Macro Dev

Macroeconomics and development
JANUARY 2025 I No. 59

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Namibia – Do the oil discoveries herald a more inclusive economy?

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Date of end of writing: 22/11/2024

Summary: Namibia, a small and outward-looking Southern African economy, faces major challenges posed by the size of its territory (34th largest country in the world, 14th on the continent) and its very low density (2nd lowest in the world). Capitalizing on its mineral resources, in particular diamonds and uranium, its natural resources (ecotourism) and its political stability, the country has achieved a higher per capita income than many other African countries. But the wealth generated is very unequally shared. While Namibia allocates a large proportion of its budget to social spending, it is the second most unequal country in the world, and has so far failed to put an end to endemic poverty fueled by high unemployment.

Its economic growth model is thus neither diversified nor inclusive. The public sector plays a dominant role and hinders the emergence of the private sector, thereby holding back job creation in high value-added industries. The international openness of this small economy makes it vulnerable to global crises, and its specialization in mining exports makes it dependent on commodity prices. The end of the commodity super cycle plunged the economy into recession in 2017 and 2019, forcing the country to tighten its belt. The Covid-19 crisis made things worse, leading to a steep contraction of real GDP of 8.1% in 2020.

The macroeconomic situation improved after the pandemic, with a rebound driven by growth in the mining sectors where prices recovered, initially for diamonds, then uranium and gold, and by the return of international tourists. This has benefited public accounts: in 2023/24, Namibia showed a positive primary balance for the first time in ten years. However, the public debt ratio remains high, and reducing it is likely to take a long time in the coming years due to the substantial public financing requirements. But this debt has a low risk profile: it is primarily domestic and external public debt is mainly bilateral, with almost half denominated in rand. This moderates the foreign exchange risk due to the fixed parity between the Namibian dollar and the South African rand.

The country is on the brink of a major change which is set to radically transform its economy. Indeed, the recent discoveries of vast oil reserves could propel the country among the leading African producers. The country has geared up for this windfall by setting up a sovereign wealth fund based on the Norwegian model. The objective is to invest these revenues over the long term, thereby cushioning the economy from global fluctuations in commodity prices and contributing to a better distribution of wealth. These discoveries are already transforming its balance of payments, with the massive flows of foreign direct investment and the imports of goods and services related to this activity. However, this course is likely to increase the country's vulnerability to the low-carbon transition by maintaining the economy in its extractive framework.

Another promising avenue for the Namibian economy lies in the energy transition. The country enjoys strong renewable energy potential, in particular for green hydrogen, due to its vast solar and wind energy resources. Projects supported by the European Union and private companies have been emerging in recent years, but the impact on local employment and added value may remain limited, as the market mainly targets exports to the major world economies.

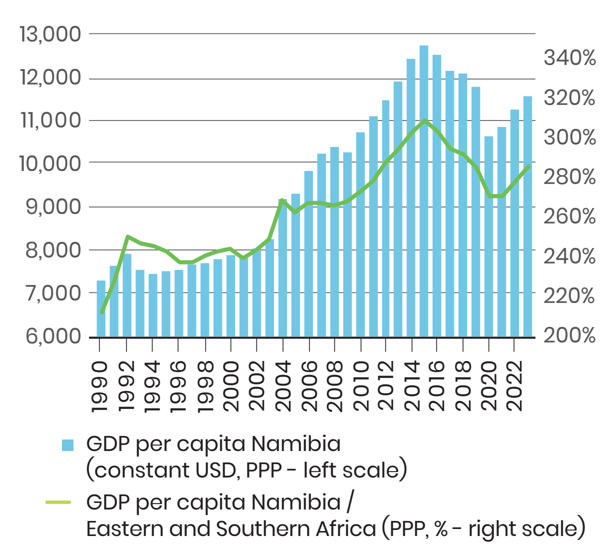
Thematic area: **Macroeconomics**
Geographical area: **Namibia**

1. Namibia's economic prosperity masks deep social disparities

Namibia is one of the few Sub-Saharan African countries to have achieved upper-middle-income status. Between 2002 and 2015, the country benefited from the commodity super cycle, with an annual average growth rate of 4.6%. To address the international financial crisis of 2008-2009, the government implemented a stimulus policy to boost business activity, in particular in the construction industry, which went on to account for up to 6% of GDP in 2015. There was a marked recovery as of 2010, and GDP growth, driven by a favorable monetary environment and a credit boom, was close to 6% for five years, well above South African growth which was 50% lower.

