Rabobank

Country report **RWANDA**

Summary

Rwanda's economy continued to outpace most other sub-Saharan African economies in 2011, owing to good harvests, a stable franc and moderate inflation compared to neighboring countries. Growth rates around 7-8% of GDP are expected to continue, driven by investments in infrastructure. However, notwithstanding strong growth and a favorable business climate, poverty remains widespread and the economy remains relatively closed with an export base that is rather undiversified (coffee, tea and minerals). Also, political life in the genocide-scarred country remains closed, as the authoritarian style of ruling by president Paul Kagame and his party does not leave room for opponents. Paul Kagame's involvement in 1994's genocide and in a conflict with the Democratic Republic of Congo continues to lead to allegations, but no problems for the country have arisen so far. The Rwandan government is still very dependent on international donor support to fund its budget, which is a risk as in the medium term donor support may fall due to austerity by donors. Rwanda's current account shows a structural deficit, caused by a structural trade deficit. External debt is slightly increasing, but still at a comfortable level.

Things to watch:

- Dependency on donor support
- Large current account deficit
- Unrest resulting from the authoritarian style of ruling by Kagame and his party

Author: **Reinier Meijer**
Country Risk Research
Economic Research Department
Rabobank Nederland

Contact details: P.O.Box 17100, 3500 HG Utrecht, The Netherlands
+31-(0)30-21-31568
R.Meijer@rn.rabobank.nl

Rwanda

National facts		
Type of government	Republic	
Capital	Kigali	
Surface area (thousand sq km)	26	
Population (millions)	10.6	
Main languages	English	
	French	
Main religions	Catholic (57%)	
	Protestant (26%)	
	Adventist (11%)	
Head of State / Government	Paul Kagame	
Prime-minister	Pierre Damien Habumuremyi	
Monetary unit	Rwandan franc (RWF)	

Economy		2011
Economic size	*bn USD*	*% world total*
Nominal GDP	6	0.01
Nominal GDP at PPP	13	0.02
Export value of goods and services	1	0.00
IMF quotum (in mln SDR) 2010	80	0.04
Economic structure	*2011*	*5-year av.*
Real GDP growth	7.2	7.5
Agriculture (% of GDP)	34	35
Industry (% of GDP)	14	14
Services (% of GDP)	52	51
Standards of living	*USD*	*% world av.*
Nominal GDP per head	562	5
Nominal GDP per head at PPP	1228	10
Real GDP per head	366	5

Social and governance indicators	rank / total
Human Development Index (rank)	166 / 187
Ease of doing business (rank)	45 / 183
Economic freedom index (rank)	75 / 179
Corruption perceptions index (rank)	49 / 183
Press freedom index (rank)	169 / 178
Gini index (income distribution)	53.1
Population below $1.25 per day (PPP)	77%

Foreign trade			2010
Main export partners (%)		*Main import partners (%)*	
Kenya	37	Kenya	20
DR Congo	15	Uganda	18
China	9	UAE	9
Thailand	6	China	6
Main export products (%)			
Coffee			19
Tea			19
Cassiteritte			14
Coltan			6
Main import products (%)			
Consumption goods			31
Intermediate goods			27
Capital goods			26
Energy			15
Openness of the economy			
Export value of G&S (% of GDP)			11
Import value of G&S (% of GDP)			31
Inward FDI (% of GDP)			1.0

Source: EIU, CIA World Factbook, UN, Heritage Foundation, Transparency International, Reporters Without Borders, World Bank, National Bank of Rwanda

Economic structure and growth

Rwanda is a small, landlocked country in East Africa and one of the most densely populated of Africa. With a GNI per capita of USD 540, Rwanda is classified as a low-income country. The agricultural sector is one of the key sectors of the economy, as the sector accounts for 34% of GDP and employs 80% of the labor force. The services sector, accounting for 52% of GDP, has grown steadily in recent years. Especially the financial, education and health sectors have seen high growth rates, growing by 14-20% in 2010.

