



Embracing Impact

How Africa Can Overcome the Emerging Market Downturn

APRIL 2016 J. PETER PHAM AND AUBREY HRUBY

In January 2016, oil prices fell to their lowest levels in more than a decade. Meanwhile, China, the world's second-largest economy, is experiencing its most sluggish growth in a quarter century—compounding the downward trend in commodity prices and dampening the global economic outlook. The effects of this broad slowdown will hurt African economies more than most, because China and other emerging markets have not only been primary consumers of African commodities, but also have been significant sources of financing for the major infrastructure and other development projects that are essential to Africa's future growth.

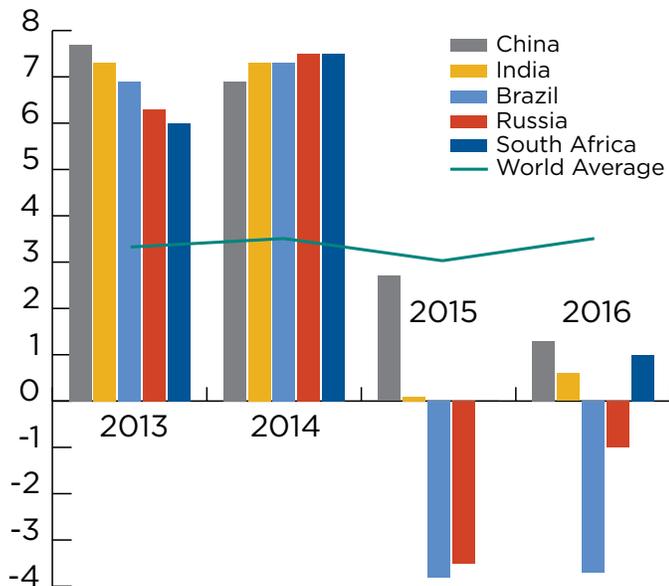
Growth projections, and degrees of optimism, vary greatly across a complex continent. But it is possible to make some generalizations about which countries will emerge unscathed—or even, better off—after the emerging market downturn passes, and which countries must act quickly and decisively to alter their negative economic course.

North Africa is projected to experience steady growth over the next five years, and standout performers like Morocco will do especially well, while for others, like Libya, given the general political uncertainty and insecurity in the country, the future is less rosy. East Africa is also set to perform well overall, and the International Monetary Fund (IMF) projects that Kenya, Ethiopia, Rwanda, and Tanzania will each grow at more than 6.5 percent in 2016, a full 3 percent over the continental average. West Africa is a mixed bag, as Nigeria struggles with falling commodity prices and corruption scandals, while Côte d'Ivoire and Senegal are widely considered some of the best prospects for investing in Africa.¹ In southern Africa, low economic growth and governance

The **Africa Center** promotes dynamic geopolitical partnerships with African states and redirects US and European policy priorities towards strengthening security and promoting economic growth and prosperity on the continent.

¹ "Africa's Prospects," Nielsen, February 2, 2016, http://www.nielsen.com/content/dam/nielsen-global/ssa/docs/reports/2016/9573_Africa_Prospects_Report_DIGITAL_FINAL.pdf, p. 2.

Figure 1. Annual Real Gross Domestic Product (GDP) Growth, 2013-16 (in percentage)



Source: IMF World Economic Outlook, October 2015.

woes in the region's powerhouse, South Africa, will continue to drag down the region's overall economic outlook.

Snapshot of Emerging Market Troubles

Commodity prices have decreased dramatically since the latter half of 2015. Oil, iron ore, copper, and platinum have been especially hard hit. This commodity price crash is causing significant budget shortfalls for governments and weakening of currencies in commodity-exporting economies worldwide. Currency pressure in oil-exporting nations has been most pronounced—and not just in Africa.²

Despite some progress on export diversification, the majority of African countries remain dependent on commodities, particularly extractives like oil, iron ore, and copper, for their economic growth.³ In Angola, for example, oil made up 94 percent of exports in 2013, while in Nigeria, it made up 79.4 percent.⁴ In Zambia,

copper made up 68.3 percent of exports.⁵ All these commodities are currently experiencing rapid price declines, and many have reached their lowest prices since the 2008 global financial crisis, if not before. (For example, Brent crude, which serves as a benchmark for oil trading worldwide, hit its lowest point in more than ten years when it traded below \$30 a barrel in January 2016.)⁶

Gold and non-extractive commodities, such as cocoa and coffee remain stable by comparison, and thus countries reliant on these products—including Ghana, Côte d'Ivoire, and Ethiopia—have been less vulnerable to price shocks, though significant dependency on any one or two products remains problematic. Countries that are not reliant on commodities at all are better off in the current market conditions than their commodity-dependent counterparts. Some diversified economies may even experience benefits in, and more rapid recovery from, the global downturn.

The downturn in commodity prices has been aggravated by economic troubles in China, which in 2015 experienced its slowest growth in a quarter century. According to the IMF, the country's gross domestic product (GDP) grew 6.9 percent last year, down from 7.3 percent in 2014. It is expected to shrink further to 6.3 percent in 2016. China's slowdown has led to declining Chinese demand, coinciding with, and contributing to, the decrease in commodity prices.

China shopped voraciously for the world's commodities during its years of rapid economic expansion, and its woes are spilling over into other markets that were already struggling with plummeting export values. China's contraction is most evident in its manufacturing, construction, and real estate sectors; economists believe that it is a result of the country's bumpy transition from an export-oriented economy to a consumer-led one.⁷ But concerns over massive Chinese debt and the country's volatile stock markets compound investor fears; in March 2016, Moody's downgraded China's credit rating outlook to negative.

2 "Pegs Under Pressure," *Economist*, October 17, 2015, <http://www.economist.com/news/finance-and-economics/21674775-currency-pegs-are-still-fashion-some-are-creaking-pegs-under-pressure>.

3 Alexandra Laurent, "State of Commodity Dependence," UN Conference on Trade and Development, 2014, p. 25

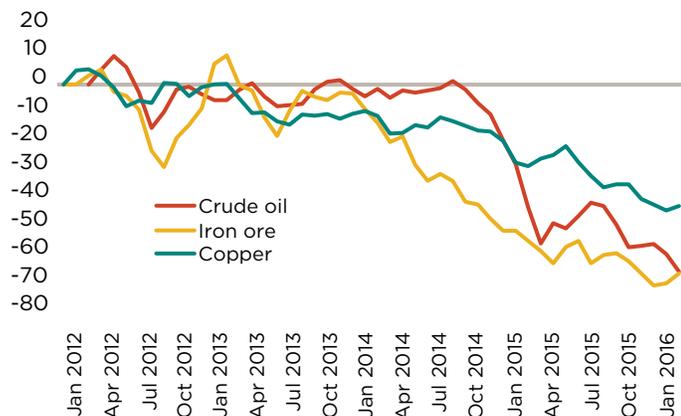
4 The Observatory of Economic Complexity, <http://atlas.media.mit.edu/en/>; Angola: <http://atlas.media.mit.edu/en/profile/country/ago/>; Nigeria: <http://atlas.media.mit.edu/en/profile/country/nga/>.

