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Inflation in Africa and the DFIs

From the north of Casablanca, Morocco, to Nairobi, Kenya, Lagos, Nigeria, and down south to Johannesburg, South Africa, the common phenomenon in the economy late in the year 2022 and presently in the new year 2023 is "inflation." Inflation is the rate at which prices increase over a given period. Inflation is typically a broad measure, such as the overall increase in prices or the increase in the cost of living in a country.

The current rise in inflation is a result of the surge in crude oil prices, which has occurred in the midst of the conflict between Russia and Ukraine, and the rising cost of energy around the world that has translated to a significant uptrend being witnessed in most economies as prices of goods and services have reached unprecedented levels.

The International Monetary Fund (IMF) has also projected that the present inflationary pressure will continue in 2023, leading to further concerns over a consequent global economic recession. In the same vein, the IMF increased the inflation projection for advanced economies to 5.7% and 8.7% for emerging markets and developing economies respectively.

While there are big differences between countries, the median inflation rate in the region increased to almost 9 percent in August 2022. Inflation in Ghana and Nigeria increased to 40.4% and 21.63% respectively.; in South Africa and Zimbabwe, the inflation rate ticked up to 7.6% and 255% respectively. Other countries that also witnessed a surge in inflation include Rwanda (16.1%), Egypt (13.2%), Botswana (12.7%), and Kenya (7.9%). Inflation, no matter how mild it may be, is having a significant effect on the economy of Africa. High inflation leads to a delay in long-run economic growth and distortions in macroeconomic stability. In the DFIs, particularly, inflation has an adverse effect on capital accumulation and investment and deteriorates income distribution. A high inflation rate damages economic growth through declining financial development, especially by damaging the operation of financial markets. Higher rates of inflation give rise to higher interest rates and reduced real rates of return on bank assets, lowering financial intermediation. Given the adverse effect, inflation, if an adequate policy is not put in place to curtail it, will push some DFIs to near-negative loan terms and poor general business performance.

According to Mr. Cyril Okoye, the Secretary General of AADFI, the current inflationary trend will hurt DFIs in Africa, impacting their operational costs, which will rise. Besides, it will affect the value of the funds DFIs lend to businesses when it is being paid back. Most African national DFIs may cut back on lending to the MSMEs, which would impact their economies' recovery. Moreover, the cost of funds will be higher, and businesses will have difficulties accessing complementary finance to support their operations. On the way forward, DFIs should price their new lending appropriately given the current inflationary trend and depending on the sources of their funding. DFIs will need to look at their operating cost and cut expenses where necessary to remain sustainable.

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