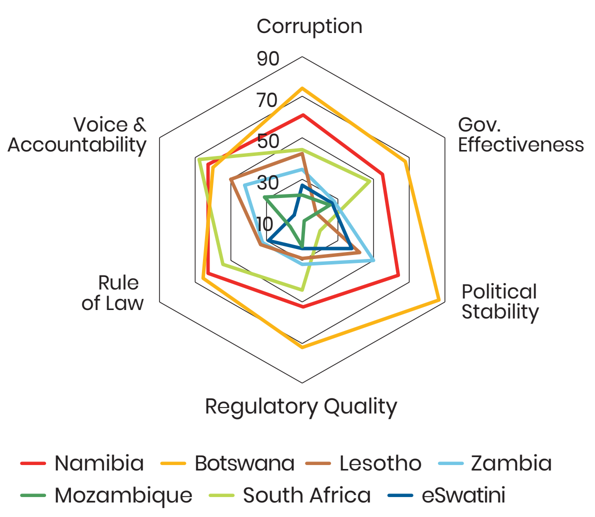
As with its neighbor, Botswana, **political stability has been one of the main enabling factors for this long-term growth in the creation of per capita wealth**. Since 1990, SWAPO (South West Africa People's Organisation), historically the party which fought for the country's independence, has maintained a hegemonic position in Namibian politics. The four successive presidents elected are from the party. In addition, the party has won all the general elections, and has held the two-thirds majority in the National Assembly during several parliamentary terms. Despite losing ground over the years, during these 34 years in office, the party has consolidated Namibian democracy and enabled this young Southern African country to rank among the countries on the continent benefiting from stable democracy, with no military coups or violent opposition to the regime.

Graph 1: Namibia has one of the highest levels of GDP per capita in the region



Source: World Bank.

Graph 2: The performance of the country's governance indicators is among the strongest on the continent



Source: World Bank.

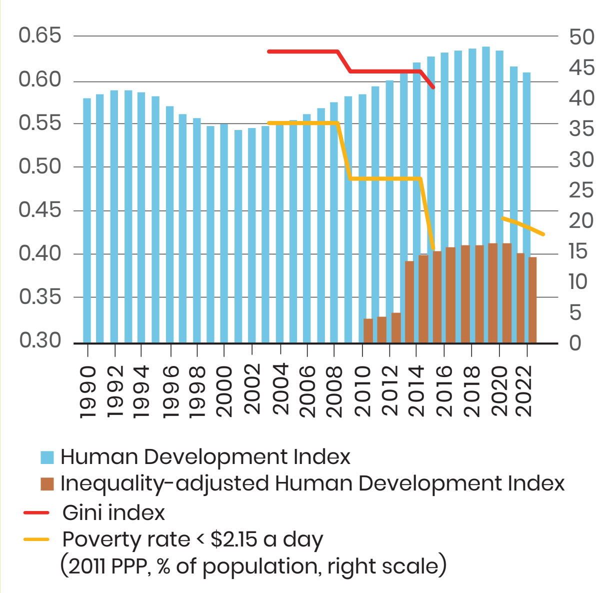
International political observation organizations classify the Namibian regime as free,[1] a polyarchy [2] (the highest possible ranking for a democracy), and an electoral democracy+,[3] ranking 5th in Sub-Saharan Africa. **They praise the robustness of the measures to protect political rights and civil liberties, in particular the holding of free elections,**[4] **the political pluralism, the respect for freedom** of expression, the press and religion, and the independent judiciary. Consequently, **the World Bank's Governance Indicators rank Namibia among the best-performing countries on the continent.**

But the high level of per capita wealth conceals the weakness of its social indicators, which are more comparable to those of lower-middle-income countries (LMICs), or even those of low-income countries. The level of extreme poverty thus remains high. The last official statistics date back to 2015: while the country recorded its highest level of per capita income, almost 16% of the population was still living on less than $2.15 a day, which is equivalent to the average of LMICs. **According to the World Bank, the situation deteriorated** in the following years. This level is estimated at 18% in 2023, a level to be compared with the poverty rate corresponding to the threshold of $6.85 defined for upper-middle-income countries (UMICs). The rate for Namibia is estimated at 60% in 2023, 3 points higher than in 2015 (while the average for this category is 25%).

Poverty is the visible part of the level of inequality in the country. There is an extremely poor distribution of income among the population: according to the United Nations Development Programme (UNDP), the richest 10% in the country own almost 50% of the wealth created and only 9% is divided between the poorest 40%, making Namibia the second most unequal country in the world after South Africa. **Almost 35 years after independence, the apartheid regime, imported into Namibia by the South African colonial power, continues to leave a mark on society.**

This poor social performance is reflected in the Human Development Index. Ranking 142nd, Namibia is a country with medium human development, like its poorest neighbors, Angola and Zambia, and well below its other neighbors, South Africa and Botswana. **The main factor affecting this composite index is life expectancy at birth**, which is well below its peers due to the AIDS virus, for which the prevalence rate still stood at 11% in 2022 and remained the leading cause of mortality.