5 The Observatory of Economic Complexity, op. cit., <http://atlas.media.mit.edu/en/profile/country/zmb/>.

6 "Crude Oil Brent," Nasdaq, <http://www.nasdaq.com/markets/crude-oil-brent.aspx?timeframe=10y>.

7 World Bank, "Global Economic Prospects," January 2016, <http://www.worldbank.org/content/dam/Worldbank/GEP/GEP2016a/Global-Economic-Prospects-January-2016-Spillovers-amid-weak-growth.pdf> p.11

Figure 2. Commodity Price Changes since January 2012 (in percentage)



Source: World Bank.

Given increasing alignment between business cycles in developing countries, it is more likely that Brazil, China, India, Indonesia, and others will experience booms and recessions simultaneously. African business cycles, historically divergent, are also rapidly aligning with those of the larger developing markets, intensifying the effect of the downturn.

Slowing Chinese growth, in particular, will have an especially negative effect on African economies. China is the continent's largest trading partner, making up 13 percent of Africa's total exports. But export dependence on China varies considerably across nations, ranging from 80 percent in Sierra Leone, to 40 percent in the Democratic Republic of the Congo (DRC), to 1 percent in Kenya.⁸

Though Chinese foreign direct investment (FDI) in Africa is relatively low,⁹ Chinese concessionary and commodity-backed lending supports tens of billions of dollars of badly-needed infrastructure projects across the continent. These projects range from a \$12 billion coastal railway in Nigeria (China's largest overseas contract) to mining development projects worth \$7 billion in the DRC.¹⁰ As China's growth slackens, its

interest in and ability to finance African projects—and especially valuable infrastructure—will necessarily slow, causing African governments to have to rethink their infrastructure development plans.

According to the five-year plan approved by the National People's Congress in March 2016, the Chinese government will target an average annual GDP growth rate of 6.5 percent through 2020.¹¹ This is a significant decline from the previous five-year average annual growth of 7.8 percent.¹² In addition, for those Chinese firms and individuals who do business in Africa, government-imposed restrictions aimed at staunching the flow of money out of China have made business deals and investments increasingly difficult.¹³

Other emerging economies are unlikely to make up for the slackening Chinese role in African markets:

- Brazil's growth has steadily declined from 0.1 percent in 2014 to an estimated -3.8 percent in 2015, with projections for 2016 improving only slightly to -3.5 percent growth.¹⁴ The current recession is expected to be Brazil's worst in more than a century.
- Russia's economy contracted by 3.7 percent in 2015, and is not projected to begin growing again until 2017.¹⁵

India remains a positive outlier, as it is expected to grow by 7.5 percent in 2016.¹⁶ Given India's long-standing commercial patterns in East and Southern Africa, the India-Africa relationship could prove a bright spot in an otherwise gloomy economic forecast.¹⁷

2014, <http://mgafrica.com/article/2014-11-20-china-firm-signs-12bn-deal-to-build-nigerian-railway-its-largest-single-overseas-contract-yet>.

11 "Unlucky for Some," *Economist*, March 12, 2016, <http://www.economist.com/news/china/21694581-governments-economic-plan-next-five-years-will-not-live-up-its-promises-bold>.
 12 Calculated using IMF GDP growth rates between 2011 and 2015.
 13 Wei Gu, "Chinese Consumers Race to Buy Dollars as Yuan Slides," *Wall Street Journal*, January 12, 2016, <http://www.wsj.com/articles/chinese-consumers-race-to-buy-dollars-as-yuan-slides-1452611031>.
 14 IMF, "World Economic Outlook Update," January 19, 2016, IMF World Economic Outlook Update p. 6.
 15 Ibid. US sanctions on Russia, imposed in March 2014 over the country's military intervention in Ukraine, are a contributing factor to Russia's contracting economy. But they are also an opportunity for Africa, as the continent is now one of the few places that Russian businesses are still able to invest.
 16 World Economic Outlook, op. cit., p. 15.
 17 See J. Peter Pham, "India's New African Horizons: An American Perspective," *Africa Review*, vol. 5, no. 2, 2013, pp. 93-103.

8 Calculated using UN Conference on Trade and Development data.

9 From UNCTAD, quoting the Balance of Payments Manual (5th Edition): "FDI refers to an investment made to acquire lasting interest in enterprises operating outside of the economy of the investor. Further, in cases of FDI, the investor's purpose is to gain an effective voice in the management of the enterprise." UNCTAD, "Foreign Direct Investment," [http://unctad.org/en/Pages/DIAE/Foreign-Direct-Investment-\(FDI\).aspx](http://unctad.org/en/Pages/DIAE/Foreign-Direct-Investment-(FDI).aspx).

10 "China Firm Inks \$12bn Nigerian Railway Deal - Its Largest Single Overseas Contract Yet," Mail and Guardian Africa, November 20,

Impact on African Markets

The overall fear of an emerging-markets slowdown blinds most mainstream investors to nuanced differences between economies, and dampens investor confidence in African markets. A number of multinational firms reacting to the negative news emanating out of emerging markets are pulling their investments from capital markets, especially those in Africa. The MSCI Africa index, an index measuring the equity market performance in Africa, has dropped by 19 percent in 2015, significantly more than that of other frontier markets.¹⁸

Consequently, Africa's economic growth is slowing. Current projections anticipate that sub-Saharan Africa's average GDP growth will drop by just over a percentage point to 3.8 percent in 2015.¹⁹ Oil-exporting countries will be hit slightly harder, with expected growth of only 3.6 percent in 2015.²⁰

Current IMF projections do suggest that a combination of factors, including normalization of economic conditions in emerging economies, an easing of China's slowdown, lifting of Iran sanctions, and "spillover" from developed economies' growth, will lead to an economic rebound for emerging markets in late 2016.²¹ Sub-Saharan Africa's average growth has dipped from 5.0 percent in 2014 to 3.8 percent in 2015, but is expected to begin growing in late 2016 and grow on average by 5 percent until 2020. By comparison, sub-Saharan Africa's growth prospects in 2010 and 2011 were 4.8 and 5.8 percent, respectively, and rising.²²

