Governance and Growth in Africa

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Growth in Africa

A number of African countries have registered moderate to high growth rates over the last decade

In some cases African countries have benefited from the commodity boom

But in other cases there has been some expansion of agriculture and industry as in Uganda and Ethiopia

However, many African countries still suffer from low growth and there is a danger that growth is vulnerable in the high-growth African countries

Growth in Africa

The new consensus is that ‘good governance’ will help all these countries achieve sustainable growth strategies

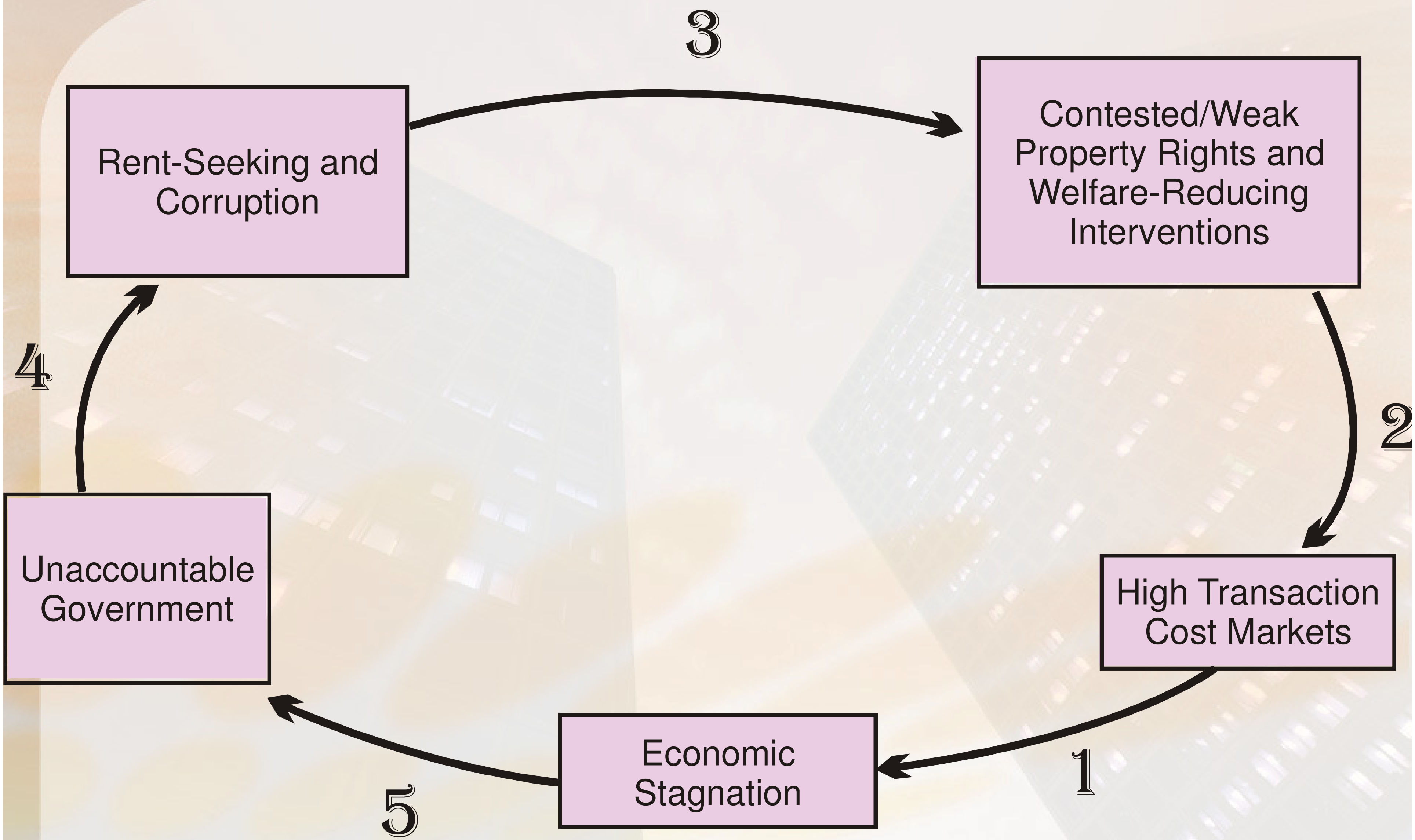
Interventions to correct market failures were often unsatisfactory in poor countries because of weak implementation capacities

The new approach is to address market failure at a higher level by reducing market transaction costs through good governance reforms

Stable property rights, rule of law, anti-corruption, government accountability are not just *goals* of development, they become *preconditions* for development

Unfortunately, the implementation requirements for the new agenda are if anything even more ambitious

Key Components of the Good Governance Agenda



But good governance is not easy to achieve

Property rights only become ‘stable’ with the emergence of productive asset owners who can pay for the protection of their assets.