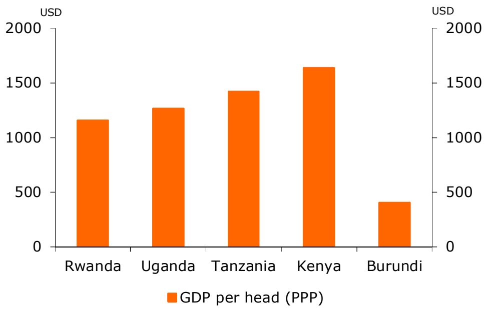
Rwanda’s export sector is underdeveloped: export of goods and services account for a meager 11% of GDP. Furthermore, exports are rather undiversified. Primary export products are coffee and tea, each accounting for 19% of total exports in 2010. Minerals are increasingly exported, but a part of them may be hindered by a new law that came into force in March 2011. This law forbids all Rwandese exporters to export minerals originating from conflict areas in Democratic Republic of Congo, to be in compliance with US law requiring minerals to be conflict-free. Main blocks of destination of Rwanda’s exports are Europe (around 50%) and Africa (around 35%). Imports are thrice as big as exports and are more diversified, consisting of consumer, capital and intermediate goods. Biggest merchandise import partners are Kenya and Uganda.

Economic growth in 2011 is expected at 7-8%, which is in line with the growth average over 2004-10 and better than most other countries in sub-Saharan Africa. The fast growth rate in 2011 is due to good harvests, a stable franc and moderate inflation compared to neighboring countries. Food production in 2011 is expected to be almost 11% higher than in 2010, as the agricultural sector benefited from plentiful rainfall and the government’s agricultural sector modernization plan started to yield results. Over the medium term, growth is expected to be somewhat slower than the 8% annual growth over the past decade, as the effects of donor inflows, infrastructure investments, a growing population, debt relief and the post-conflict growth acceleration after 1994's genocide (see next section) have worn off. However, growth is expected to remain comfortable around 7% in 2012/13, supported by infrastructure investments, a favorable business climate, and a positive stimulus from regional integration in the East African Community (EAC).[1] Infrastructure investments include the building of methane gas extraction plants by US, Finnish and Egyptian companies. As just 14% of the population has access to electricity now, these plants can expand access to electricity, and thereby develop the country substantially.

Apart from the trade contacts Rwanda maintains with EAC countries, the country has long-standing diplomatic ties with Belgium, who ruled Rwanda from 1918 until independence in 1961. Moreover, Rwanda has good contacts with donors United Kingdom and the Unites States. Relations with France and the Democratic Republic of Congo have improved after recent reconciliation meetings, but relations with France do not seem overly warm.

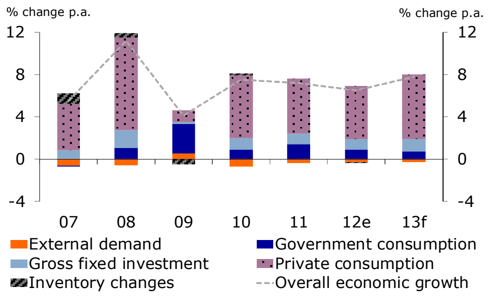
The banking sector of Rwanda is well-capitalized and profitable. The entry of foreign banks since 2005 has made the sector more competitive, but banks' loans remain highly concentrated and nonperforming loans remain high, indicating the banks charge high margins to make a profit. Another indication of the underdeveloped state of the country is access to formal finance, which is still limited with credit to private sector making up just 12% of GDP in 2010.

Figure 1: Income level



Source: World Bank WDI

Figure 2: Growth performance



Source: EIU

Political and social situation

Nominally, Rwanda is a presidentially democracy with multiparty elections since 2003. The president is both the head of state and head of government, and appoints the prime minister and the Council of Ministers. Last elections in Rwanda took place in 2010. An overwhelming re-election of president Paul Kagame – he won 93% of the votes – underscored the domination of the political scene by him and his Rwandan Patriotic Front (RPF) party. Kagame's final term as president ends in 2017, but in December 2011, Kagame refused to rule out the option of amending the constitution to allow him to stand for a third term in office. Kagame and his party are characterized by an authoritarian style, as they are fully engaged in keeping order, public security and a closely controlled external image. The authorities generally suppress opposition parties, civil-society organizations and dissident regime insiders, while press restrictions persist. Reporters without Borders' Press Freedom Index indicates the unfavorable environment for journalists: Rwanda ranks 169 out of 178 countries. Several journalists and opponents of the Rwandan government have been killed under mysterious circumstances over the years. Most recently, in December 2011, a

[1] The East African Community (EAC) is a customs union comprising of Kenya, Uganda, Tanzania, Rwanda and Burundi.