As both Africa's largest economy and most populous country, Nigeria has often been regarded as a

bellwether for the economic well-being of the continent as a whole. The country's average annual GDP growth rate between 2005 and 2013 was an impressive 7.5 percent, a period which coincided with the growing acceptance of the "Africa Rising" narrative. However, Nigeria's estimated 2015 GDP growth will be closer to 4 percent, where it is expected to stay annually until 2019, possibly leading to a reevaluation of this long-standing barometer.²³

The rapid fall of oil prices has hit Nigeria's budget hard. While the country has managed to diversify its economy to a significant degree, more than two-thirds of government revenues are still reliant on oil sales.²⁴ The country's deficit is expected to double to \$15 billion in 2016, equivalent to 3 percent of Nigeria's GDP.²⁵ President Muhammadu Buhari's staunch refusal to devalue the naira has tied the hands of his fiscal management team, leaving them with little option but to increase the national debt in an effort to postpone a budgetary crisis. Thus, in January 2016, Finance Minister Kemi Adeosun announced that the government would borrow approximately \$9 billion—56 percent of which will be external debt—to close the gap.²⁶ In her January 2016 visit to Nigeria, IMF Managing Director Christine Lagarde warned, "Hard decisions will need to be taken on revenue, expenditure, debt, and investment going forward."²⁷ But as of March 2016, the government was in discussions with China about a further loan of up to \$2 billion.²⁸

Angola, the other major oil exporter on the continent, had an average annual growth rate of 10.8 percent from 2005 to 2013. In 2015, the growth rate dropped to 3.5 percent and is expected to remain below 4 percent

18 Matina Stevis, "Africa Bruised by Investor Exodus," *Wall Street Journal*, February 25, 2016, <http://www.wsj.com/articles/africa-bruised-by-investor-exodus-1456050601>.

19 IMF, "Regional Economic Outlook: Sub-Saharan Africa," October 2015, <http://www.imf.org/external/pubs/ft/reo/2015/afr/eng/pdf/sreo1015.pdf>, p. 10.

20 Ibid. In North Africa, GDP growth is a mixed bag: Libya's economy contracted by some 25 percent in 2014, although, assuming the country's non-extremist warring factions can come together in a unity government as they have pledged, it is expected to slowly recover in the coming years and get back to low, positive growth by 2016; Egypt and Morocco experienced steady GDP growth from 2014 to 2015, and while some North African economies are projected to experience declines in 2015 and 2016, the overall trajectory for the region is positive. See World Economic Outlook, op. cit., p. 173.

21 World Economic Outlook, op. cit., p. xvi.

22 IMF, "Regional Economic Outlook: Sub-Saharan Africa," April 2010, <https://www.imf.org/external/pubs/ft/reo/2010/afr/eng/sreo0410.pdf>, p.1.

23 World Economic Outlook, op. cit.

24 "After Oil," *Economist*, June 18, 2015, <http://www.economist.com/news/special-report/21654361-oil-shock-has-left-deep-hole-governments-finances-economy>.

25 Myles Udland, "Africa's Largest Economy Needs a \$3.5 billion Emergency Loan After Getting Hammered by the Oil Crash," *Business Insider*, January 31, 2016, <http://www.businessinsider.com/nigeria-asks-world-bank-for-loan-ft-reports-2016-1>.

26 Paul Wallace, "Nigeria to Increase Budget Gap as Oil Falls Below Benchmark," *Bloomberg Business*, January 21, 2016 <http://www.bloomberg.com/news/articles/2016-01-21/nigeria-widens-2016-budget-gap-forecast-after-oil-price-plunge>.

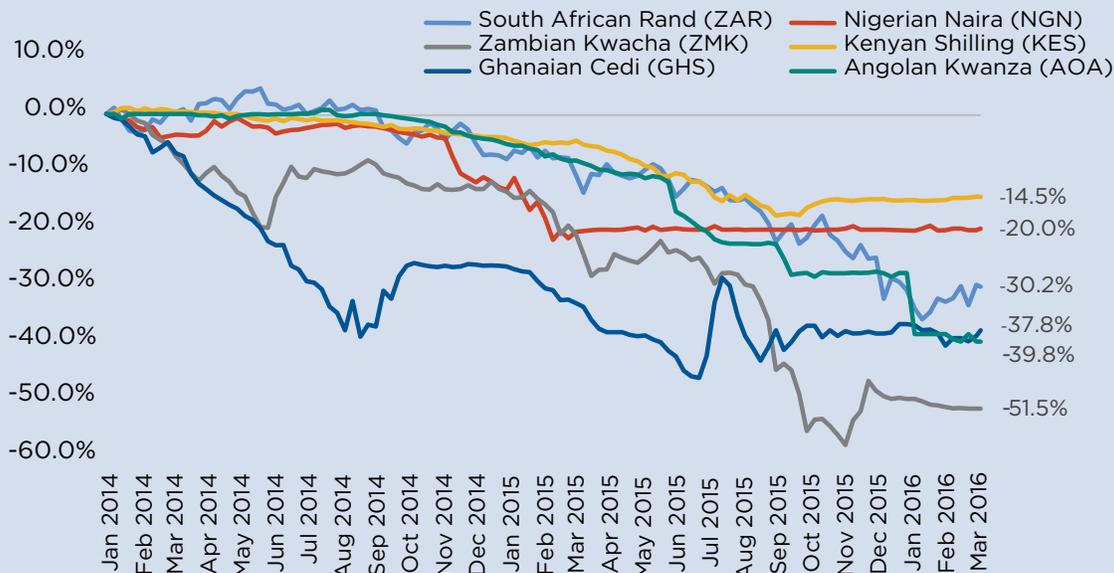
27 Christine Lagarde, "Nigeria—Act with Resolve, Build Resilience, and Exercise Restraint," January 6, 2016, <https://www.imf.org/external/np/speeches/2016/010616.htm>.

28 Ulf Laessing and Felix Onuah, "Exclusive: Nigeria to Seek China Loan, Shelves Eurobond Sale for Now - Sources," Reuters, February 20, 2016, <http://uk.reuters.com/article/us-nigeria-borrowings-exclusive-idUKKCN0VJ2AE>.

BOX 1: CURRENCY WOESⁱ

The impact of falling commodity prices in dependent economies is reflected in weakening currencies. Falling currencies, in turn, make the importation of a broad array of basic and luxury consumer goods more expensive, which dampens the spending power of wealthier individuals and the new consumer classes across the region.

Figure 3. Select Currencies Shown against the US dollar between January 2014 and March 2016



Source: Bloomberg.