Fighting corruption requires
- legal sources of finance for running politics,
- a budget large enough that redistributive demands can be met through the budget, and
- the conversion of illegal rent seeking into legal rent seeking requires that critical rent seekers are legitimate

Accountable electoral politics emerges when parties can offer enough to broad constituencies through the budget

Good governance is desirable but…..

This does not mean that improvements in good governance are not achievable at all in developing countries

Improvements are both possible and desirable

The question is whether the *feasible* improvement along this path can be significant enough to make a significant impact on transaction efficiency within a policy period

If the feasible improvement in ‘good governance’ is small, then we have to look for *other* governance reforms to achieve improvements in resource mobilization and the efficiency of investment allocation

The historical evidence from case studies shows that this is exactly what successful developers did

The Asian experience: Governance capabilities that matter

	Property Rights	Rents and Rent seeking	Political Stabilization
Dynamic Transformation States	Protection, creation and transfer of rights to *productive* groups Destruction or loss of rights of *unproductive* groups (ex post flexibility)	Business-government relationships allow emerging entrepreneurs to engage in catching-up strategies (effective rent management capabilities)	Provides sufficient systemic stability *and* allows productive outcomes in property rights and rents
Slow or Unsustainable Transformations	Protection and transfer of rights to *unproductive* groups Destruction or loss of rights of *productive* groups (absence of capabilities to discipline politically powerful)	Political interests and weak institutions protect *growth-reducing* rents AND fail to protect or manage *growth-enhancing* rents (state lacks capabilities to prevent rent capture)	Fails to maintain systemic stability *or* results in damaging property rights or rent outcomes

Political conditions and growth enhancing governance

The identification of governance priorities cannot just be based on governance goals that make sense in theory but has to be based on the feasible capabilities of a state to enforce specific rules

These capabilities are built up over time: Looking at any model of East Asian or any other governance story as an end product is misleading because this ignores the process through which these governance structures emerged

Moreover initial conditions differ significantly between countries including Asian countries so that their growth strategies and governance structures are also significantly different

Contemporary analysis suggests several false dichotomies between African and Asian political economy (Medard's neo-patrimonialism, Chabal and Daloz's institutionalization of disorder, the role of ethnic fragmentation or Hyden and Williams' economy of affection)

A ‘Hirschmanian’ Approach to Governance Reforms

Hirschman’s observation about project implementation was that success depended on entrepreneurial skills to solve problems that had not been foreseen

Rarely did ex ante analysis identify true costs and benefits: this is also why the current fashion with identifying ‘binding constraints’ gives a false sense of scientific validity to an exercise that yields different results for different analysts

For most late developers today, a pragmatic approach would be to identify a small number of areas where growth enhancing governance reforms could be implemented to overcome specific market failures

Pragmatic Approaches to Market failures

From the perspective of governance reforms the scarce resource is the political capacity to implement and enforce

It therefore makes sense to select a number of reasonably obvious starting points for capacity building in terms of challenges faced by growth sectors in the country

The critical condition is that the priorities for capacity building should be selected in such a way that the ‘entrepreneurial reform capacity’ is focused in these areas and exit can be assured if results are not satisfactory

A number of obvious market failures can constrain investment in new technologies and slow down productivity growth

Capital Market failures

Learning and adapting new technologies involves financing losses for periods that are not known in advance

The good governance route is to improve the rule of law and rely on private contracting (for instance stock markets and venture capital)

A pragmatic approach would be to focus on a small number of financial instruments (capital cost subsidies or equity participation by government) to critical investors

The challenge is to build institutional and governance capacity to manage these properly with clear exit options

Labour Market failures

Underinvestment in training (both within firms and in training institutes)

Good governance is trying to create conditions for better contracting between the different parties

Subsidies for training could be the answer but in the absence of governance capabilities, subsidies can also be wasted with no useful outcome

Some problems can be reduced through careful design of the subsidy: for instance subsidizing loans taken out by workers is less likely to be captured than subsidies to training institutes

But in each case monitoring and evaluation capacities have to be developed and clear exit criteria

Land Market failures

Property rights are typically not clearly defined resulting in problems in land acquisition for new projects and expansion of existing projects

The good governance strategy is to clarify these rights and achieve a rule of law and low corruption

A pragmatic strategy would be to develop clearly defined land agencies tasked with identifying and acquiring land for industry (or agriculture), developing politically acceptable compensation schemes, and linking land up with infrastructure providers

The initial scale could be very small if governance capacities are limited, better to achieve a small well working industrial cluster than an ambitious strategy on paper