GLOBALISATION AND THE AFRICAN STATE

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Introduction

Allow me first to thank you for inviting me to address you today. Since I was appointed Minister of Finance in 1996 the question of economic governance in both its international and domestic guises has been one of my preoccupations. That preoccupation has arisen as a direct result of the reintegration of the South African economy with the global economy, which has created for us unprecedented challenges in addressing the various pressures, risks and opportunities that derive from integration, and more broadly globalisation, and also because economic governance is central to my work on building the foundations for more rapid economic growth in the Southern Africa region.

Nancy Birdsall describes the debate on globalisation as being fundamentally about who's running the global economy and in whose interest. She argues that while most economists, finance officials and central bankers agree that the benefits of global, market-based integration can more than offset the costs for the poorest countries and the poor within countries, most social activists in contrast point out that so far, this potential has not been realised. That is the challenge we face today: to translate the potential benefits of globalisation into real, tangible gains for the poorest in the world. [Nancy Birdsall, "Why it matters who runs the IMF and the World Bank", Center for Global Development, January 2003]

Globalisation presents a critical challenge to sound economic governance in all states, and in particular African states. I want to speak today about how globalisation interacts with three systemic fragilities in Africa - the role of the state in growth, regional African institutions and the relationship between Africa and the 'North'. Finally, I will turn to the current African approaches to these problems and how they link with global economic governance.

The challenges that face the African continent are immense. The gross domestic product of Spain is roughly equivalent to that of Africa as a whole. Approximately one in two people on the African continent survives on less than $1 per day. A more disturbing statistic is the one provided by William Easterly in a paper that I will return to later: the GDP per capita on the African continent in 1998 was the same as the GDP per capita in 1960.

Historical context

For centuries under colonialism, the economic system imposed on Africa was one where raw materials were extracted, taken to Europe, processed and resold to the colonies. Labour too was drawn from the continent in significant quantities. The fact that a fair price was not paid for these 'exports' would be putting it mildly. In the post-colonial era, the prevailing economic relationships changed very little. Africa exported raw materials at prices it had very little influence over to the North and imported finished products. To pay for these imports, African states were given large amounts of credit. Aid flows, in many

but not all cases, have reinforced this dependency paradigm. Even today, Africa exports its raw materials and brainpower.

For over five hundred years, the economic system on the African continent did not foster the development of an industrial base and did not allow intellectual capital to be nurtured. While many would argue that in the post-colonial era poor governance and bad policy choices on the continent played a major role in crafting the present economic scene, there are just as many who would argue that it is the structure of power relations between coloniser and colony that fostered the creation of elites that plunder, of states that are powerless and of political systems built on patronage.

The African state

In part, globalisation presents risks to Africa because the apparatus of the state in most African countries is weak, but also because few African states have managed to find the right mix of policy to sustain rapid economic growth and poverty reduction.

In that context of inconsistent growth and widespread poverty, the globalisation challenge can tip states in the wrong direction - away from good governance, effective regulation, and pro-growth policies and toward rent-seeking, the stifling of the private sector, and the further weakening of already inadequate social policies and institutions.

At the same time, Africa has been slow to develop the sort of international institutions capable of assisting in the policy and sectoral adjustments needed to benefit from globalisation. Regional institutions and arrangements have also lacked the institutional capacity to offer external support to adjustment or to create the large-scale infrastructure projects to support market creation. And that weakness is often mirrored by the cautious approach of many African states to perceived losses of sovereignty incurred by regional integration.

In both of these areas, however, Africa is making great strides, as I shall discuss. The open question, and one which will influence global economic issues for decades to come, is whether further progress will be made on the creation of an international environment that is capable of supporting our efforts.

Globalisation and fragile economic growth

One of the larger challenges posed by globalisation is the extent to which governments need to adjust macroeconomic and/or microeconomic policies to achieve more rapid economic growth in an environment of open markets.

For African countries, that challenge assumes giant proportions. Most African economies retain fairly high trade barriers, largely due to weaknesses in revenue collection from other forms of taxation, whose reduction would require significant economic adjustment in the domestic economy. Public and private regulatory institutions and market structures are often not sufficiently developed and deep to weather the effects of poor policies and exogenous shocks. A good example is the impact of a cessation or sudden resumption of foreign aid - the size of these flows are globally miniscule - but locally massive - with predictable local economic effects.

Such imbalances are more destabilizing for African economies - because even small imbalances can disrupt thin markets, and because the adjustment process is often impeded, rather than facilitated, by the policy response.

In particular, adjustment processes usually place the burden of such adjustment on politically under-represented social groups, leading to an increase and perpetuation of poverty. Some marginalized groups become permanently locked out of economic opportunity, distorting the distribution of income, reducing the potential growth of the economy, and giving rise to political instability.

These considerations lead to a few tentative ideas. First, African economies will remain highly sensitive to the role of Multilateral institutions and donors - financial flows need to be handled delicately to avoid severe economic repercussions.