- Zambia's currency, the kwacha, depreciated sharply between September and December 2015, and remains stable but low against the dollar, down some 58 percent at one point last year.
- In February 2015, the Central Bank of Nigeria devalued the naira 20 percent against the US dollar. In January 2016, the IMF called for more flexibility on the exchange rate to eliminate the spread between official and black market trading, which may lead to further devaluation of the currency. Buhari fervently opposes this measure, arguing that Nigeria imports too many goods for a currency devaluation to have an impact.
- The Ghanaian cedi has lost some 13 percent of its value against the dollar in the past year, but the uptick in gold as a hedge to global market volatility is helping Ghana to stabilize the cedi after two years of precipitous decline. In March, inflation fell as the currency remained stable.
- South African President Jacob Zuma caused the rand's biggest slide since 2011, when he unexpectedly fired the country's finance minister in December 2015. The rand dropped 5.4 percent against the dollar in a single day. The currency rallied slightly four days later when the government announced Pravin Gordhan as the new Finance Minister (he previously held the position from 2004-09). Feuds between the Minister and President Zuma continue to cause concern in South Africa.

ⁱ Unlike other African currencies, the West African CFA franc (XOF) and the Central African CFA franc (XAF), the currencies of the eight-member West African Economic and Monetary Union (UEMOA) and the six-member Economic and Monetary Community of Central Africa (CEMAC), respectively, have held their value. This is a result, however, of the fixed exchange rate that both CFA francs have with the Euro (€1 = XOF/XAF 655.957), which is guaranteed by the Banque de France. The downside of this stability is that in return for the peg, the countries have to deposit a substantial share of their foreign exchange earnings and reserves with the French central bank, funds that are unavailable for development in Africa, where the strict, anti-inflationary monetary policy often results in lack of liquidity for CFA franc economies.

annually in coming years.²⁹ As a result, Angola's budget is 40 percent lower than that of two years ago. Facing that reality, the government has made drastic—and sometimes controversial—public spending cuts. Earlier this year, the government ran out of money to pay its garbage collectors, and the buildup of trash and sewage exacerbated a major outbreak of yellow fever in Angola's capital Luanda. Some health experts fear that a cholera epidemic could be next.³⁰

Growth projections for diversified countries in East Africa—especially those with a small but growing manufacturing base—are better than their commodity-dependent peers. Kenya, which currently exports no crude oil and whose fast economic growth depends on a combination of manufacturing, infrastructure, and agriculture, is expected to grow at 6.8 percent in 2016 and 7 percent in 2017.³¹ The country is also helped by a vibrant tourism sector, which has accounted for roughly 12 percent of Kenyan GDP over the past five years.³² While the threat of terrorism—al-Shabab in neighboring Somalia has carried out multiple cross-border attacks, mainly in the northeastern part of the country—and the resulting travel advisories issued by Western embassies have dissuaded foreign tourists, Kenyans themselves increasingly prefer to travel and vacation domestically, which offsets the loss of international visitors.³³ Kenya remains ripe for strong growth, and projections estimate the country's GDP will grow at more than 8 percent over the next two years.

Another economic success story is Ethiopia, which, notwithstanding some domestic political and ethnic unrest, is set for more than 8 percent growth in both 2016 and 2017. Ethiopia's state-led development model has focused on industrialization and manufacturing, and well-known names in the industry have flocked to

Ethiopia to set up textile and shoe processing plants. Turkish and Chinese manufacturers have been some of the most active. The Huajian Group, one of the first investors in Ethiopia's Eastern Industrial Zone, now employs four thousand Ethiopians and produces seven thousand shoes per day, earning \$18 million from exports in 2014.³⁴ This type of investment rests on the back of efforts to build out the local leather value chain—Ethiopia produces nearly 2.7 million cattle hides, 8.1 sheepskins, and 7.5 million goat skins annually.³⁵ Producing and getting goods to market is globally competitive in Ethiopia, given its low electricity prices and massive public expenditures on infrastructure. A \$475 million commuter light rail train system started operations in November 2015 and can carry up to sixty thousand passengers per hour.³⁶ A string of hydroelectric dams that has begun to come online—including the Grand Ethiopian Renaissance Dam (scheduled to be completed next year), which, with its 6,000 megawatts (MW) capacity, will be Africa's largest hydroelectric project—also assures manufacturers of a steady and cheap power supply for their operations.

Homegrown Problems

The Chinese slowdown and falling commodity prices do not explain all African nations' economic challenges. There are other, homegrown problems that affect some African economies, and many started long before the current downturn:

- **Corruption and mismanagement:** Corruption, especially in the oil sector and around other valuable extractive industries, remains a major impediment to growth. In Nigeria, for example, Buhari inherited a scandal concerning \$20 billion in missing oil revenues; he came to power on the promise to get back the “mind-boggling” sums of stolen revenue.³⁷ Similar corruption issues plague South

29 “World Economic Outlook,” op. cit.

30 “Angola's Chaotic Capital of 6.5 Million Has Been Taken Over By Mountains of Trash,” Agence France Presse, January 28, 2016, <http://mgafrika.com/article/2016-01-28-angolas-chaotic-capital-of-65-million-has-been-taken-over-by-mountains-of-trash>.

31 “Kenya Emerging as One of East Africa's Growth Centers,” The World Bank, March 2015, <http://www.worldbank.org/en/country/kenya/publication/kenya-economic-update-anchor-ing-high-growth-can-manufacturing-contribute-more>.

32 Knoema, “Kenya - Travel & Tourism,” <http://knoema.com/atlas/Kenya/topics/Tourism/Travel-and-Tourism-Total-Contribution-to-GDP/Total-Contribution-to-GDP-percent-share>.

33 “Up to 66 percent of Kenyans Prefer Local Tourism, Says Survey,” *Daily Nation*, October 2, 2014, <http://www.nation.co.ke/business/Up-to-66-per-cent-of-Kenyans-prefer-local-tourism-says-survey/-/996/2473178/-/cgcc0kz/-/index.html>.

34 Katrina Manson, “The Ethiopia Paradox,” *Financial Times*, July 24, 2015, <http://www.ft.com/intl/cms/s/0/68d05fe2-30b3-11e5-8873-775ba7c2ea3d.html#slide0>.

35 “Why Ethiopia is Becoming a Leader in the Leather Industry,” <http://www.ethiopianembassy.be/blog/2015/04/18/why-ethiopia-is-becoming-a-leader-in-the-leather-industry/>.

36 “Ethiopia Starts First Light Rail Passenger Service in Addis Ababa,” September 22, 2015, *Railway-Technology.com*, <http://www.railway-technology.com/news/newsethiopia-starts-first-light-rail-passenger-service-in-addis-ababa-4675845>.

