Eritrea

Recent macroeconomic and financial developments

Eritrea's economy recovered from multiple shocks, notably desert locust invasions and COVID-19, to grow by 2.9% in 2021, a switch from a contraction of 0.6% in 2020. Growth was led by industry and services on the supply side and private consumption and investment on the demand side. The uptick in global demand and prices for metals boosted industry, but services' contribution to growth in 2021 was lower than pre-COVID levels as hospitality, tourism, transport, and trade were hit by containment measures. Stability of global supply and value chains eased inflation to 4.5% in 2021 from 4.8% in 2020.

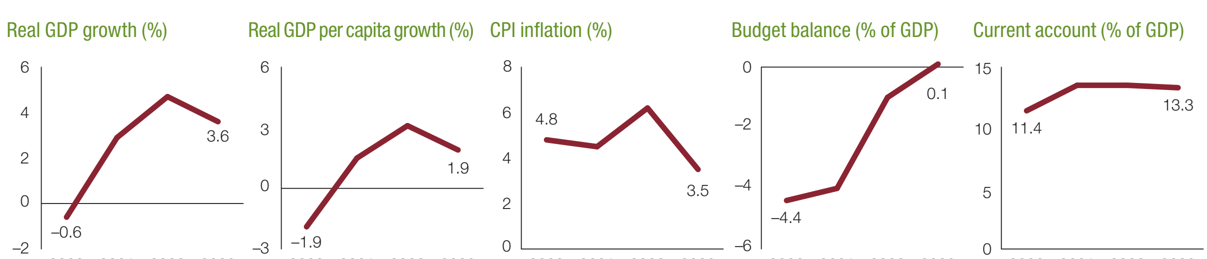
The financial sector is small, bank-based, and offers a limited range of financial services. The fiscal deficit narrowed to 4.0% of GDP in 2021 from 4.4% in 2020, reflecting fiscal consolidation and a gradual pickup in public revenues with the economic recovery. The fiscal deficit was financed by a drawdown on government deposits with the central bank. Eritrea's public debt-to-GDP ratio dropped by 9.1 percentage points to 175.6% in 2021 relative to 2020; the country remains in debt distress. The current account surplus widened to 13.5% of GDP in 2021 from 11.4% in 2020, reflecting the rise in global demand for and prices of metals (metals account for about half of total exports). International reserves were estimated at 4 months of imports in 2020.

Outlook and risks

GDP growth is projected at 4.7% and 3.6% in 2022 and 2023, due to increased international prices for metals. Growth will be led by industry and services, and by private consumption and investment. Fluctuations in commodity prices are a key downside risk to the outlook, which calls for increasing value addition and export diversification. Higher food and oil prices triggered by the Russia–Ukraine conflict are expected to increase inflation to 6.2% in 2022 before it eases to 3.5% in 2023. Fiscal consolidation and enhanced public revenues from metal exports is projected to lower the fiscal deficit to 1% of GDP in 2022 and generate a surplus of 0.1% in 2023, with the current account surplus stabilizing at13.5% and 13.3% of GDP. The $21.51 million (0.9% of GDP and 2.2% of international reserves) SDR allocation, recorded at the central bank, is expected to boost international reserves.

Climate change issues and policy options

Eritrea is highly susceptible to climate change, including El Niño. In 2008–21, Eritrea experienced five major droughts, which affected over 3.3 million. Reliance on rainfed agriculture absent an integrated climate-smart agriculture policy has increased deforestation, land degradation, and vulnerability of smallholder farmers. Eritrea is ranked 178 out of 181 countries on the 2019 Country Index of the Notre Dame Global Adaptation Initiative and 130 out of 180 on the 2021 GCRI. The climate adaptation and mitigation plans are outlined in the 2021 NDC strategy, which commits to reduce GHG emissions by 12.6% unconditionally and by 38.5% with international support by 2030. The NDC identified agriculture, marine resources, health, water, and land resources as the most vulnerable sectors, and proposes rehabilitation of degraded land; introduction of energy-saving cooking solutions and solar-powered water systems; and promotion of integrated coastal marine management systems. Transition to RE is equally critical given the country's reliance on fossil-powered thermal plants for electricity. Implementing the NDC will cost about $7 billion, requiring innovative climate financing.



Source: Data are as of April 2022 and are from domestic authorities; figures for 2021 are estimates and figures for 2022 and 2023 are projections by the African Economic Outlook team. Data on the budget balance correspond to Eritrea's fiscal year, which runs from July 1 to June 30.