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Domestic Resource Mobilization and Developmental States

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Chapter 3

Towards a "developmental State"

A. Introduction

Despite the ritual implementation of SAPs over the past quarter century, many African countries have yet to experience sustained and robust growth rates high enough to ensure the attainment of the MDGs by the target date. The collapse in both savings and investment continued unabated, until recently. A breakdown in physical infrastructure, combined with a weakening of state capacity to carry out basic public management functions through SAP-induced retrenchment and de-industrialization, increased the size of the informal economy. The continuing lack of diversification of many sub-Saharan African economies also meant that the region's vulnerability to adverse external factors such as commodity price fluctuations did not diminish, and in several cases has rather increased, within the context of trade liberalization.

Since the mid-1990s, several countries have experienced moderate but sustained growth in output. But this growth has been episodic, and in many cases driven by favourable weather (good rainfall) and external environment (mainly high commodity prices), as well as debt relief (within the framework of the Heavily Indebted Poor Countries Initiative) and, since 2000, increased volumes of aid. Considering that macroeconomic stability is the most notable achievement of SAPs, questions are now being asked how the continent could capitalize on this, and also on the newfound mood for democratic dispensation, in order to consolidate economic growth as a means of embarking on a path of sustainable development.

This chapter attempts to map out the common elements of developmental States and examines their applicability (or non-applicability) to Africa. It argues that the necessary ingredients are in place for African countries to tackle their development challenges within the framework of a "developmental State". Increased domestic resources complemented by augmented aid flows are unlikely to provide an escape route from Africa's underdevelopment without a fundamental shift in policy orientation away from the neoliberal stalemate. This is perhaps the only means by which Africa could break into manufacturing

export, a strategy developed by almost all benchmark countries (see, for example, Johnson et al., 2007).

B. The developmental State: concept and characteristics

Origins of the concept

The extraordinary economic performance of a group of developing economies in East Asia since the 1960s, which came to be labelled as the first- and second-tier newly industrializing economies (NIEs),[32] has attracted competing explanations. The conventional view attributes the rapid economic development of these economies to trade liberalization and associated export promotion. It contends that the rapid growth of these economies was triggered by market-led outward-oriented development strategies that ensured optimal allocation of resources (see, among others, Fei and Ranis, 1975; Myint, 1982).

In a comprehensive study of these economies, the World Bank was more cautious in its conclusions, to the point of fudging the issues at stake. It identified "market-friendly" policies as part of the policy menu of these countries. At the same time, the Bank acknowledged the role of government policies in the areas of skills acquisition, technological progress, and financial and labour markets (World Bank, 1993). Not surprisingly, therefore, the Bank has been accused of falling prey to the traditional dichotomies of "States versus markets" and "export-oriented versus import substitution", an attitude which is symptomatic of the reluctance or the unwillingness of conventional economists to acknowledge the contributions of heterodoxy to the development debate (Akyüz et al., 1998).

To the non-conventional (heterodox) school, the performance of these countries is underscored by strategic development and industrial policies that derive from a symbiotic relationship between the political and bureaucratic elite and entrepreneurs. A variety of interventionist measures was used to direct resources away from old to new industries in order to alter their long-term development trajectory. The government–business relations that were critical to the success of this strategy were mediated through various institutions and policies. This ensured that subsequent "economic rents" were marshaled to address the objective of rapid economic growth. The institutional and policy framework of these countries also supported their strategic and systematic integration into the

global economy (Amsden, 1989, 1991; Wade, 1990; UNCTAD, 1996a, 1997; Akyüz et al., 1998).

The concept of "developmental States" emanated from this last insight into the performance of NIEs, and as such has become associated with the history of development in East Asia. It incorporates a simultaneous and specific combination of economic, political and institutional structures, which have been used heuristically to elucidate the phenomenal economic growth in the NIEs (Sindzingre, 2004). Nevertheless, not all observers who subscribe to this account have the same perspective on the political and economic philosophy, let alone the role of institutions, that underpin the "economic miracle" of the NIEs. Whilst there is some consensus that the NIEs commonly share some characteristics, some analysts are quick to point out that there are important differences between the institutional and policy framework of the first- and second-tier NIEs, as well as among individual countries (see, for example, UNCTAD, 1996a, 1997; Akyüz et al., 1998; Culpepper, 2006).

