficit, estimated at 6.5% of GDP this year, since cooking gas is subsidized. Rising prices will also intensify inflationary pressures, as in the case of gasoline and other fuels where prices are liberalized. With trade unions pressing authorities to adjust wages to compensate for higher prices, inflation appears set to be higher still.

Most African energy importers are poor and less industrialized economies, with large agricultural sectors. They are not as dependent on imports of energy and cereals as Morocco, but they have less fiscal space to react, and a bigger proportion of their population is close to poverty thresholds, and even more exposed to food price shocks, than in Morocco.

It is important to note that, depending on the extent and duration of sanctions against Russia, and Russia's response, Africa could see new export opportunities in Europe (its most important market) and Russia, displacing European exports to Russia and Russian exports to Europe. Among the sectors which could be so affected are fruits and vegetables and fish in Russia, and fertilizers in Europe. For example, Morocco's exports of fertilizers, amounting to 4.5% of GDP in 2019, compete with Russia's on European markets, while Morocco's exports of fruits and vegetables and fish, which account for 2.6% of Morocco's GDP, compete with Europe's exports in Russia. Another example is South Africa, for which exports of fruits and vegetables constitute 1.1% of GDP.

The effects of the war at the sectoral level on Africa, which are negative for most countries, will likely be augmented by the effect of deteriorating macroeconomic conditions. Higher oil prices and international policy interest rates to fight inflation, widening spreads on risk assets as uncertainty persists, and slowing of the European economy, will spill over onto Africa. Those African countries that have access to international markets could see their borrowing costs increase by 1% or 2%. This should not cause a problem for countries with small external debts and manageable current account deficits, with Morocco among them. However, many countries in Africa—especially those that rely on official finance—have reached high levels of external debt in the wake of the pandemic and are now especially exposed.

Policymakers across the world are monitoring developments closely. Now that the invasion has been launched, one can only hope that the war will be as short and as bloodless as possible. In any scenario, a regime of sanctions against Russia, and retaliatory measures by Russia, are likely to persist for years to come. Energy and food importers in Africa will remain exposed to the crosswinds.

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The Policy Center for the New South: A public good for strengthening public policy. The Policy Center for the New South (PCNS) is a Moroccan think tank tasked with the mission of contributing to the improvement of international, economic and social public policies that challenge Morocco and Africa as integral parts of the Global South.

The PCNS advocates the concept of an open, responsible and proactive « new South »; a South that defines its own narratives, as well as the mental maps around the Mediterranean and South Atlantic basins, within the framework of an open relationship with the rest of the world. Through its work, the think tank aims to support the development of public policies in Africa and to give experts from the South a voice in the geopolitical developments that concern them. This positioning, based on dialogue and partnerships, consists in cultivating African expertise and excellence, capable of contributing to the diagnosis and solutions to African challenges.

The views expressed in this publication are those of the author.

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