Secondly, that multilateral adjustment programmes need to be more holistically conceived than they are at present. Dani Rodrik has pointed out the importance for growth of microeconomic policies that facilitate the shifting of people from old and non-competitive industries to new industries and new forms of economic activity. Such policies entail assertive re-skilling, high quality education, and access to social and other forms of capital in open environments in which individuals can take advantage of new economic opportunities. [Dani Rodrik, "Development Strategies for the next century" February 2000]

Whilst William Easterly, in a paper entitled National Policies and Economic Growth argues that while economic growth is negatively affected by bad policies (an increase in deficits or inflation and the imposition of high trade barriers), the reverse effect is not necessarily true. He finds that there is no strong correlation between the pursuance of macroeconomic reform and growth. Countries reduce their deficits, lowered inflation rates and liberalized trade regimes did not necessarily perform better after the reforms. [William Easterly, "National Policies and Economic Growth: A reappraisal" Center for Global Development, May 2003]

Moreover, Shanta Devarajan (et al) finds that there is no positive correlation between public or private investment and growth in Africa. Similarly, aid flows have not had a discernable effect on growth either. They find that only eight out of 34 African countries had a positive relationship between aid and investment, with 12 displaying a clear negative relationship. Intuitively, this seems a strange finding. [Shantayanan Devarajan, William Easterly and Howard Pack, " Low Investment is not the Constraint on African Development" Center for Global Development, October 2002]

The evidence of policy failure in Africa is considerable. GDP per capita growth since 1980 has been lower than in the preceding 20 years. Yet, it was during this period where Africa privatised, liberalised and brought down deficits and inflation. John Nellis describes the case of Zambia. In what the World Bank in 1998 hailed as the most successful privatisation programmes in Africa, Zambia sold 90 percent of its' state owned enterprises. Since then, in just over a decade Zambia has had one of the largest reductions in industrial capacity ever observed. Factories have closed down, unemployment has risen and poverty is pervasive. [John Nellis, "Privatization in Africa" Center for Global Development, February 2003]

The Zambian case is not atypical. The general conclusion from his study of privatisation in Africa has been that where the regulatory capacity is weak, institutions immature and markets thin and where Governments lack the capacity to manage complex contracts, privatisation can worsen the economic environment, not strengthen it. The sequencing of policy reforms has not been given sufficient attention. Nevertheless, the multilateral financial institutions still focus on privatisation instead of building regulatory and institutional capacity and more appropriate sequencing.

Put differently, economic growth is not just a function of prudent macroeconomic policies (lowish deficits and inflation and manageable debt levels). Microeconomic policies that facilitate adjustment through the provision of social capital and opening up of economic opportunity - especially to the poor, are critical too. The difficulty is that such reforms are unlikely to be achieved by weak states, which can themselves be further weakened by large-scale financial assistance with tight conditionality. Not only are weak states incapable of defining and operationalising broader notions of public welfare, but they often have no interest in moving in that direction.

The challenge posed by globalisation is that as policy makers we must constantly grapple with the new pressures and changes in our environment - new areas of policy, new regulations and institutions all confront us every day. Occasionally, the pressures become very great and we do nothing, taking refuge in the sovereignty of our states and the threat of its loss as a means of defending our inaction.

Indeed many African communities hold too dear the idea of national sovereignty, perhaps because it is a relatively recent facet of our existence, but also - because like in all other communities - it is seen to be politically useful. Unfortunately, this has tended to slow the development of African institutions - even though the economic and political bases for their development are manifest in the weak level of trade between our economies, the lack of infrastructure, and our small size.

Building regional institutions

To overcome our aversion to regional and global institutions, it seems critical that we recognize that collective state action need not reduce sovereignty. Indeed, it seems to me that the European experience of integration suggests that national sovereignty may be enhanced through integration, despite the piecemeal loss of sovereignty in some areas. When applied to the pressures of globalisation, this thesis seems to me to hold even more strongly - globalisation can be addressed in regional and global institutions in such a way as to increase the power of states and better reflect the social and economic preferences of their citizens.

This idea seems especially pertinent in a regional context. Limited infrastructure, non-existent regulation or limited enforcement capacity, thin and undiversified markets for finance, goods and services all limit the extent to which African economies develop. The experience and practice across the continent is, of course, diverse. While some regions remain in low-level equilibria, others have made great strides in bedding-down policy, regulation, and macroeconomic stability, and are reaping the rewards of higher investment.

Despite international economic turmoil, economic growth in Africa is expected to average 3.1% this year and 4.2% next year. This is more than twice the average growth we achieved from 1984 to 1993, and marginally higher than the average for all developing countries.

Macroeconomic stability is being consolidated, with average consumer price inflation rising by about 9.7% in 2002, down from 13.2% in 2001, and 54.6% in 1994. Underpinning these improving inflation figures are our fiscal balances, which have declined from deficits of -5.2% of GDP in 1994 on average to deficits of -2.1% in 2001.

