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Growth in Africa

IT CAN BE DONE

Jeffrey Sachs has long been one of the most persuasive advocates of economic reform in Latin America and Eastern Europe. In this article, he explains why he thinks reform could work wonders in Africa too

IN THE old story, the peasant goes to the priest for advice on saving his dying chickens. The priest recommends prayer, but the chickens continue to die. The priest then recommends music for the chicken coop, but the deaths continue unabated. Pondering again, the priest recommends repainting the chicken coop in bright colours. Finally, all the chickens die. "What a shame," the priest tells the peasant. "I had so many more good ideas."

Since independence, African countries have looked to donor nations--often their former colonial rulers--and to the international financial institutions for guidance on growth. Indeed, since the onset of the African debt crises of the 1980s, the guidance has become a kind of economic receivership, with the policies of many African nations decided in a seemingly endless cycle of meetings with the IMF, the World Bank, donors and creditors.

What a shame. So many good ideas, so few results. Output per head fell 0.7% between 1978 and 1987, and 0.6% during 1987-94. Some growth is estimated for 1995 but only at 0.6%--far below the faster-growing developing countries. Asia, for example, recorded a whopping 7% per capita growth in 1995. It is little surprise, then, that Africa is receiving about 3% of the foreign direct investment flows to developing countries, while developing countries in East Asia and the Pacific are attracting about 40% of the FDI flows.

Africa is constantly berated for its poor politics and bad economic ideas, though much of the mischief has come from the outside. In the 1960s, the fad at the World Bank and among many donors was "development planning". In the 1970s, this gave way to "basic needs", a doctrine which led the World Bank to back the socialist strategies of soon-to-be-bankrupt Tanzania and other non-market economies. In the 1980s, "basic needs" was supplanted by "structural adjustment" which rightly focused on markets but neglected to set priorities in reform. In the ensuing frustration, the focus in the 1990s has shifted to "good governance": donors now berate African governments for their "lack of ownership" of reforms dictated by the IMF and World Bank.

Structural adjustment has produced some real gains. Per capita GDP is rising again after more than a decade of decline. Even so, very few cases of rapid growth are emerging from IMF-World Bank programmes. For every case of a success story like Uganda, there are others in which democratisation and incipient market reforms have been reversed under the pressure of worsening economic conditions.

The structural-adjustment programmes remain deeply flawed. The IMF is so obsessed with price stability it doesn't think very hard about anything else. The World Bank, on the other hand, has hundreds of good ideas but no priorities. Standard bank programmes call on weak, debt-ridden governments to introduce value-added taxes, new customs administration, civil-service reform, privatisation of infrastructure, decentralised public administration and many other wonderful things--often within months. It was, alas, par for the course when the bank set 111 conditions in its "policy-framework paper" on Kenya.

This overflow of conditionality may be a reflection of the Bank's own organisational weakness. In a period of tightening budgets, each department has drummed up business for itself by pushing for roles in as many loans as possible. Leadership by previous bank presidents was too weak to set sensible priorities--which in turn helps explain why structural adjustment-policies have failed to promote vigorous growth. The main challenge for the new president, James Wolfensohn, is not, as is sometimes suggested, mainly managerial. It is conceptual: to set priorities.

The best evidence of the failure of the IMF and World Bank in Africa lies in the programmes themselves. The institutions have actually been targeting low levels of growth per head throughout Africa--often just 1-2% per year--even though worldwide evidence shows that market-oriented poor countries can grow faster than richer countries. Many low and middle-income nations are averaging per capita growth of more than 5% per year. Of the 53 countries in Africa, only Botswana, Mauritius, and Uganda (since 1989), have come close to that average, and all apparently grew at less than 5% per capita in 1995.

The IMF and World Bank would be absolved of shared responsibility for slow growth if Africa were structurally incapable of growth rates seen in other parts of the world or if the continent's low growth were an impenetrable mystery. But Africa's growth rates are not huge mysteries. The evidence on cross-country growth suggests that Africa's chronically low growth can be explained by standard economic variables linked to identifiable (and remediable) policies. Remedies that have worked in East Asia can also work, with suitable modification, in Africa. Where they have been tried--in Mauritius, to some extent in Botswana and (very recently) Uganda--the result has been growth at East Asian rates.

Why has Africa failed?

Studies of cross-country growth show that per capita growth is related to:

- the initial income level of the country, with poorer countries tending to grow faster than richer countries;
- the extent of overall market orientation, including openness to trade, domestic market liberalisation, private rather than state ownership, protection of private property rights, and low marginal tax rates;
- the national saving rate, which in turn is strongly affected by the government's

own saving rate; and

- the geographic and resource structure of the economy, with landlocked and resource-abundant economies tending to lag behind coastal and resource-scarce ones. To their credit, structural-adjustment programmes have helped Africa to focus on the second and third of these problems.

