ERITREA

Table 1	**2020**
Population, million	3.5
GDP, current US$ billion	2.1
GDP per capita, current US$	588.8
School enrollment, primary (% gross)[a]	68.4
Life expectancy at birth, years[a]	65.9

Source: WDI, Macro Poverty Outlook, and official data.
Notes:
(a) Most recent WDI value (2018).

Real GDP growth declined 0.6 percent in 2020 as a drop in net exports and private consumption was cushioned by a sharp increase in capital spending in mining. The latter resulted in a fiscal deficit of 4.8 percent of GDP. Despite the positive impact of the new mines on growth, the medium-term outlook remains bleak without a re-engagement with the broader international community and the resolution of the external arrears. Latest available data from 1996/97 suggests poverty is widespread.

Key conditions and challenges

With UN sanctions lifted in November 2018, Eritrea has started emerging from a decade of international isolation. However, the re-engagement progress with development and international partners stalled a year ago. Efforts to shift from a centrally planned to a market-led economy have been very slow and sporadic, and large SOEs dominate economic activity. Monetary policy is characterized by administrative measures and fiscal dominance, while severe import restrictions enable a fixed exchange rate regime pegged to the US dollar and characterized by low foreign exchange reserves. The banking system is largely lending to the government and lacks international correspondence banks, while payment and settlement systems are absent. The country is among the most vulnerable and least adapted to climate change in Sub-Saharan Africa, and frequent weather shocks pose a heavy burden for the economy and rural livelihoods. The mining sector, which started operating in 2011, accounts for over 90 percent of total exports, yet contributions to budget revenues are limited.

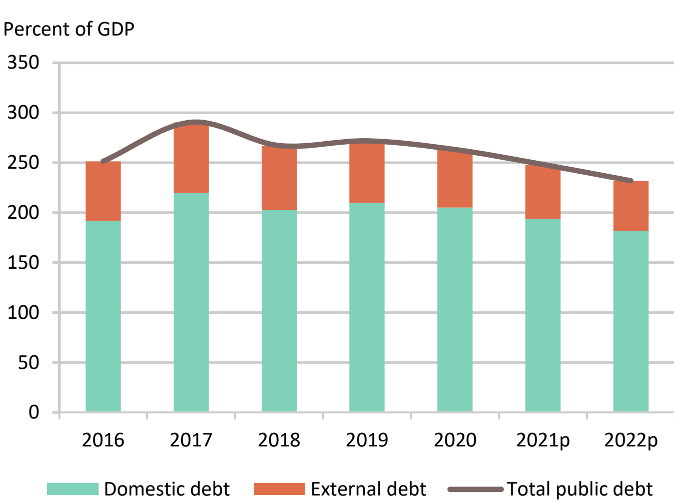
The Covid-19 crisis hit Eritrea amid a hiatus in its reengagement with development partners leaving it without needed external funding. In addition, informal-cross border trade was affected by the conflict in northern Ethiopia. Yet, Eritrea's isolation moderated the magnitude of the initial external shock.

The emergency conditions prevailing in the country over the past decade have led to data production capacity constraints. Specifically, national accounts data are limited to unofficial GDP estimates by the Ministry of Finance and inflation estimates are produced only for the capital, Asmara, while full balance of payments accounts are missing. The last population census in Eritrea took place more than 25 years ago. Therefore, little is known about socioeconomic outcomes, including poverty. Data from 1996/97, covering only urban areas, suggests that poverty was widespread with around 70 percent of the population living in poverty.

Recent developments

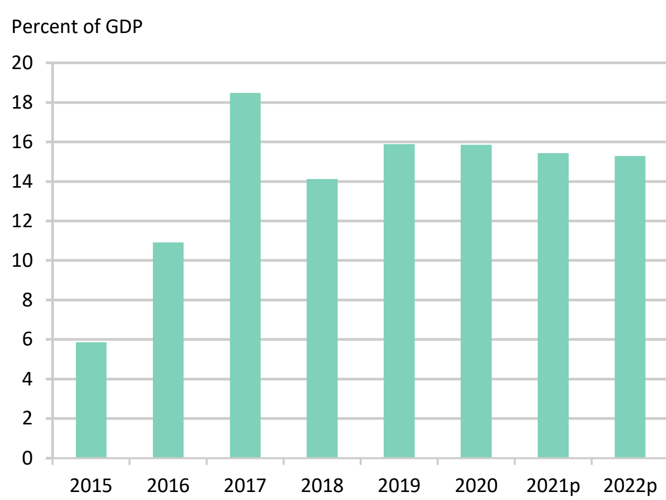
Hit by the COVID-19 crisis, real GDP growth declined an estimated 0.6 percent in 2020 from 3.8 percent in 2019. A lockdown over several months and border closures weighed heavily on private consumption. Yet, the sharp rise in government capital spending moderated the impact of the Covid crisis on output growth. Specifically, the sharp decline in exports of about 6.5 percent was offset by a contraction in imports and sharp increase in government investment totaling about 5 percent of GDP. The latter marked the opening of two mines (Colluli and Asmara) supported by net FDI inflows. The government also continued building the

FIGURE 1 Eritrea / Evolution of total public debt



Sources: Ministry of Finance, Planning and Economic Development.