Various attempts to explain the 1998–1999 Asian financial crisis have also exacerbated the competition among the different explanatory claims. The crisis exposed some of the weaknesses of these economies and triggered a reassessment of the policies, as well as of the concept of the "developmental State" itself. Does "developmental State" contain the seeds (corruption, cronyism, directed credit, fragile financial systems, including weak prudential regulations) of its own destruction, as suggested by the "counter–literature" of neoliberals? (See, for example, Suehiro, 2001.) Have the NIEs simply fallen victim to the ineluctable and destructive forces of globalization and the greed of speculators? Or, as argued by some observers (see, for example, UNCTAD, 1998a, 2000b), did the NIEs simply lose the "Midas touch" and not display the same cautious approach to capital account opening as they did to trade liberalization? Irrespective of our responses to these questions, the fact is that these countries have some useful lessons (positive or otherwise) for other poor developing countries, especially those in sub-Saharan Africa.

Characteristics

The literature distinguishes the developmental State from "non-developmental States" by both its ideology and structure. The ideology of the developmental State is fundamentally "developmentalist", as its major preoccupation is to ensure sustained economic growth and development on the back of high rates

of accumulation, industrialization and structural change. Structurally, such a State has (or develops) the capacity to implement economic policies that effectively deliver development, which in turn gives it legitimacy. This capacity is derived from a combination of institutional, technical, administrative and political factors. It is a "strong State" that enjoys autonomy from social forces that might otherwise dissuade it from the use of its capacity to design and implement polices that are in its long-term interest. At the same time, it develops some "social anchoring" that prevents it from the use of its autonomy in a predatory manner, which is what secures it the approval of key social actors (see Castells, 1992; and Myrdal, 1968 in Mkandawire, 2001: 290). Thus, what makes the developmental State effective is not just autonomy, but "embedded autonomy", in which the State is immersed in a network of ties that bind it to groups or classes that can become allies in the pursuit of societal goals (Evans, 1995).

Mkandawire contends, however, that this definition of a developmental State is misleading, as it equates "success" to the strength of the State, whilst measuring this strength by the presumed outcome of its policies. It also emphasizes success at the expense of the "trial and error" nature of policymaking, which is an important feature of even the most successful developmental States. Indeed, in a developmental State, there must be some room for poor performance stemming from "exogenous factors, miscalculation or plain bad luck", as indeed was the case with African developmental States from about the mid-1970s. Therefore, a developmental State is "…one whose ideological underpinnings are developmental and one that seriously attempts to deploy its administrative and political resources to the task of economic development" (emphasis in the original) (Mkandawire, 2001: 291). The ideological underpinnings of state policies are crucial, as these provide the rationale for some of the policies, give legitimacy to some of the sacrifices that might otherwise not be welcome, and bind the ruling class together (Mkandawire, 2001).

UNCTAD's research on the East Asian NIEs[33] reveals that, although there were noticeable differences in these economies, common features could also be identified. The policy and institutional reforms were all implemented simultaneously. However, there are considerable differences between the first- and second-tier NIEs. In particular, the policies of the latter group resulted in competitive resource-based and labour-intensive industries. Most importantly, this research underscores three characteristics which are crucial to the success of the NIEs and therefore critical in the analysis of developmental States. Firstly, institutional reforms and policy interventions revolve around a "profit–

investment nexus", an accumulation dynamic, which is critical to the growth process. Secondly, there are close and interdependent linkages with exports – an "export–investment nexus". Finally, the process of managing "economic rents" ensures their beneficial impact on the development process. In their analysis, Akyüz et al. (1998) suggest that these three principles are more common in the development strategies of the first-tier NIEs (that is, including Japan but excluding Hong Kong, China; see box 1 for a detailed discussion of these principles).

Cleary, this analysis of the development experience of the NIEs (see box 1), indicates that neither the "market" nor the "State" can by itself deliver the ultimate goal of development. The real path to sustainable growth and development emanates from a pragmatic mix of markets and state action, taking into consideration the country-specific development challenges. The experiences of the NIEs, nevertheless, point to some common characteristics of developmental States.[34] Active development strategies, in particular industrial policies, are at the heart of the success of these States in "creating winners" rather than "picking winners". Clear policies and goals are set for the economy in terms of export promotion, investment in human capital and credit allocation via state development banks. Issues of economic coordination were addressed through innovative measures, whilst efforts were directed at minimizing bureaucratic failure (Amsden, 2001). Industrialization was driven by learning processes, borrowing of technology and an array of policies, including targeted taxation, protection, restrictions on foreigner shareholding, financial sector policies that revolve around directed lending, a skilled and educated labour force, including training in the civil service and in technology at tertiary levels, and the development of infrastructure. This is what accounts for differences between Asia and Africa in terms of gross domestic expenditure in research and development and the intensity of that research and development (the ratio of gross domestic expenditure in research and development as a ratio of GDP), which persist today (see table 4). All of these are underscored by long-term relations between political powers and the private sector, and between the banks and public and private firms – the so-called "alliance capitalism". Typically, heterodox economic policies, such as state intervention (targeted on growth) and political rent-seeking, were subjected to market discipline.