These four factors can account broadly for Africa's long-term growth predicament. While it should have grown faster than other developing areas because of relatively low income per head (and hence larger opportunity for "catch-up" growth), Africa grew more slowly. This was mainly because of much higher trade barriers; excessive tax rates; lower saving rates; and adverse structural conditions, including an unusually high incidence of inaccessibility to the sea (15 of 53 countries are landlocked) plus a high reliance on natural-resource exports.

Fortunately, the geographical and resource conditions play only a modest role in Africa's growth shortfall. The lion's share can be attributed to the lack of openness, lack of market incentives and lack of national saving. The table shows the result of a study* into how much these factors contributed to Africa's growth shortfall. The study calculates that, because of its low initial income, Africa should have grown 1.4 percentage points faster than a sample of eight fast-growing developing countries in 1970-89. In fact, growth was 3.1 percentage points slower--an overall shortfall of 4.5 points. Of this, the study attributes 1.8 points to lack of trade openness; 1.9 points to low savings rates; and 0.9 points to highly distorted domestic markets. Africa's innate structural conditions, including landlockedness and natural-resource dependence, explain another 0.5 points of slower growth, not the bulk of the shortfall. Once these factors are taken into account, there is only a small (0.5 point) residual, or unexplained puzzle, to Africa's growth.

If the policies are largely to blame, why, then, were they adopted? The historical origins of Africa's anti-market orientation are not hard to discern. After almost a century of colonial depredations, African nations understandably if erroneously viewed open trade and foreign capital as a threat to national sovereignty. As in Sukarno's Indonesia, Nehru's India, and Peron's Argentina, "self sufficiency" and "state leadership", including state ownership of much of industry, became the guideposts of the economy. As a result, most of Africa went into a largely self-imposed economic exile. Colonial institutions such as agricultural marketing boards became instruments for more government intervention, and the international community became a willing partner to the new development strategies.

The statist and closed-economy strategy was already in deep trouble by the early 1980s, but a decade or more of foreign aid postponed collapse in many countries, at the cost of delaying reforms and adding to the mountain of foreign debt. Within African countries, vested interests (usually urban based, and against smallholder agriculture) kept the old strategies alive. In the donor countries, cold-war machinations, naivety, and narrow commercial interests linked to foreign aid, led donor governments and the international financial institutions to turn a blind eye to the growing policy failures. Now, however, as western aid money dries up and a new generation of leaders is elected in Africa, it is becoming harder and harder to ignore the policy failings. The question now has become: what can be put in their place?

Adam Smith in 1755 famously remarked that "Little else is requisite to carry a state to the highest degrees of opulence from the lowest barbarism, but peace, easy taxes, and tolerable administration of justice." A growth agenda need not be long and complex. Take his points in turn.

Peace, of course, is not so easily guaranteed, but the conditions for peace on the continent are better than today's ghastly headlines would suggest. Several of the large-scale conflicts that have ravaged the continent are over or nearly so. The end of apartheid has ended confrontations throughout Southern Africa. Mozambique and Namibia are at peace, and in Angola, the fighting is subsiding. Relations between Uganda, Kenya and Tanzania are better than at any time in the past 25 years. Ethiopia's 30-year civil war has come to an end with Eritrean independence. The ongoing disasters, such as in Liberia, Rwanda and Somalia, would be better contained if the West were willing to provide modest support to African-based peacekeeping efforts.

"Easy taxes" are well within the ambit of the IMF and World Bank. But here, the IMF stands guilty of neglect, if not malfeasance. African nations need simple, low taxes, with modest revenue targets as a share of GDP.

Easy taxes are most essential in international trade, since successful growth will depend, more than anything else, on economic integration with the rest of the world. Africa's largely self-imposed exile from world markets can end quickly by cutting import tariffs and ending export taxes on agricultural exports. Corporate tax rates should be cut from rates of 40% and higher now prevalent in Africa, to rates between 20% and 30%, as in the outward-oriented East Asian economies. As a rule of thumb, marginal tax rates of any kind higher than 20% will surely be evaded, and will open festering wounds of corruption. Simple tax schemes--such as low and uniform tariff rates of around 10%--vastly simplify administration, and are likely to raise government revenues in the process.

Remarkably, the IMF often stands against tariff reduction and simplification. Looking at spreadsheet calculations rather than reality, IMF missions frequently insist on packages of higher tax rates combined with "improved tax administration" to satisfy overly-ambitious revenue objectives. The Fund should know better than to urge Mozambique, whose income is $100 per head, to collect 23% of GDP in government revenues, especially when the current tax system is already haemorrhaging with evasion, corruption and maladministration. The Fund has since backed down, slightly. But it might note that the American federal government has never aimed to collect as much as 23% of GDP in revenues.

Adam Smith spoke of a "tolerable" administration of justice, not perfect justice. Market liberalisation is the primary key to strengthening the rule of law. Free trade, currency convertibility and automatic incorporation of business vastly reduce the scope for official corruption and allow the government to focus on the real public goods--internal public order, the judicial system, basic public health and education, and monetary stability. A vastly simplified reform agenda, then, is essential to improved government performance.