Graph 3: Inequalities prevent Namibians from escaping extreme poverty



Source: World Bank, UNDP.

[1] Freedom House, https://freedomhouse.org/country/namibia/freedom-world/2024

[2] Harvard University, https://dataverse.harvard.edu/dataset.xhtml?persistentId=doi:10.7910/DVN/WPKNIT

[3] For the V-Dem Institute of the University of Gothenburg (Sweden), which classifies the various types of democratic regimes, the most advanced level of democracy is liberal democracy, followed by electoral democracy with a + or -.

[4] The general elections of December 2024, which were won by the ruling party's candidate with 57% of votes, were disrupted by logistical problems resulting in the polling being extended by several days and a contestation of the result by the main opposition party.

Despite **other relatively positive human development factors, resulting from the government's efforts in terms of social spending** (half of the State budget is spent on education and health), a two-tier system has developed, with high-quality private provision that serves the elite and lower quality public provision for the majority of the population and which, in view of the size of Namibia, is still difficult to access.

Finally, Namibia's highly capital-intensive growth model does not offer sufficient employment opportunities. **The unemployment rate has remained stable but high since independence, ranging between 19% and 23% of the working population.**

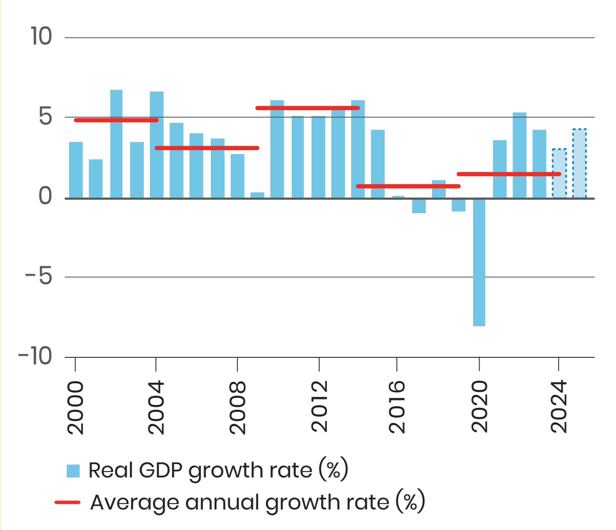
The omnipresence of the public sector in the economy also holds back job creation in the nascent private sector. The level of civil service wages, which has increased over the years, has had a crowding out effect on job creation in the private sector by diverting human resources and talents, while exacerbating the mismatch of skills. The increase in civil service wages is not specific to Namibia, but its level is well above other countries with similar levels of income. This situation, combined with a heavy regulatory burden, holds back entrepreneurship and partly accounts for the low representation of the private sector in the economy, the lack of job creation, and the high unemployment rate.

2. After years of stagnation, the macroeconomic situation is regaining momentum

The reversal of the terms of trade started to affect the Namibian economy in 2015. It decelerated and the country experienced two years of recession in 2017 (-1%) and 2019 (-0.8%), interspersed with sluggish years with growth rates not exceeding 1%.

Imbalances have emerged, despite the government's efforts to maintain a stable macroeconomic framework, attractive to foreign investment. **The expansionary policy between 2010 and 2015 resulted in successive fiscal deficits and an increase in public debt.** To address these challenges, the government had to rationalize its investment expenditures, which in particular affected the construction industry and contributed to the slowdown in activity. **In 2020, the Covid-19 epidemic thus hit a seriously weakened economy:** there was a severe recession, which reached -8.1%, four times higher than the sub-Saharan average.

Graph 4: Namibia has returned to robust growth since 2021



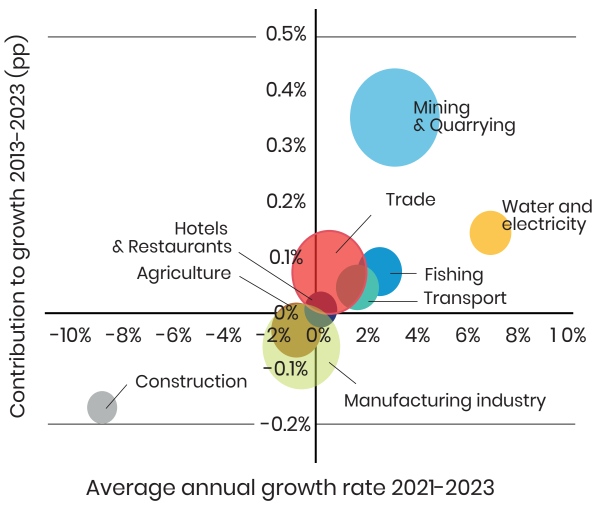
Source: IMF.

