São Tomé and Príncipe

Recent macroeconomic and financial developments

The economy of São Tomé and Príncipe contracted by an estimated 6.4% in 2020, after growing by 2.2% in 2018 and 1.3% in 2019. The contraction in output, for the first time in a decade, is attributed to a sharp decline in tourism and service sectors, which were severely hurt by weak external and domestic demand and COVID–19 containment measures. Subdued aggregate demand also hurt the hotels and restaurants, transport, construction, and manufacturing sectors, while cocoa exports were disrupted by widespread international border closures.

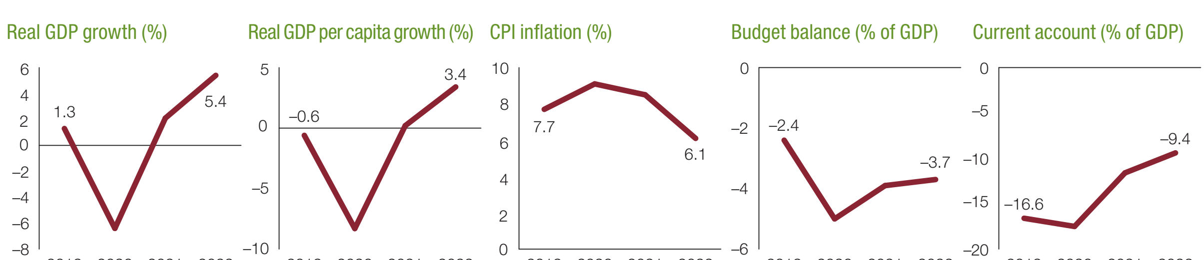
Monetary policy was accommodative to support growth. To help bank lending to a distressed private sector, the central bank reduced the minimum reserve requirements—from 21% in 2019 to 17% in 2020 for foreign-currency denominated accounts and from 18% to 14% for domestic currency accounts. Annual inflation increased to 9.1% in 2020 from 7.7% in 2019 due to pandemic-related shortages of food and other essential goods. The fiscal deficit was estimated to widen to 5.0% of GDP in 2020 from 2.4% in 2019, as spending related to COVID–19 increased and tax revenues fell. The deficit is being financed through external borrowing. Public debt rapidly rose to 104.9% of GDP in 2020 from 94.8% in 2019. The current account deficit widened to 17.5% of GDP in 2020 from 16.6% in 2019, mainly due to the reduction in tourism and cocoa receipts. Nonetheless, official reserves improved to four months of import cover from three months in 2019, boosted by budget support inflows. The banking sector remained stable, but non-performing loans increased to 28% in June 2020 from 26.7% a year earlier, as weak economic activity caused by the pandemic put pressure on borrowers' ability to repay their loans.

Outlook and risks

The economy is projected to grow by 2.1% in 2021 and 5.4% in 2022, underpinned by increased export demand for cocoa, chocolate, and palm oil and the resumption of tourism as global economic conditions improve. Growth will also be helped by an uptick in the service sectors as domestic demand strengthens. Improvements in export receipts and tourism earnings will help narrow the current account deficit and bolster international reserves in 2021. Furthermore, the government is implementing macroeconomic and structural policy reforms—such as fiscal consolidation and strengthening the central bank's independence. It is also committed to continue investment in public infrastructure to improve the business environment. Nevertheless, the economy is likely to face significant headwinds, including a potentially longer shock from the COVID–19 pandemic and a sluggish global economic recovery. This could slow recovery of the tourism sector and dampen the demand for the country's exports. The medium-term growth outlook could also be weighed down by accelerated fiscal consolidation, as the government pursues measures to improve the macroeconomic environment. Lastly, growth prospects will be clouded by an increase in poverty due to job losses triggered by the pandemic.

Financing issues and options

The country's public sector debt is high, driven mainly by oil imports for power generation, accounting for 22% of total imports in 2020. According to the International Monetary Fund's 2020 Debt Sustainability Analysis, the country is classified as being in debt distress due to prolonged unsettled external arrears, but public debt is deemed sustainable in the long term. Public debt is projected to decrease to 100.2% of GDP in 2021 and 96.4% in 2022 due to ongoing investment in alternative power sources and fiscal reforms, which could reduce external borrowing to cover oil imports. The introduction of a value-added tax of 15% in 2020 will improve revenue collection and bolster the fiscal position, which, in turn, will create fiscal space for investment in public infrastructure.



Source: Data are as of December 2020 and are from domestic authorities; figures for 2020 are estimates and figures for 2021 and 2022 are projections by the African Economic Outlook team.