Governments should concentrate on setting ambitious growth targets founded upon openness to trade and should pursue them by making conditions comfortable for new exporters, domestic and foreign. That means keeping currencies convertible and depreciating them when necessary to protect the profitability of the emerging export sectors. Trade policies should guarantee, above all, that exporters have ready access to capital goods and intermediate inputs at world prices. Export-processing zones for labour-intensive manufacturing are especially helpful here. And tax policies should offer generous terms for all investors, whether domestic or foreign.

All of this is possible only if the government itself has held its own spending to the necessary minimum. The Asian economies show how to function with government spending of 20% of GDP or less (China gets by with just 13%). Education can usefully absorb around 5% of GDP; health, another 3%; public administration, 2%; the army and police, 3%. Government investment spending can be held to 5% of GDP but only if the private sector is invited to provide infrastructure in telecommunications, port facilities and power. Fortunately, foreign investors are lining up for such project financing, even in less dynamic Africa. To the extent that foreign investors can help, African governments themselves should typically focus on road-building, especially roads to connect rural areas to national markets and international ports. This is especially vital in Africa, where much export-led growth should come from smallholder agriculture--such as cotton in the Sahel, tea in Kenya, tobacco in Malawi--and often in rather remote areas.

This fiscal agenda excludes many popular areas for government spending. There is little room for transfers or social spending beyond education and health (though on my proposals, these would get a hefty 8% of GDP). Subsidies to publicly-owned companies or marketing boards should be scrapped. Food and housing subsidies for urban workers cannot be financed. And, notably, interest payments on foreign debt are not budgeted for. This is because most bankrupt African states need a fresh start based on deep debt-reduction, which should be implemented in conjunction with far-reaching domestic reforms. The precedents for deep debt-relief are notable and growing, starting with Germany in 1953 and Indonesia in 1969, and now including Poland, Egypt and many others.

Can aid support growth?

Here we reach the last element needed to make Africa grow: aid. Foreign aid, notoriously, has not made much difference in Africa. It has sometimes delayed reform and has sometimes been irrelevant. Aid works only when it is limited in time (and thus is not a narcotic), and is part of an overall market-driven growth strategy. Both conditions have been lacking: aid has become a way of life for many countries, and IMF-

World Bank programmes have rarely constituted a growth strategy.

Before public support for foreign assistance is undermined entirely by cynicism and fatigue, it must be recast along workable principles. First, aid should be much more selective. It should go only to those countries taking strong measures to promote market-based, export-led growth. Second, aid should be limited in duration. It can help reform-minded governments pay their bills during the initial period of reform; it cannot substitute for exports or growth in the longer term. It is hard to see why any balance-of-payments support should extend beyond another decade, and many aid programmes should be phased out sooner. A pre-announced sliding scale of aid--generous at the start, declining later--would concentrate the minds of African policymakers wonderfully.

Part of the assistance should come in the form of debt cancellation. No one can doubt the dreadful policy errors of the past, nor the mutual complicity of African and donor nations. A fresh start requires a thick line drawn under the past. As with other forms of assistance, debt cancellation should be deep, phased over time, and conditional on fundamental reforms.

The richer countries would do well to reorient a significant proportion of flows to regional assistance programmes, in support of public goods beyond the reach of individual African countries. For example, the World Bank and World Trade Organisation should take a special interest in landlocked countries--born with a strike against them--to help guarantee safe, secure and efficient access to ports. Donors would do well to bolster the more challenging public good of regional peace, by giving greater and more timely financial backing to regional peacekeeping operations. Finally, science and technology (especially in public health and agro-industry) could usefully be supported at the regional level.

The biggest source of support from donor nations would also be the cheapest. America, Europe and Japan should launch a "New Compact for Africa", guaranteeing open markets for African exports and committing themselves to help reintegrate Africa into the world economy. The commitment would help prove to both sides that the long period of economic marginalisation is over, and would energise both African nations and the West to overcome the practical obstacles to a new dawn of rapid growth throughout Africa.

THE AFRICAN SHORTFALL

GDP growth per person in Africa, 1970-89	0.2
GDP growth per person in 8 fast-growing economics	3.4
Difference	-3.1*
Expected difference**	1.4
Overall shortfall	-4.5
Accounting for the shortfall	
Lower openness	-1.8
Lower savings rate	-1.9
Lower market efficiency	-0.9
Adverse structural factors:	
Lack of market access	-0.3
Resource dependence	-0.2
Total explained shortfall	-5.1
Unexplained residual	0.5*

Source: Sachs & Warner *Due to rounding **Given lower income in Africa.

Food production per person

AFRICA	-11.3
LATIN AMERICA	31.4
ASIA	70.6

SOURCE: FAO

GRAPH: Africa's failure

PHOTO (BLACK & WHITE): Jeffrey Sachs

ILLUSTRATIONS

Jeffrey Sachs is the director of the Harvard Institute for International Development, which is currently pursuing research and advisory projects in 20 African countries. He advised the Bolivian, Polish, Russian and other governments on their economic policies, and his outspoken criticisms of the IMF made him a prominent figure in the debate on western aid to reforming countries.

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