Since 2021, the Namibian economy has regained its impetus with an average growth rate of 4.4% (compared to -0.3% between 2017 and 2019). **This GDP growth has mainly remained concentrated in the mining sector**, with production driven by high diamond prices in 2021-2022, bolstered by the upturn in demand in the United States,[5] then for gold and uranium, and also by an unprecedented increase in oil and gas exploration activities. In 2023, non-mining GDP suffered from the poor perfomance of agriculture due to a major drought caused by the El Niño phenomenon, and from the continued high cost of imports, which has an adverse effect on the construction and manufacturing industries. However, it was the first full year without travel restrictions, which allowed a gradual return of international tourists bringing revenues that contributed to growth.

Despite a slight slowdown anticipated in 2024 (3.1% compared to 4.2% in 2023), due to weaker international demand and slower growth in the primary and secondary sectors (drought, less profitable base effect for mining activities), growth should remain robust in the medium-long term: an increase in uranium production with the start of operations at mines which were at a standstill and the upturn in agriculture and construction, which is already apparent in 2024. Indeed, a number of public infrastructure projects are ongoing or planned (including for roads, drilling and transport). The Central Bank thus anticipates a growth rate of above 4% for 2025 and 2026.

This dynamic growth has led to an improvement in government accounts since 2022. The total deficit reached 3.2% of GDP for the fiscal year[6] 2023/24 and, for the first time in ten years, the government recorded a positive primary balance, estimated at 1.9% of GDP. For the fiscal year 2024/25, the government expects to maintain the deficit at 3.2% of GDP, with a stabilization at around 3% in the medium term, which is based on growth in government revenue, in particular from the Southern African Customs Union (SACU).[7] However, the payroll and interest payments will remain high, and will alone account for 60% of revenue, consuming a part of the gains related to growth. The government has also announced tax breaks and an increase in investment in infrastructure. In this election year, the government could also use budgetary leverage for electoral purposes. **In the medium term, the government anticipates an increase in the total deficit to 3.9% of GDP in 2025-26** and a decrease in the primary surplus of 0.4% of GDP due to a decline in SACU revenue of 19%, before an improvement in these two balances in the following fiscal year (-3% of GDP and 1.3% of GDP).

Graph 5: The mining sector remains the main driver of growth



N.B.: The diameter of the bubbles represents the average weight of the sector in GDP

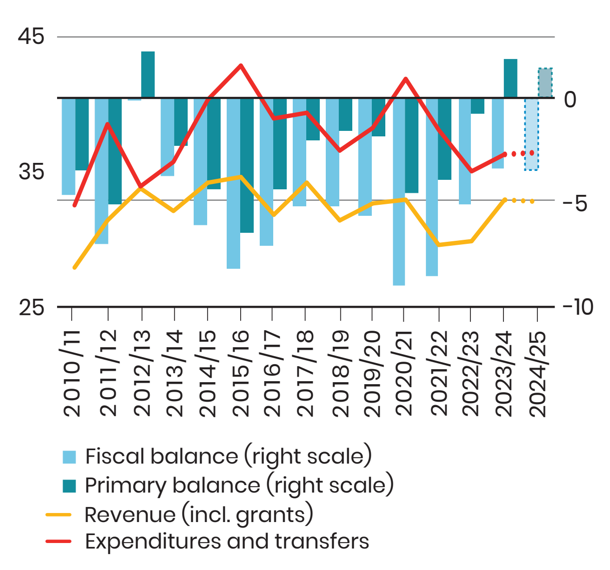
Source: UNCTAD, NSA.

[5] However, there was a downturn in the diamond market in 2023: overproduction and the decline in demand adversely affected cut diamond prices, which collapsed. In addition, the most popular rough diamonds suffer from competition from the much cheaper synthetic gems which flood the market.

[6] Namibia's fiscal year starts in April and ends in March.