Flexibility was built into long-term industrial strategies, whilst short-term, rigid, regulatory measures promoted the strengthening of institutions. Technocratic autonomy was given primacy over political power, although it was embedded in society, as well as in private sector and industrial networks. The strengthening of

Box 1

Newly industrializing economies: dynamics of capital accumulation, export–investment nexus and rent management

The role of capital accumulation in the process of growth and development is reflected in the emphasis on the "profit–investment nexus" in the development strategies of the NIEs. This explains the phenomenal rise in savings and investments in these economies from very low levels in the 1950s. The ratio of gross national savings to GDP, for example, increased dramatically, from around 3 per cent (1951–60) to almost 35 per cent in the early 1990s in the Republic of Korea; from about 10 per cent to 27 per cent in Taiwan Province of China; and from 9 per cent to 34 per cent in Hong Kong, China over the same period. There were also corresponding increases in the ratio of gross domestic investment to GDP over the same period: 10 per cent to 37 per cent in the Republic of Korea; 16 per cent to 23 per cent in Taiwan Province of China; and 9 per cent to 28 per cent in Hong Kong, China (see table 3).

By maintaining political stability, these Governments created a "pro-investment" macroeconomic environment with occasional tolerance towards some degree of inflationary pressure in order to boost investor confidence. When restrictive measures became necessary as a means of balancing national economic development goals, consumption, rather than investment, was first sacrificed. Strong incentives were introduced to boost profits above free-market levels through a variety of fiscal instruments,[a] whilst trade, financial and competition policies[b] were used to create "rents" that boosted corporate profits and therefore the potential investible resources available to corporations. These measures encouraged corporate savings, which in turn boosted capital accumulation. A combination of these incentives (and disciplinary measures)[c] created and sustained a dynamic profit–investment nexus: high profits increased not only the incentives of firms to invest, but also their capacity to finance new investments, and higher investment raised profits by enhancing rates of capital utilization and the rate of productivity growth.

An integral part of East Asian development strategy was policy measures that link the profit–investment nexus to the "export–investment nexus". This is in recognition of the fact that developing countries need not only master off-the-shelf technologies, they must also enhance their competitiveness in mature product markets with established firms.[d] In effect, it is not just the volume or level of investments that is important; the sectors in which these investment are made are equally if not more important.

Investment promotion measures were implemented as an integral part of measures to establish domestic capital and intermediate goods industry and technological upgrading. They were also implemented with other policies, such as a re-institution of import controls, rolling back tax exemptions on the import of some intermediate and capital goods, and granting higher investment tax credits to businesses buying domestically produced machinery. These were combined with polices that enhance technological capacity at the national, industry and firm levels, and tax and other incentives for enterprise training, which were implemented as an integral part of national training programmes. These programmes emphasized technical subjects at higher levels of education and the involvement of industry in vocational training schemes, alongside measures to facilitate local research and development, including direct financial subsidies. A critical link in the process of industrial upgrading was the transfer and adaptation of foreign technology (see table 4).

Box 1 (contd.)

The integration of these economies into the global economy was gradual, strategic and tailored to meeting specific sectoral requirements, which were sequenced in accordance with the level of industrial and economic development. Similarly, the principle of strategic integration was applied to technology transfer. In those sectors in which FDI played a big role (such as textiles and electronics, for example, in Japan, the Republic of Korea and Taiwan Province of China), government policy was vital in promoting joint ventures, screening imported technologies and bargaining over local content requirements. Direct government support was crucial to the process of integrating transnational corporations in a national industrialization strategy.

Of all the unorthodox policies in the development arsenal of the East Asian economies, creating and managing economic rents was probably the most contentious and risky. This is because rents, if not managed properly, could become permanent and not only weaken entrepreneurship but also smother productivity growth in the long run. In the light of these dangers, it was ensured that policies and institutions that created the initial rents to kick-start a development process were eventually withdrawn. Recipients of rents were expected to conform to international market-based disciplines, as they had to meet a combination of performance criteria such as export targets.

A variety of factors was crucial to the successful management of economic rents and in boosting domestic savings, investment and exports (see table 3). Firstly, a strategic alliance with common developmental goals was forged between Government and business institutions, and pivoted on an efficient and meritocratic civil service. Secondly, the evolution and organization of a domestic entrepreneurial class in the form of large diversified corporate groups and conglomerates (as in Japan and the Republic of Korea) and large state-owned enterprises (as in Taiwan Province of China), were important in ensuring the successful outcome of these policies. Thirdly, the process of industrial development spawned a series of formal and informal links with the entrepreneurial class that facilitated the implementation and coordination of policy measures. Finally, institutional links between corporations and banks contributed to the establishment of an improved investment regime. One expression of this was the socialization of risks through state–owned, bank–based lending and state direction of the financial sector as a means of addressing financial sector imperfections.