37 For more on Nigeria's current economic troubles, see Aaron Sayne and Aubrey Hruby, “Nigeria's Oil Revenue Crunch,” Atlantic Council, January 2016, http://www.atlanticcouncil.org/images/publications/Nigeria_s_Oil_Revenue_Crunch_web.pdf.

African President Jacob Zuma, who in February 2016 pledged to repay \$24 million of public funds he used to upgrade his private residence. Moreover, Zuma's general mismanagement of Africa's second-largest economy—most recently illustrated by his appointing and firing of two Finance Ministers in the space of four days in December 2015—has rocked the confidence of both major investors and ordinary consumers.

- **Onerous debt obligations:** Ghana was one of the early countries to tap global financial markets in order to fund large infrastructure projects, and it has issued four Eurobonds since 2007. The most recent issuance, in 2015, had Ghana paying more than it wanted, at 10.75 percent. With a strong dollar and slowing growth, public debt has soared, reaching nearly 71 percent of the country's GDP in mid-2015; by comparison, Ghana's debt was 120 percent of GDP in 2000, before the country joined the Heavily Indebted Poor Countries Initiative and qualified for debt relief.³⁸ Ghana is engaged with both the IMF and Asian institutions on programs to lessen the debt load, which may include a new petroleum tax and restricting the wage bill.³⁹
- **Environmental curveballs:** Progressively worsening drought across southern Africa has drained Zambia's dams and, by extension, the country's hydropower potential—that accounts for more than half of Zambia's electricity supply. Combined with the high cost to import electricity and diesel fuel for generators, the government overspent its 2015 budget by \$1.4 billion due to emergency power purchases.⁴⁰ Even with the extra spending, Zambia experienced regular power blackouts

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through the end of last year, dealing a further blow to an economy already reeling from falling prices for the product of its important copper mines.

- **Insecurity and political instability:** Domestic instability continues to threaten even the fastest-growing African economies. Northeastern Nigeria and parts of neighboring countries continue to be racked by the violent terrorist insurgency Boko Haram; Kenya continues to be targeted by terrorist strikes; Ethiopia has faced escalating protests, some of which resulted in violence, in various parts of the country over the past three years; and the Democratic Republic of the Congo faces a fraught election cycle that could easily plunge the country, or the region, back into conflict.⁴¹

Reasons for Optimism

Despite the current bump in the road, there are fundamental reasons for optimism about Africa's continued economic growth. Key demographic trends, coupled with increased economic diversification and deepening regional integration, bode well for African economies in the medium- and long-term. Some investors even see now as an ideal time to buy into African assets and

companies, given current depressed prices and more bullish long-term prospects.

- **Promising demographics:** Africa is home to a large, and growing, population of young people. In fifteen countries, half the population is under eighteen years old; in three countries, half are under sixteen years old.⁴² While burgeoning youth populations present a challenge to governments to improve education and infrastructure systems and provide employment for a growing segment of the population, they also offer an opportunity—in 2050, 25 percent of the global workforce will be African.⁴³ Increasingly, these young people are

38 "Ghana's Public Debt Climbs to 71 percent of GDP in June as cedi slides," *Reuters*, September 14, 2015, <http://www.cnbc.com/news/western-africa/2015/09/14/ghana-public-debt-cedi-slides/>; "HIPC Paper," Bank of Ghana, <https://www.bog.gov.gh/private-content/Research/Sector%20Studies/HIPC%20Paper2005%20final-main.pdf>, p. 11.

39 Lisa Steyn, "Are We Heading for an African Debt Crisis?" *Mail and Guardian*, February 12, 2016, <http://mg.co.za/article/2016-02-11-are-we-heading-for-an-african-debt-crisis>.

40 "Weathering the Storm: Zambia's 2016 National Budget," *PricewaterhouseCoopers*, October 9, 2015, <http://www.pwc.com/zm/en/assets/pdf/PwC%20Zambia%202016%20Budget%20Bulletin.pdf>.

41 See Gérard Prunier, "Why the Congo Matters," *Atlantic Council*, March 2016, http://www.atlanticcouncil.org/images/publications/Why_the_Congo_Matters_0308_web.pdf.

42 "The State of the World Population," *United Nations Population Fund*, 2014, https://www.unfpa.org/sites/default/files/pub-pdf/EN-SWOPI4-Report_FINAL-web.pdf.

43 J. Peter Pham, "Africa's Pivotal Year," *American Interest*, January 12, 2016, <http://www.the-american-interest.com/2016/01/12/african-pivotal-year/>.



moving to cities, and Africa remains the second-fastest urbanizing continent, behind Asia: by 2030, the number of Africans living in rural and urban settings will be roughly equal; just two decades later, more than 60 percent of Africans will live in cities.⁴⁴ Sixty cities—and the number is rising—already have more than one million inhabitants.⁴⁵

Urbanization will increasingly yield economic growth. Countries can begin to take advantage of the benefits of agglomeration and economies of scale; urban residents have better access to physical infrastructure, financial services, and consumers—these consumers, in turn, create a market for local agricultural goods that supports rural Africans.⁴⁶

- **Diversifying products and partners:** African countries are increasingly exporting diverse products to larger numbers of partners.⁴⁷ Moreover, intra-African trade has almost doubled in the past two decades, albeit beginning from a low base. This key opportunity for trade diversification had largely been overlooked, but efforts toward greater regional integration are now underway.

As markets grow in size, as a result of regional integration, they also become more diversified and attractive to foreign investors. The East African Community recently eased work permit requirements for East African citizens, and the Economic Commission of West African States is rolling out biometric identification cards to facilitate ease of travel and business across

44 KPMG, “The Role of Cities in Africa’s Rise,” 2012, <https://www.kpmg.com/Africa/en/IssuesAndInsights/Articles-Publications/Documents/The-Role-of-Cities-in-Africas-Rise.pdf>.

45 Mark Bradford, “The 10 African Cities Poised for Take-Off,” World Economic Forum, May 8, 2014, <http://www.weforum.org/agenda/2014/05/top-10-cities-forum-africa-2014>.

46 J. Peter Pham, “Africa,” *Choosing to Lead*, September 2015,

<http://www.choosingtolead.net/africa>.

47 Aubrey Hruby, “Diversifying African Trade: The Road to Progress,” Atlantic Council, December 2015, http://www.atlanticcouncil.org/images/publications/Diversifying_African_Trade.pdf, p. 4.

borders. While regional economic communities (RECs) are deepening integration, there are grander movements on a continental level. In 2015, the Tripartite Free Trade Agreement was signed between three RECs and encompasses twenty-seven nations.⁴⁸ It has formed the backbone for negotiations on an ambitious future continental free trade area. As intra-African trade and investment increases, it may also offset some of the FDI lost amid the current downturn.