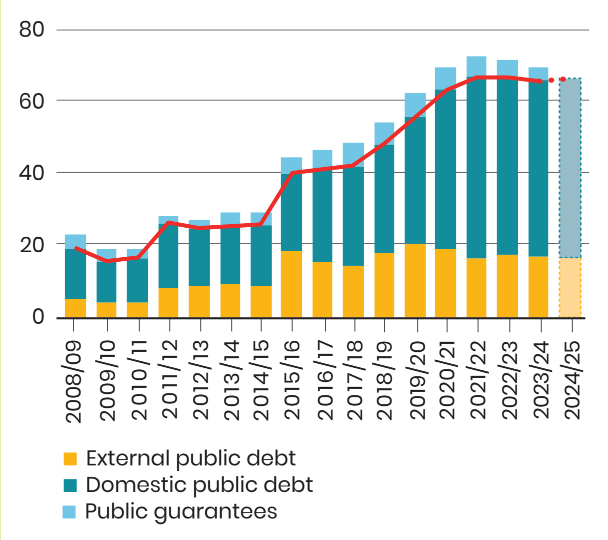
[7] The difference in the structure of Namibia's government revenue lies in the substantial share of revenues from the SACU. It can reach up to a third of the country's total government revenue. Yet the predictability of this revenue is compounded by the volatility of the amounts, which depend largely on the performance of the South African market, and by the time lag resulting from the allocation mechanism.

Graph 6: A positive primary balance that should remain positive



Source: IMF, Ministry of Finance, fiscal years from April to March.

Graph 7: The debt ratio remains at a high level, despite the decline in the public deficit since 2022



Source: IMF, Bank of Namibia, AFD calculations.

While Namibia's public debt ratio was under control until 2014/15 (26% of GDP), the repeated public deficits and the depreciation of the Namibian dollar against the US dollar (caused by the fixed parity with the rand which depreciated against the dollar between 2014 and 2016) drove it up to 56% of GDP in 2019/20. Public spending related to the Covid-19 crisis exacerbated this trend, and public debt has stagnated at a high level of 66.8% of GDP on average since the fiscal year 2021/22. The government's objective is now to reduce it to less than 50% of GDP in the medium term, while the IMF expects a stagnation at the current level until 2028-29.

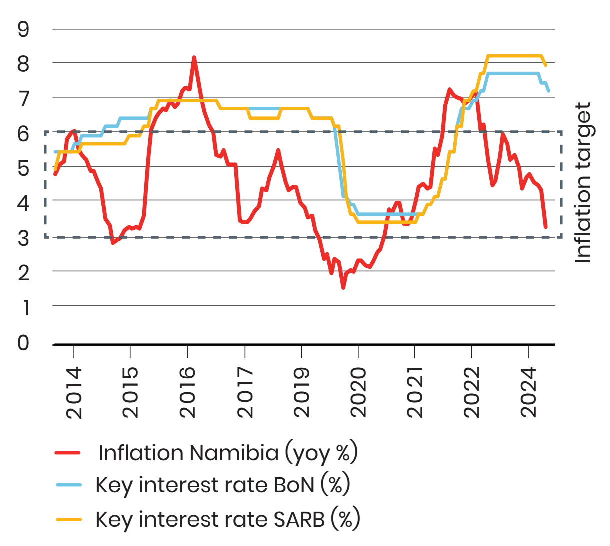
Since 2020, Namibia has had substantial public financing requirements (23% of GDP on average), generated by the government's primary deficits until 2022/23 and the significant increase in debt service costs related to the rise in interest rates. Short-term domestic debt has tripled since 2016 to a level of stock of 17% of GDP since 2021-22 which must be repaid within the year.

The structure of public debt has certain specific characteristics, with predominantly domestic debt which accounted for three-quarters of total public debt at the end of the last fiscal year. Three-quarters of external debt is to official creditors. 43% of this external debt is denominated in rand, which moderates the foreign exchange risk due to the fixed parity between the Namibian dollar and this currency. The remaining maturity stands at 6 years and the government is seeking to extend it further.

In its latest Debt Sustainability Analysis of December 2023, the IMF indicates that the risk of sovereign debt distress is moderate, in particular due to the fact that there is a deep local and regional market, interested in long-maturity securities. However, the medium-term liquidity risk is high, mainly due to the continuing public financing requirements, with a peak in 2025 (28.4% of GDP), coinciding with the repayment next October of the last Eurobond issued in 2015 ($750 million). The authorities are anticipating this repayment with pragmatism. They have already started saving on a sinking fund to repay $500 million. For the balance, they have given themselves until February 2025 to consider the best refinancing strategy, so that they can roll over this amount depending on the cost of the available sources of financing at that time.