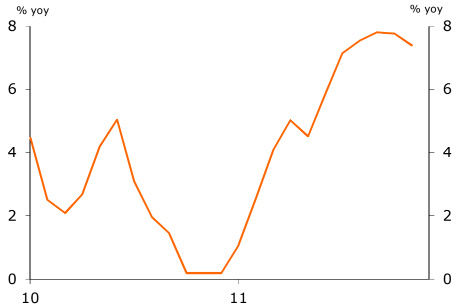
Rwandan journalist was assassinated in Uganda. More attempts to assassinate dissidents have taken place on foreign soil, including the UK and South Africa. Rwandan government has denied any involvement in the deaths and assassination attempts. Furthermore, since 2009 several grenade attacks have taken place in public spaces in Rwanda. In 2011, an attack killed 2 people and wounded 28, and another attack wounded 21 people. Reportedly, the attacks point to the frustration underlying the Rwandan Patriotic Front's domination of the political scene. Kagame's increasing autocratic leadership may fuel further tensions between him and opponents, which could escalate into large-scale social unrest. However, for now we expect that the unrest will remain local and small-scale. Therefore, we do not expect the unrest will affect the business environment.
Rwanda is scarred by the genocide in 1994, in which an estimated 800,000 people or 20% of the total population, were killed in the space of 100 days in a tribal dispute between the majority Hutus and the minority Tutsis. Most of the people killed were Tutsis, but also moderate Hutus who opposed the killing campaign and the forces directing it were killed. President Kagame's engagement in the Rwandan genocide of 1994 has continued to lead to allegations in 2010/11. Allegedly, Kagame led rebel forces in the Tutsi-led Rwandan Patriot Front in 1994 and gave the command to shoot down a plane with former Hutu president Juvenal Habyarimana, sparking the genocide. However, Kagame himself denies any involvement. The same holds for the crimes he – allegedly – committed in a Hutu hunt down into the Democratic Republic of Congo in 1996/97. For now, we do not think pending cases against Kagame by the International Criminal Tribunal for Rwanda and the French judiciary will have influence on domestic politics or the international position of the country.
Rwanda has made large progress in fighting corruption, making it the least corrupt nation in the East Africa Community. Rwanda is ranked 49 out of 183 countries on Transparency's Corruption Perceptions Index, while Italy and Ghana are less-favorably ranked on place 69. Nevertheless, corruption persists and tends to most seriously affect small and medium-sized companies.
Despite improvements in the social situation, especially in education and health sectors, a majority of the Rwandan population still lives in poverty. Supported by the World Bank, the government is carrying out a policy to tackle poverty through improved food security and targeted schemes for job creation and social protection.

Economic policy

Rwanda's economic policy is formulated in close cooperation with the IMF. Over the last years the government has markedly improved the business climate in the country, making it one of the best countries in Africa to do business in. Government expenditure for the current budget year is focused around four pillars: infrastructure rollout, maintaining growth in productive sectors, development of human capital, and promotion of good governance. In the medium term, the government aims to increase resource allocation to investment projects in infrastructure, as improved infrastructure stimulates growth and has low recurrent costs. The budget balance of Rwanda generally shows a moderate deficit between 0% and 3% of GDP, better than many other sub-Saharan African countries. This is a result of close involvement of the IMF in policy formulation and a large amount of donor inflows, accounting for 46% of total budget revenues, or nearly 12% of GDP, in 2011/12. In 2012, the budget deficit is expected to remain around 2% of GDP. In the medium term, grants are expected to fall somewhat, as donors are likely to cut their funds due to austerity measures. Also the country's slide to an evermore authoritarian style of rule is a key risk for Rwanda's donor funds. However, the government is expected to offset the fall in revenues somewhat by improvements in tax compliance. Therefore, the country's own revenue is expected