- **Growing discretionary spending and strong African brands:** Analysts project that the number of African households with disposable income will pass 128 million by 2020.⁴⁹ This rising consumer class may not automatically turn into an importing class, as many have predicted. Strong African brands, many of which have localized supply chains, and a growing preference to buy local will help mitigate the impact of widespread currency devaluation and slower growth. A slew of recent studies highlight the popularity of African brands in the face of international competitors. More than 89 percent of Nigerians believe that local apparel brands are more fashionable than international ones,⁵⁰ and in Ghana, consumers prefer GoldenTree, a local chocolate and candy brand, three to one over its closest competitor, the global brand Mars.⁵¹ If Africa's growing consumer class is willing to buy locally, weak currencies are less painful, and less politically dangerous.

Africa's more diversified economies, and particularly oil-importers including Ethiopia and Kenya, actually stand to gain from a collapse in commodity prices. According to a 2015 analysis, Kenya, Côte d'Ivoire, and Ethiopia spend more than a fifth of their total

import bills on oil.⁵² As of mid-March, Brent crude oil was trading around \$40 a barrel with other blends priced slightly lower. The same principle applies to import bills for food, and the UN Food and Agriculture Organization recently determined that sub-Saharan Africa would save an estimated \$10 billion dollars on its food import bill as a result of falling global commodity and transport costs.⁵³

The depressed prices in the majority of Africa's largest economies are, in fact, the reason that many seasoned emerging market investors see now as the time to buy. Despite the outflow from public markets, in 2015, almost \$4 billion was raised for Africa-focused private equity funds, nearly matching the \$4.2 billion raised in 2014.

Recommendations

To weather the emerging market downturn, African governments should work to eliminate costly inefficiencies, increase diversification, and speed regional integration. The US government under President Barack Obama has accelerated its "commercial diplomacy" with the continent, but the next administration should do even more to encourage trade and development between the United States and Africa.

African governments should:

Attack inefficiencies and prioritize productivity.

African countries continue to be held back by lagging productivity and sluggish competitiveness rates. In the latest World Economic Forum Global Competitiveness Report, even countries with high economic growth—like Ethiopia and Côte d'Ivoire—do not rank well, placing at 109 and 91, respectively, out of 140 countries ranked.⁵⁴ But the current downturn offers African governments an opportunity to attack costly inefficiencies, including lengthy transport processes and other non-tariff

48 The agreement was signed by the Common Market for Eastern and Southern Africa, the EAC, and the Southern African Development Community. See J. Peter Pham, "Free Trade Pact Highlights Egypt's Pivot Back Towards Africa," *AfricaSource*, <http://www.atlanticcouncil.org/blogs/africasource/free-trade-pact-highlights-egypt-s-pivot-back-towards-africa>.

49 "Lions on the Move: The Progress and Potential of African Economies," McKinsey & Company, June 2010, p. 3. McKinsey measures "disposable income" as a household making more than \$5,000 per year.

50 "The Rise of the African Consumer," McKinsey & Company, October 2012, p. 4.

51 "The Power and Promise of Brands—and the Perils of a 'One Size Fits All,'" *How We Made it in Africa*, March 21, 2014, <http://www.howwemadeitinafrica.com/the-power-and-promise-of-brands-and-the-perils-of-a-one-size-fits-all/>.

52 "The Contrarian: Oil Lows are a Net Positive for Africa," *Invest Africa*, January 2015, http://investafrica.com/wp-content/uploads/2015/09/Invest-Africa-Research_Oil-Lows_January-2015.pdf.

53 "Food Outlook," Food and Agriculture Organization of the United Nations, October 2015, http://www.fao.org/fileadmin/user_upload/newsroom/docs/Food%20Outlook%20October%202015.pdf, p. 128. The worsening drought in southern and eastern Africa may impact these projections, as nations will be forced to import more food to meet local demand.

54 Press Release, "'New Normal' Productivity Spells Uncertainty for Global Economy," World Economic Forum, September 30, 2015, <http://reports.weforum.org/global-competitiveness-report-2015-2016/press-releases/>.



King Mohammed VI of Morocco inaugurates the Noor Solar Project near Ourzazate. Morocco is a major player in renewable energy, and uses wind power to enhance the country's diversification efforts. *Photo credit: MAP.*

barriers to the movement of goods, people, and capital. Doing so now will leave governments better prepared for future economic fluctuations.

Heads of state from Kenya, Rwanda, and Uganda (with Burundi, the Democratic Republic of the Congo, Ethiopia, South Sudan, and Tanzania as active observers) have already focused political will on enhancing trade by easing transit time and communication costs in the region. Through the Northern Corridor Integration Projects (NCIP), they have reduced cargo truck transit times by more than two weeks without any additional investment in infrastructure.⁵⁵ The NCIP process—one that systematically identifies trading and business environment inefficiencies through enhanced regional integration—should be applied by other RECs and governments in Africa.

55 Aubrey Hruby, "China's Slowdown: An Opportunity for Africa to Address Longstanding Economic Inefficiencies," *Financial Times*, October 26, 2015, <http://blogs.ft.com/beyond-brics/2015/10/26/chinas-slowdown-an-opportunity-for-africa-to-address-longstanding-economic-inefficiencies/>.

Current low oil prices also offer a rare opportunity for countries to eliminate expensive petrol subsidies. Angola has cut subsidies, raising fuel prices by 39 percent;⁵⁶ in Nigeria, oil prices are already so low that the fuel subsidy, which has long troubled prior administrations—and at its height cost the government some \$13.6 billion a year⁵⁷—is not currently being paid. The time is ripe to eliminate it from the books altogether.

Other commodity-dependent countries should follow suit in eliminating costly subsidies and better preparing for future economic downturns. Even countries that are not reliant on commodities, such as Kenya, have used low oil prices to better prepare for future price fluctuations. In October 2015, the country passed a 16

56 "Angolan Fuel Prices Rise as Government Lowers Subsidy," Reuters, January 2, 2016, <http://af.reuters.com/article/investing-News/idAFKBN0UG04B20160102>.