The IMF remains cautious over the growth prospects, due to the potential risks to Namibia's economic situation in the medium term. The sluggish South African growth could affect Namibia in view of the close links between the two economies. In addition, the contribution of domestic consumption, the main driver of growth since 2021, is declining due to the cost of credit. However, the Central Bank took the lead in August and October 2024 by cutting its key interest rates twice. This decision to support growth is motivated by the return of inflation to the target range of 3%-6% since the end of 2023, and by the cut in South African key interest rates.

Graph 8: Return of inflation to target, the BoN has lowered its rates



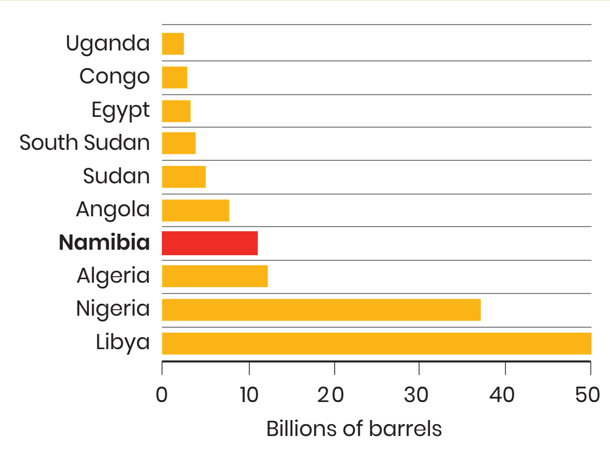
Source: Central Banks, AFD calculations.

Despite the rate cuts, the growth of bank credit remains very low at the end of 2024, for both households and companies, well below its long-term trend, as bank lending has been historically strong in Namibia. However, the share of local investment in GDP was divided by more than two-thirds between 2015 and 2022 and amounted to only 10% of GDP in 2022. But this has no impact on economic growth, which was largely driven by gross fixed capital formation (GFCF) in 2023. Indeed, the low level of local investment has been offset since last year by the sharp increase in foreign direct investment related to the exploration for hydrocarbons. Finally, in the external sector, the trade deficit is growing, due to the increase in the deficit in the services balance, which is increasingly affecting growth through a negative contribution of net foreign trade to GDP in volume.

3. Oil, hydrogen: towards a potential radical transformation of the Namibian economy

After decades of failure, the drilling programs conducted in 2021-22 by Shell and TotalEnergies in the Orange Basin off the coast in the south of the country have found huge light oil resources. Up until the recent discoveries by the Portuguese company Galp in April 2024, which estimates them at 10 billion barrels, and pending those of Chevron and ExxonMobil, the discoveries of the French and British majors are estimated at 11 billion barrels and 62 billion cubic meters of natural gas. This could propel Namibia among the world's top 20 oil producers. In 2023, Total spent half of its global exploration budget in Namibia, and is expected to devote 30% of it there this year, prior to announcing its final investment decision in 2025 for a production expected to start in 2029-2030. On the basis of existing discoveries, Namibia's maximum production capacity is estimated at 700,000 barrels per day over the next decade, meaning that Namibia would rank 5th or 6th among Africa's oil-producing countries. The start-up of production in the two promising fields of Shell and TotalEnergies could double the country's GDP.

Graph 9: Namibia's estimated oil reserves could rank the country 4th in Africa



Source: Global Firepower, AFD calculations.

However, access to the resources is complicated and the economic viability has yet to be proved. Indeed, the fields are located at about 300 km off the coast, at a depth of 3 km, then 3 km underground. But the potential is so great that the majors are falling over each other to acquire exploration licenses in this untapped basin, which has the advantage, compared to the Mozambican gas fields and the oil fields in the Gulf of Guinea, of being located in a peace zone, with no risk for the investments.