FIGURE 2 Eritrea / Wage bill



Sources: Ministry of Finance, Planning and Economic Development.

important connection road from the Ethiopian border to the port of Massawa. Deflationary pressures aggravated prior to the Covid-19 crisis by the temporary opening of borders with Ethiopia in 2019 have eased and inflation reached 4.9 percent in 2020.

The external current account surplus is set to narrow to 10.7 percent of GDP in 2020 from 12.1 percent in 2019, largely due to a slowdown in remittances but also due to a compression of the merchandise trade surplus to around 3 percent in 2020 from 4.5 percent of GDP in 2019. The traditionally large net errors and omissions stem largely from trade with Ethiopia undertaken by the private sector rather than the government.

Meanwhile, the fiscal deficit widened to close to 5 percent of GDP in 2020 from 1.5 percent in 2019. The fiscal expansion was driven by an investment push in two mines and the road to Massawa as well as small dams. Public debt is estimated at above 260 percent of GDP, of which 80 percent is owed to domestic banks. That said, fiscal and domestic debt outcomes remain uncertain given frequent data revisions due to reporting lags of several months due to widespread manual processes.

Outlook

Aided primarily by the economic recovery in China, export growth of commodities is likely to lift real GDP growth to 2 percent in 2021 from -0.6 percent in 2020. As the Colluli and Asmara mines export at full capacity and aggregate demand rebounds on the back of sustained and widespread vaccination, real output growth could accelerate to an average of about 4.5 percent over the next two years. The government also expects spillover effects from the new potash mine of Colluli to fertilizer production, which in turn could increase productivity in agriculture, improving food security and livelihoods, especially if introduced in parallel with policy reforms that foster private sector development.

Nevertheless, significant downside risks cloud the horizon. Sizable uncertainties surround the evolution of the Covid-19 pandemic, including logistical and economic roadblocks hampering the prospects of timely and widespread vaccination domestically and abroad. Furthermore, severe climate vulnerabilities continue to burden Eritrea and could worsen in coming years. Finally, the fragile macroeconomic situation and severe credit constraints leave the country with little space to boost preparedness facing these risks, and to control damages should they materialize.

In this context, efforts to normalize the country's relations with the international community could result in a pathway to reduce significantly external arrears and provide much-needed external financing. This in turn would provide resources to build much needed infrastructure over the medium term, to help abate the risks associated with climate change and jump-start the private and financial sectors.

TABLE 2 Eritrea / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
Real GDP growth, at constant market prices	13.0	3.8	-0.6	2.0	4.9	3.8
Private Consumption	13.2	5.5	-1.9	2.0	8.0	6.1
Government Consumption	0.8	39.3	16.4	8.8	4.7	4.1
Gross Fixed Capital Investment	-62.8	67.5	152.2	17.7	-10.4	0.4
Exports, Goods and Services	8.9	-5.0	-6.5	35.6	6.4	4.2
Imports, Goods and Services	18.7	1.4	-3.8	22.9	6.4	6.3
Real GDP growth, at constant factor prices	12.8	3.7	-0.7	2.0	4.9	3.7
Agriculture	24.0	27.0	-0.5	3.4	3.1	2.5
Industry	11.1	13.0	-0.7	1.4	10.2	7.6
Services	4.9	-26.0	-1.1	0.3	1.5	0.5
Inflation (Consumer Price Index)	-14.4	-16.4	4.9	2.9	1.9	2.0
Current Account Balance (% of GDP)	15.4	12.1	10.7	13.9	13.5	12.1
Net Foreign Direct Investment (% of GDP)	2.9	3.9	3.8	3.6	3.5	3.4
Fiscal Balance (% of GDP)	4.3	-1.5	-4.8	-4.4	-0.8	-0.7
Debt (% of GDP)	267.1	271.8	263.1	248.2	231.8	219.7
Primary Balance (% of GDP)	5.7	0.2	-3.2	-2.9	0.6	0.6

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.
Notes: e = estimate. f = forecast.