57 "A Citizens' Guide to Energy Subsidies in Nigeria," Institute for Sustainable Development, 2012, https://www.iisd.org/gsi/sites/default/files/ffs_nigeria_czguide.pdf, p. 11. Naira to USD calculations made based on the 2011 naira.

percent value-added tax on all oil products, to better position the country against future external shocks.⁵⁸

While governments have a role to play, the private sector is an equally powerful player in unlocking hidden growth through enhancing worker productivity. Andela, an education start-up based in Lagos, Nigeria, proves an innovative example. The company recruits young Nigerian students to participate in a four-year funded fellowship designed to produce world-class software developers, and it pairs Nigerian developers with companies in the United States, serving as an example of how to mobilize a largely untapped supply of talent on the continent by equipping young people with the skills that are demanded by the market.⁵⁹

High unemployment rates among college graduates in Nigeria (some 20 percent of 11.1 million unemployed young Nigerians are college graduates) and other African countries, show that an educated workforce is not necessarily a productive workforce.⁶⁰ Companies investing in the region should partner with governments to address the productivity gap, not only for macroeconomic reasons, but also for their own sustainable profitability.

Intensify diversification efforts.

Many African countries have made commendable progress in diversifying trade partners and products, and they will suffer much less in the current downturn than those economies that remain highly dependent on one or two products. But while progress has been made, it needs to be prioritized in both good and bad economic times.

The potential of the agricultural sector is largely untapped. African governments should look to examples of countries that have successfully diversified away from solely exporting commodities, to

58 James Anyanzwa, "Kenya to Reintroduce VAT on All Oil Products," *Business Daily*, October 17, 2015, <http://www.businessdailyafrica.com/Kenya-to-reintroduce-VAT-on-all-oil-products/-/539552/2918042/-/5cnnvn/-/index.html>.

59 Oluwaseun Adegoke Ayeniyi, "Rebooting School: The Andela Story," *Ventures Africa*, June 15, 2015, <http://venturesafrica.com/features/rebooting-school-the-andela-story/>; Klint Finley, "This Company is Paying Nigerians to Learn Computer Programming," *Wired*, December 18, 2014, <http://www.wired.com/2014/12/andela/>.

60 Tunji Akande, "Youth Unemployment in Nigeria: A Situation Analysis," Brookings Institution, September 23, 2014, <http://www.brookings.edu/blogs/africa-in-focus/posts/2014/09/23-youth-unemployment-nigeria-akande>.

BOX 2: Diversification Case Study—Morocco

Historically lacking the major reserves of exportable hydrocarbons that have been a blessing—as well as a curse—for some of their neighbors, Morocco's leaders have emphasized building a diversified economy, fostering not only northwest Africa's most significant tourism industry, but also positioning the country as a regional hub for everything from manufacturing to financial services.ⁱ

Recently the country has also focused efforts on improving agricultural productivity, with national plans for irrigation sustainability and market access designed to boost agriculture exports.ⁱⁱ The government's "Green Plan" aims to create 1.5 million new jobs by 2020, by accelerating the development of competitive agriculture through over one thousand new projects with high value-added to both production and agro-food, as well as by supporting smallholder cultivation in difficult rural areas, in transition to hardier high-value crops and processing of local products. Morocco has also emerged as a major player in the global transition to renewable energy, pioneering the use of cutting-edge wind and solar technology in Africa. The Noor Solar Project, recently inaugurated by King Mohammed VI near Ouarzazate, for example, is the world's largest concentrated solar power plant, and part of an ambitious plan to source 42 percent of the country's energy needs to renewable sources by the end of the decade, and to then even begin exporting electricity to Europe.

i J. Peter Pham and Ricardo René Larémont, "Morocco's Emergence as a Gateway to Doing Business in Africa," Atlantic Council, August 2014, http://www.atlanticcouncil.org/images/publications/Moroccos_Emergence.pdf.

ii "Growing Morocco's Agricultural Potential," The World Bank, February 18, 2016, <http://www.worldbank.org/en/news/feature/2016/02/18/growing-morocco-s-agricultural-potential>.

an enhanced agricultural sector for lessons learned. In Morocco, the government prioritizes high-value crops, including citrus fruits and tomatoes, and established the Agency for Agricultural Development to aid such efforts.⁶¹ Ethiopia has taken a local approach, and provides agricultural inputs and technical know-how

61 Sunil Sanghvi, Rupert Simons, and Roberto Uchoa, "Four Lessons for Transforming African Agriculture," McKinsey & Company, April 2011, <http://www.mckinsey.com/industries/public-sector/our-insights/four-lessons-for-transforming-african-agriculture>.

to millions of smallholder farmers. As a result, the country doubled its maize production over a twenty-year period, and is now the second-largest maize producer in sub-Saharan Africa.⁶² Rwanda's farmers produced nearly 800,000 tons of grain in 2014—more than three times what they harvested in 2000—thanks in large part to improved techniques, including better management, fertilization of their fields, and the use of hybrid seeds.⁶³

Focus on adding value locally.

In the face of high import costs, African countries should focus efforts on local value addition as a twenty-first century approach to import substitution. In the past, African governments have attempted this in diverse ways: Gabon banned the export of unhewn timber in 2010, while Ghana used tax incentives to encourage cocoa companies, such as ADM and Cargill, to process cocoa locally and create value-added products including cocoa butter, cocoa liquor, and cocoa powder. Processing agricultural produce nearer to African farms would not only reduce waste from spoilage, but also create well-paying jobs that are resistant to commodity price shocks for Africa's youthful population, a point that African Development Bank President Akinwumi Adesina, an agronomist by training, repeatedly makes.⁶⁴

African countries do not always need to look too far afield for inspiration or partners to create value-added exports. The 2014 \$2.3 billion Gabon-Morocco partnership, which will combine ammonia (produced from Gabon's abundant natural gas reserves) with phosphoric acid (from Morocco's phosphate deposits, the largest in the world) to produce fertilizer,⁶⁵ is

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a good example of a joint venture that will create jobs and generate revenue for both countries.⁶⁶ The fertilizer produced, once the project is completed, will then be able to meet almost one-third of the expected demand across Africa. An important component of this initiative is a plan, championed by the Moroccan phosphate group OCP's Chairman, Mostafa Terrab, to develop a network of small- and medium-sized project contractors and create a more robust ecosystem of value-added business in the partner countries.⁶⁷

To support the progress being made in Africa, the United States should:

Sustain and expand high-level commercial diplomacy across Africa.

US companies often misperceive the level of risk in investing in African markets. This perception gap was first outlined in Ernst and Young's 2013 Africa Attractiveness Survey, which found that 86 percent of business leaders, who already work in Africa believe that the continent's attractiveness will improve in coming years. Only 47 percent of those without a business presence on the continent believe the same.⁶⁸ The US government has an important role to play in making these businesses more comfortable venturing into African markets.