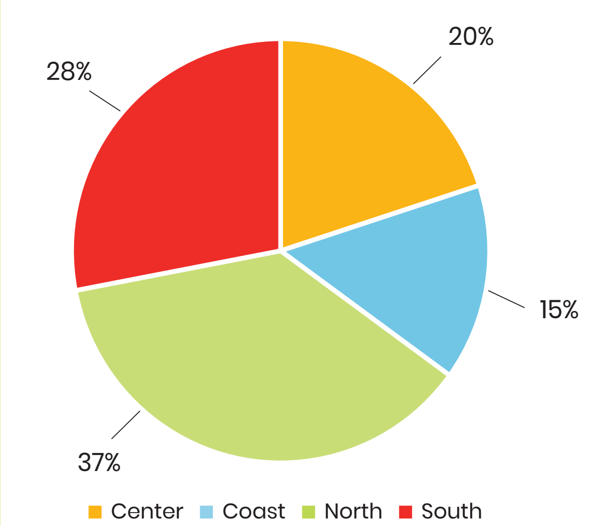
In the meantime, Namibia is preparing itself by copying the good practices of the countries that have managed to avoid the resource curse (or even the "presource curse"[8]) which affects a number of African oil-producing countries (including Angola, Congo, Equatorial Guinea, Gabon and Nigeria), and comes with phenomena such as rent-seeking, the destabilization of economic activity due to price volatility, and currency appreciation. Shortly after the announcement of the discoveries, Namibia thus created the sovereign fund Welwitschia in 2022. The fund is based on the Norwegian oil fund. Its purpose is to manage the revenues generated by the exploitation of the country's natural resources (future oil production, but also including diamonds and uranium, for example), while protecting the economy from the volatility of international markets. It will enable a more effective distribution of the profits generated by these revenues in the long term between the various segments of the population. As with its Norwegian model, the management of the Namibian fund is delegated to the Central Bank. A total of 300 million Namibian dollars (NAD), or €18 million, composed of seed capital from the government, was injected into the fund when it was created. In the future, it will be financed by the royalties received from the sale of natural resources, and by the contribution of specific public enterprises. It is both an intergenerational savings fund and a stabilization fund.

[8] Natural resource curse even before the exploitation.

The other highly publicized potential avenue for the diversification of the economy is based on Namibia's comparative advantage in terms of solar and wind energy production capacity, allowing for green hydrogen production. Namibia could thus theoretically produce some of the world's most competitive green hydrogen. It particularly interests the European Union and certain member countries, including Germany, which are committing a significant amount of funding for the development of projects. Several opportunities are being considered: green ammonia, green fertilizer, energy storage, mobility, and green steel. The government has launched the Southern Corridor Development Initiative (SCDI), a special economic zone covering 26,000 km², which will gather the industrial centers for the production of components across the value chain: renewable energies, electrolyzers, desalination plants, and storage and transport infrastructure. Pilot projects have started in the corridor, financed by European and private funds. It is estimated that the European donors have already committed $1.5 billion in loans for the development of green hydrogen in Namibia. CMB, the Belgian shipping company, is planning to invest $3.5 billion in a green hydrogen and ammonia production complex over the next five years.

However, the technology is recent, highly capital-intensive (the country estimates that it will need $190 billion of investments by 2040, equivalent to an annual GDP for 15 years), and its development is expected to take several years. This diversification is environmentally attractive, but is unlikely to provide direct benefits for the Namibian economy and local employment. Indeed, the projects envisaged are mainly export-oriented for European, Chinese, Japanese and Korean markets.

Graph 10: Tourism: the beds sold in 2023 are located all over the country

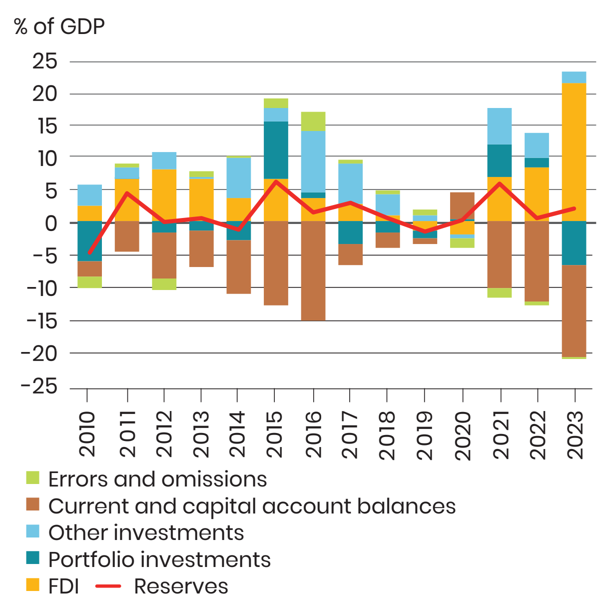


Source: HAN/Oxford Economics Africa.

Finally, in the service sector, **the development of tourism, for which the country has a real comparative advantage, would reduce its dependence on mining and, especially, provide Namibians with jobs across the country.** Indeed, in 2019, the sector provided 2.5 times more jobs than mining, and while the areas of tourist interest are mainly located in the north, they are distributed across the country. An ambitious strategy to promote the destination, similar to Tanzania's post-Covid strategy, focusing marketing efforts on the country's strengths as a top destination for glamping[9] and ecotourism linked to wildlife, would increase the number of arrivals.