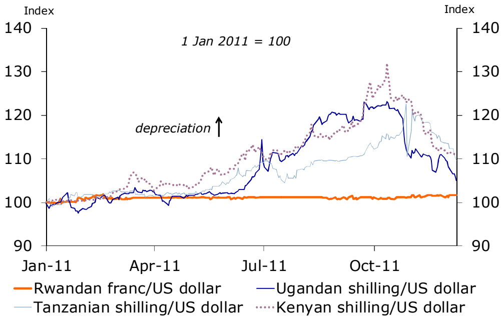
to increase, reaching around 15% of GDP in 2015. Government debt[2] is sustainable at 25-28% of GDP in 2011/12.
Core mission of the monetary policy of the National Bank of Rwanda (central bank) is ensuring price stability. A second objective is stimulating economic financing, and thereby higher economic growth. In 2009-10, the second objective seemed dominant, as the central bank lowered its key repo rate with 300bps to stimulate economic growth. Inflation was still among the lowest in the region in 2010, owing to unexpectedly low domestic food prices and a generally benign external environment. However, inflation has been accelerating since early 2011, reflecting rising global food and fuel prices. In August 2011, consumer price inflation accelerated to 7.5% year-on-year, the highest rate in two years. Since then, inflation has remained high (at 6-7%), but in single digits. As of October 2011, the central bank started monetary tightening, as concerns over inflation were increasing. The rate has gone up two times by 100bps and stood at 7% in November 2011. As the National Bank of Rwanda will continue its monetary tightening policy, single digit inflation is expected to continue in 2012.
Rwanda has a managed float exchange rate regime. Contrary to the currencies of other countries in the region, the Rwandan franc followed a stable path in recent years. Although not explicitly targeted, the low volatility in turbulent times globally suggests strong intervention by the central bank. Also, the fact that Rwanda is more self-sufficient in food production than its neighboring countries and less open, contributed to the stability of the currency and moderate inflation.

Figure 3: Inflation



Source: EIU, National Institute of Statistics of Rwanda

Figure 4: Exchange rate



Source: EcoWin

Balance of Payments

Rwanda's trade balance shows a structural imbalance, as exports lag far behind imports, causing a trade deficit of about 15% of GDP in 2011, which is slightly higher than 2010's 14.2% of GDP due to higher imports. The services balance shows a smaller, but also structural deficit, amounting to 5% of GDP in 2011. Both are expected to remain at this level in 2012. The transfer surplus, which mainly consists of donor inflows and is estimated at 10% of GDP in 2011, compensates for those deficits somewhat, but, all in all, the resulting current account deficit is expected to remain notably high, around 10% of GDP in 2011. Coming from deficits around 7.5% of GDP in 2009/10, the rising current account deficit is worrying, but can be explained by higher oil prices and more imports. In 2012, the current account deficit is forecast to remain around 10% of GDP. In the medium term, prospects are brighter, as large investment projects in cement production and energy sector are coming on stream, which can make the country more self-reliant and may increase export receipts. Furthermore, in the medium term, prospects for the services sector, including the tourism sector, are growing, which could also raise export receipts. Nevertheless, donor backing remains vital for

[2] Including publicly-guaranteed debt of the central government and the central bank.

the country's balance of payments. Phasing out of donor aid, due to austerity by donors, is a key risk for Rwanda.
Net foreign direct investment inflows are relatively small, estimated at 1% of GDP in 2010.

External position
Total external debt of Rwanda stood at 18% of GDP in 2010, which is low compared to regional peers and sub-Saharan African average. However, debt relief, received in 2006 under the Multilateral Debt Relief Initiative (MDRI) and received up to 2005 under the Heavily Indebted Poor Countries (HIPC) programme, has considerably cut back external debt. In 2004, before this debt relief, debt amounted to about 90% of GDP. Now, external debt is rising again, to about 22% of GDP in 2011/12, but it is expected to remain at an acceptable level in the medium term. As the private sector has no debts, all debt stock is held by the public sector. Debt stock consists of loans to official creditors, and is mostly medium- and long-term.
Official reserves remain comfortable around 5.5 months of imports.
The only reported arrears are principal arrears to official creditors. They stood at USD 77mln in 2010, which is unchanged compared to 2008/09.