But we are unlikely to reap the rewards of more rapid economic growth with only macroeconomic stability. Growing our economies requires us to create and support effective regional institutions that are credible interlocutors for national governments. This means that they are backed by appropriate economic and political governance mechanisms, both internal to the regional institution and at the national level. They should be able to ensure public sector led provision of market infrastructure and foster the private sector. As the cornerstones of the African Union, Regional Economic Communities (RECs) must be strengthened to provide the framework for developing cross-border market infrastructure, addressing externalities, and forming common policies and regulations.

As in the context of domestic governance noted earlier, in this area weak states can be critical obstacles to progress.

I do not subscribe to the idea that either the institution of the state or the institution of the market can or should do everything in economic development. There are simply too many examples of failures of systems of paternalistic states and uncontrolled markets for me to accept either as a one-size-fits-all model for development.

Rather, our model is one of an active, accountable state, dependent on appropriate and non-distortionary revenue generation to provide the means for individuals to engage in economic activity in markets - and where people are unable or incapable of doing so, to provide a basic standard of living. That model depends in turn on well-regulated markets in which the private sector invests, produces, employs, and

competes. To my mind, that is a very special partnership, and one which informs New Partnership for Africa's Development (NEPAD), and in particular the move toward peer review and use of standards and codes in Africa. Such a state can work in partnership with the private sector to unlock rents, expand economic activity and reduce poverty.

Africa and global economic governance

Our experience, albeit short, with NEPAD and the African Union (AU) has been an enriching one. We have come together, as a continent; defined the broad tenets of good governance and of sound economic management and are building the institutions to support those who adhere to these principles.

The development of regional economic communities and of effective and accountable institutions, such as the Pan Africa Parliament and the African Peer Review Mechanism, will contribute to Africa's ability to address the pressures of globalisation.

In summary, NEPAD enables us as Africans to better manage what we get out of the international financial and developmental architectures, whilst pursuing domestic reforms aimed at maximising the benefits.

In combination with the finely structured NEPAD efforts, the international environment must become more supportive of our efforts in Africa and the developing world more generally. The failure so far to make significant progress in lowering agricultural subsidies and increase market access is a dismal reflection of global insecurities, and sours the commitments made in Monterrey and Johannesburg to do much more than trade reform.

Nonetheless, I want to conclude my talk with some comments on what increasingly seems to me to be a prerequisite for a supportive international economic environment. That is, to complete the reform of the international financial architecture that was given so much energy by the Asian crisis.

One of the key realisations in the aftermath of the Asian crisis (and reinforced by that of Argentina) was that domestic regulatory institutions and governance matter, not just for prevention of crises but also for their resolution and the recovery of the stricken economies. To get a handle on domestic weaknesses that make economies prone to crisis, it was important to engage more fully with governments and the national economic and regulatory systems they are responsible for. For that reason, and others, a range of emerging market economies were invited to the discussions on prevention and resolution and helped in the formulation of new codes and standards.

All of this has been immensely beneficial for the international financial system, the strengthening of regulatory and oversight functions in national systems, and the spreading of knowledge. Global economic governance, and hence reform of the international financial architecture, however, remains incomplete. We need a multilateral basis for overcoming future bouts of financial contagion - to maintain the connection between developing economies and international capital and goods markets and enable them to grow and reduce poverty.

The logical extension of the new role of emerging market economies and other developing countries would have been to reform the governance of multilateral institutions to enable them to take part in the decision making of those bodies. Not only would this strengthen reform efforts, and thereby reduce the contingent costs of future crises, but it would also strengthen the legitimacy of those institutions in other parts of the developing world.

Instead we are left with multilateral institutions, which, despite the impressive efforts of their staff, are experiencing a degradation of their legitimacy because of their governance structures

The very tools and instruments that the world has to address poverty and inequality and poor governance are themselves the subject of scrutiny in the field of representivity. If the World Bank, IMF, World Trade Organisation, Financial Stability Forum and the Bank for International Settlements do not represent the voices of the poor and marginalized, are they unlikely to correctly analyse the policy choices that can be used to address the concerns of the poor and marginalized.

Stephany Griffith-Jones outlines three compelling reasons for the voice of the poor to be given a platform in our multilateral institutions through a greater say by developing countries. First, she correctly points out that decisions taken do not reflect the perspectives of the majority affected by poverty. Second, calls for developing countries to improve their governance arrangements, expand democratic accountability and protect the marginalized are likely to fall on deaf ears if the proponents themselves lack representivity. Lastly, the voting arrangements in many of these institutions do not reflect the current global economic environment. Rather, they reflect a picture of development that is 60 years old. [Stephany Griffith-Jones, Improving the Voice of Developing Countries in Governance of International Financial Institutions, Unpublished?]

Firm proposals have been put on the table. The issue of voice was discussed at the annual IMF and World Bank Spring meetings in 2002 and in Monterrey, Mexico. The dilemma is to balance the need to maintain the support of the rich nations with the ability to remain credible, legitimate and relevant.

In a world of volatile capital flows, powerful financial markets, and destabilizing macroeconomic policy decisions, it seems only a matter of time before the major financial contributors to the IMF and World Bank recognise the prudential character of reform, as financial costs grow ever higher.