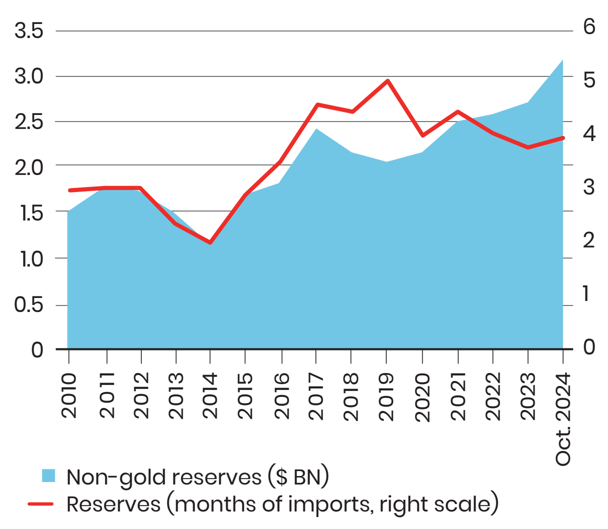
[9] "Glamping" is short for glamorous camping. It is a new trend in outdoor tourism, combining luxury, nature, comfort and respect for the environment.

Graph 11: The oil discoveries are transforming the balance of payments of the small Namibian economy



Source: IMF, AFD calculations.

Graph 12: FDI is reinforcing essential currency reserves



Source: IMF, AFD calculations.

At present, these projects are catalyzing foreign direct investment. This investment, which had largely contributed to growth between 2000 and 2015, had tended to abandon the country from 2016 onwards. Since 2021, it has returned in force and accounted for 21.1% of GDP in 2023, a record in Africa. Two-thirds are related to oil and gas exploration activities, or are intra-group loans in the mining sector. **The associated massive capital inflows and imports of goods and services affect the current account of Namibia**, whose small economy remains vulnerable to external shocks. The current account deficit has deteriorated every year and reached 14.8% in 2023, largely due to the deficit in the services balance: 7.7% of GDP in 2023, a level not seen in 30 years, due to imports related to the offshore exploration. On the other hand, the record foreign direct investment (FDI) has largely covered the current account deficit and has strengthened international reserves, which increased by 11% in 2023. Non-gold reserves stood at $3.2 billion in October 2024, just over 4 months of imports, a level deemed adequate by the IMF to maintain the fixed parity between the Namibian dollar and the South African rand.

Despite the promising avenues, the prospects for the diversification of the Namibian economy should be treated with caution. They guarantee little local employment (with the exception of tourism) and increase the dependence on commodity prices, including for hydrogen, and exposure to external shocks. In addition, **the exploitation of hydrocarbons will increase the risk of the already exacerbated low-carbon transition.** Indeed, the country is vulnerable to the energy transition due to the importance of the mining sector in its economy. This vulnerability is not related to salaries and jobs, as the mining industry is not labor-intensive, or to government revenue from sectors identified as declining in the context of the global transition, which remain below 15% of total revenue, but to the share of currency reserves accumulated by these sectors (24%). However, the fact that the country holds substantial metal and rare earth deposits linked to the transition, along with its green hydrogen potential, which sharpens the appetites of Western countries, could offset these vulnerabilities.

In June 2023, the Namibian government banned the export of unprocessed crushed lithium minerals and other critical minerals (cobalt, manganese, graphite and rare earth) to **derive greater benefit from strong global demand for these materials by increasing their added value through local processing**. Lithium reserves are estimated at 230,000 tons and the country holds 27 rare earth minerals, including dysprosium and terbium, which are required for electric car batteries and wind turbines. According to the United States Geological Survey, the subsoils of Namibia and South Africa hold the two largest quantities of rare mineral deposits in Africa. In 2022 and 2023, Namibia signed trade agreements with the European Union and Japan for the exploration and development of rare earth, lithium, and other minerals for the transition.s, de lithium et d'autres minéraux de la transition.

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List of graphs

List of acronyms and abbreviations

BoN: Bank of Namibia

FDI: Foreign direct investment

IMF: International Monetary Fund

LMIC: Lower-middle-income country

NSA: Namibia Statistics Agency

SACU: Southern African Customs Union

SARB: South African Reserve Bank

SCDI: Southern Corridor Development Initiative

SWAPO: South West Africa People's Organisation

UMIC: Upper-middle-income country

UNCTAD: United Nations Conference on Trade and Development

UNDP: United Nations Development Programme

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Publishing Director Rémy Rioux
Editor-in-Chief Thomas Mélonio
Graphic creation MeMo, Juliegilles, D. Cazeils
Design and production Ferrari

Date of end of writing: 22/11/2024

Legal Deposit 1st quarter 2025
ISSN 2266-8187
Printed by the AFD reprographics department

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