In 2000, the United States set a new standard for commercial engagement with the passage of the African Growth and Opportunity Act (AGOA) under President Bill Clinton (the legislation has since been expanded and extended six times under his successors). Engagement around health issues gained

of total global reserves of phosphate rock. The expansion of existing mines and the development of a new mining complex are expected to boost production significantly in the coming years. http://minerals.usgs.gov/minerals/pubs/commodity/phosphate_rock/mcs-2016-phosp.pdf (part of a larger report).

62 Tsegede Abate, et. al., "Factors that Transformed Maize Productivity in Ethiopia," *Food Security*, vol. 7, no. 5, October 2015, <http://link.springer.com/article/10.1007%2Fs12571-015-0488-z>.

63 "A Green Evolution," *Economist*, March 12, 2106, <http://www.economist.com/news/briefing/21694521-farms-africa-are-prospering-last-thanks-persistence-technology-and-decent>.

64 "Embrace Agriculture, Improve Food Processing - Adesina," *Zambia Daily Mail*, February 17, 2016, <https://www.daily-mail.co.zm/?p=59465>.

65 According to the most recent US Geological Survey estimates, while Moroccan facilities only produce about 30 percent of the amount mined by the world's largest phosphate producer, China, the North African country holds approximately three-quarters

66 Peter Engelke, "Addressing the Food, Water, and Energy Nexus," Atlantic Council, December 2014, http://www.atlanticcouncil.org/images/files/Food_Water_Energy_Nexus_re-numbered.pdf, p. 22; "Morocco-Gabon Sign for \$2.3 Billion Fertilizer Joint-Venture," Morocco on the Move, March 7, 2014, <http://moroccoonthemove.com/2014/03/07/morocco-gabon-sign-deal-2-3-billion-fertilizer-joint-venture-reuters/#sthash.WSE6zOMy.dpbs>.

67 "A South-South Partnership Project Between Morocco and Gabon," OCP Group, <http://www.ocpgroup.ma/media/corporate-news/south-south-partnership-project-between-morocco-and-gabon>.

68 Ernst & Young, "Africa 2013: Getting Down to Business," p. 5.



US President Barack Obama speaks at the inaugural US-Africa Business Forum during the US-Africa Leaders Summit in August 2014. While continuing his predecessors' legacy of engagement around health and economic development, the Obama Administration has added a layer of "commercial diplomacy" with Africa. *Photo credit: White House.*

new prominence with the United States President's Emergency Plan for AIDS Relief (PEPFAR) under President George W. Bush, who was also responsible for the establishment of the Millennium Challenge Corporation (MCC). MCC has provided billions for infrastructure and other transformative major initiatives to countries that have demonstrated their commitment to good governance and economic freedom; so far, fifteen African countries have been beneficiaries of MCC compacts.⁶⁹ While continuing the high levels of assistance under PEPFAR and MCC, President Barack Obama has shifted focus to business by adding a new layer of commercial diplomacy to his administration's Africa strategy. The inaugural 2014 US-Africa Leaders Summit had a significant business component, and at the first-ever US-Africa Business Forum, American companies announced tens of billions of dollars of

investment into Africa; a second Forum will take place in 2016.

The Obama administration has also launched Power Africa as a hallmark initiative, through which it aims to address long-standing obstacles to electricity access across African countries, and hopes to spur the generation of 30,000 MW of new power (when Power Africa launched in 2013, sub-Saharan Africa's power capacity was overwhelmingly concentrated in South Africa, and two-thirds of Africans lacked regular and reliable electricity access) by partnering with governments and the private sector.⁷⁰ Currently, more than one hundred companies, including Citi, General Electric, and Goldman Sachs, are Power Africa partners, standing prepared to invest in energy projects across African markets.

⁶⁹ African countries that have received a second MCC compact include Benin (Power sector specific), Cape Verde, Ghana (Power sector specific), Lesotho, Morocco (Employability and Land specific), Senegal, and Tanzania.

⁷⁰ "The Roadmap," Power Africa, <https://www.usaid.gov/sites/default/files/documents/1860/power-africa-roadmap-v2.pdf>, p. 8.

These programs appear to be working. In 2014, the United States became the largest investor in Africa, increasing FDI projects by 29.5 percent from 2013.⁷¹ In the latest Ernst & Young attractiveness survey, researchers found that while the number of foreign direct investment projects on the continent decreased between 2013 and 2014, the amount of capital involved, and the subsequent jobs created by the projects, increased. North Africa proved an especially attractive place to invest, and the region experienced a growth in the number of FDI projects and FDI capital between 2013 and 2014.⁷² The next US administration should continue—and even scale up—the commercial engagement policy.

Moreover, as significant as AGOA has been for commercial relations between the United States and African countries, the next administration should set a priority to continue its predecessors' high-level engagement, with the objective of upgrading the unilateral preferential trade scheme under AGOA into a permanent program. This lasting program should encourage African integration, while also opening the door to a future free-trade agreement between the United States and Africa as a whole (to date, Morocco is the only African country with a free-trade agreement with the United States).⁷³ Bilateral investment treaties (BITs), which afford investors important guarantees

about fair and equitable treatment and access to neutral arbitration, among other protections, should also be pursued.⁷⁴

Conclusion

The current emerging market downturn offers a serious challenge to economies across the developing world. For countries that have successfully diversified their economies, the impact of falling commodity prices may prove less painful than for those countries that rely heavily on the export of one or two items for economic growth. Effects of this downturn on economic powerhouses China, Brazil, and Russia have already trickled down to negatively affect African growth.

Some countries—including Morocco, Senegal, Côte d'Ivoire, and some of those in East Africa—will weather the downturn better than their neighbors and will use current economic conditions as an opportunity to effectively prepare for future price shocks. Hopefully, others will follow.

Dr. J. Peter Pham is Director of the Atlantic Council's Africa Center.

Aubrey Hruby is a Senior Fellow at the Atlantic Council's Africa Center.

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71 Ernst & Young, "Making Choices," p. 18. Ernst & Young tracks investment into Africa based on the number of FDI projects, rather than the amount of money spent per project.

72 "Making Choices," op. cit., p. 4.

73 J. Peter Pham, "5 Ideas for a Post-Midterms Africa Agenda," *The Hill*, November 10, 2014, <http://thehill.com/blogs/pundits-blog/international/223473-5-ideas-for-a-post-midterms-africa-agenda>; "Morocco's Emergence as a Gateway to Doing Business in Africa," op. cit.

74 The United States currently has BITs with only nine African countries: Cameroon, the Republic of the Congo, the Democratic Republic of the Congo, Egypt, Morocco, Mozambique, Rwanda, Senegal, and Tunisia.

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