Rwanda

Selection of economic indicators	2007	2008	2009	2010	2011	2012e	2013f
Key country risk indicators							
GDP (% real change pa)	5.5	11.2	4.1	7.5	7.2	6.5	7.8
Consumer prices (average % change pa)	9.1	15.4	10.4	2.3	7.8	6.6	6.9
Current account balance (% of GDP)	-3.9	-5.4	-7.3	-7.6	-10.2	-9.7	-7.3
Total foreign exchange reserves (mln USD)	553	596	743	813	906	973	1007
Economic growth							
GDP (% real change pa)	5.5	11.2	4.1	7.5	7.2	6.5	7.8
Gross fixed investment (% real change pa)	5.9	11.7	1.5	8.0	7.0	6.9	8.3
Private consumption (real % change pa)	5.9	11.7	1.5	8.0	7.0	6.9	8.3
Government consumption (% real change pa)	-0.7	9.1	27.0	7.5	11.3	6.9	5.7
Exports of G&S (% real change pa)	3.6	4.8	-7.4	10.0	5.4	5.0	4.5
Imports of G&S (% real change pa)	5.6	5.8	-6.9	10.0	5.4	5.0	4.5
Economic policy							
Budget balance (% of GDP)	-1.4	-0.2	-2.2	-0.1	-2.0	-2.3	-1.6
Public debt (% of GDP)	29	22	23	24	25	28	27
Money market interest rate (%)	6.0	7.7	7.2	7.1	7.5	8.0	8.0
M2 growth (% change pa)	23	26	22	15	19	16	17
Consumer prices (average % change pa)	9.1	15.4	10.4	2.3	7.8	6.6	6.9
Exchange rate LCU to USD (average)	548.3	549.3	568.2	583.1	602.3	624.8	632.3
Recorded unemployment (%)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Balance of payments (mln USD)							
Current account balance	-147	-252	-383	-421	-605	-622	-539
Trade balance	-452	-623	-772	-787	-892	-945	-983
Export value of goods	184	257	188	297	373	359	382
Import value of goods	637	880	961	1084	1265	1304	1364
Services balance	-93	-113	-178	-247	-312	-331	-318
Income balance	-15	-34	-37	-46	-50	-41	-40
Transfer balance	413	518	604	658	648	695	801
Net direct investment flows	67	103	119	62	72	85	88
Net portfolio investment flows	0	0	0	0	0	0	0
Change in international reserves	113	43	146	70	93	68	34
External position (mln USD)							
Total foreign debt	562	652	747	939	1116	1180	1160
Short-term debt	11	14	6	7	9	10	10
Total debt service due, incl. short-term debt	112	100	117	n.a.	n.a.	n.a.	n.a.
Total foreign exchange reserves	553	596	743	813	937	1000	1030
International investment position	-135	-172	-249	-417	n.a.	n.a.	n.a.
Total assets	721	879	1174	1251	n.a.	n.a.	n.a.
Total liabilities	856	1051	1423	1668	n.a.	n.a.	n.a.
Key ratios for balance of payments, external solvency and external liquidity							
Trade balance (% of GDP)	-12.1	-13.3	-14.8	-14.2	-15.0	-14.8	-13.4
Current account balance (% of GDP)	-3.9	-5.4	-7.3	-7.6	-10.2	-9.7	-7.3
Inward FDI (% of GDP)	1.8	2.2	2.3	1.0	n.a.	n.a.	n.a.
Foreign debt (% of GDP)	15	14	14	18	21	23	22
Foreign debt (% of XGSIT)	66	52	62	n.a.	n.a.	n.a.	n.a.
International investment position (% of GDP)	-3.6	-3.7	-4.8	-7.5	n.a.	n.a.	n.a.
FX-reserves import cover (months)	7.3	5.1	6.0	5.9	5.7	5.9	5.8
FX-reserves debt service cover (%)	495	598	636	n.a.	n.a.	n.a.	n.a.

Source: EIU, IMF