Source: Akyüz et al., 1998. See also UNCTAD 1996 and 1997.

a Tax exemptions and special depreciation allowances were applied across the board, but also targeted specific industries as a means of supplementing corporate profits and encouraging profit retention as a means to accelerating capital accumulation.

b These included a range of selective protection policies, interest rate controls and credit allocation, managed competition (including the encouragement of mergers), coordination of capacity expansion, restrictions on entry into specific industries, and the screening of technology acquisition, among others.

c A variety of measures was deployed to discourage luxury consumption by potential investors as well as to eliminate speculative investments based on arbitrage, for example, and to restrict the outflow of capital during the initial stages of development.

d As developing countries operate within their production possibility curve, supporting industrial development requires increasing the propensity to invest and promoting movements along existing learning curves.

Table 3

Gross national savings, gross domestic investment and exports in the Asian NIEs and Africa, 1971–2005

(Per cent of GDP)

	Gross national savings					Gross domestic investment					Export of goods and services				
	*1951-1960**	*1971-1980*	*1981-1990*	*1991-2000*	*2001-2005*	*1951-1960**	*1971-1980*	*1981-1990*	*1991-2000*	*2001-2005*	*1951-1960**	*1971-1980*	*1981-1990*	*1991-2000*	*2001-2005*
Hong Kong SAR, China	9.2	30.9	31.8	31.5	31.4	9.1	26.6	27.0	29.0	22.6	..	86.7	110.8	134.6	169.4
Taiwan Province of China	9.8	..	..	..	..	16.3	30.4	22.8	23.9	19.1	9.6	46.3	53.2	46.6	56.2
Indonesia	..	..	26.7	26.1	27.2	9.2[a]	19.3	29.2	26.2	22.8	13.6[a]	23.2	24.2	31.6	33.2
Korea, Republic of	3.3	23.7	31.5	35.8	32.1	10.0	29.0	31.0	34.2	29.8	2.0	26.4	33.5	32.1	39.5
Malaysia	23.2[b]	..	27.9	35.0	34.0	15.3[a]	24.9	30.9	34.7	22.4	51.4[a]	47.7	59.7	96.2	117.8
Singapore	-	28.8	41.8	48.9	40.0	11.4[a]	41.2	41.2	33.8	20.8	-	156.2	292.2	177.3	214.2
Thailand	15.3	22.7	26.6	33.4	30.0	13.5	28.5	30.7	33.5	26.3	18.3	19.8	26.9	46.3	68.0
Africa	..	..	16.2	15.2	17.9	..	22.4	20.4	21.0	20.3	..	27.5	24.1	27.2	34.9
Sub-Saharan Africa	**..**	**23.5**	**17.5**	**14.4**	**16.4**	**..**	**21.4[c]**	**19.5[c]**	**21.0[c]**	**20.1[c]**	**..**	**26.0**	**23.7**	**28.1**	**35.7**

Source: World Bank, *World Development Indicators*, online, May 2007.

a 1960 only.

b Including Singapore, which became independent in 1963, having enjoyed self-government between 1955 and 1963.

c Gross domestic investment for sub-Saharan Africa (excluding South Africa).

* Akyüz et al. (1998) from UNCTAD database.

institutions stimulated economic growth, which in turn strengthened democratic traditions and dispensation. While not often mentioned, social policies were an important ingredient in the arsenal of developmental States. These policies revolved around non-state entities such as families and firms, with the State guaranteeing the implementation of social welfare programmes. Finally, all these countries, with the exception of Hong Kong, China, were highly selective in their liberalization and export-oriented strategies, often ensuring the development of a competitive sector before opening it up (UNCTAD, 1996a, 1997; Akyüz et al., 1998; Wade, 2003).

The development process in the developmental States has been described as an institutional interventionist solution (to the problems of underdevelopment) pivoted on the principle of reciprocity. There is a "reciprocal control mechanism", whereby Governments provide assistance (e.g. subsidies) to the manufacturing sector, which then reciprocates by meeting a performance standard (e.g. export

target). Governments tried “getting the control mechanisms ‘right’”, rather than trying to get “prices right” (Amsden, 2001).

It is certainly difficult to be prescriptive in all these policy areas in attempting to identify a “replicable strategy”, if that were at all possible, for attaining a fast pace of development for poor developing countries, such as those in sub-Saharan Africa. However, in view of the pivotal role played by the financial sector in rapidly boosting domestic savings and in development strategies in the developmental States of East Asia, the sections below endeavour to identify some broad policy lessons for African countries. Considering that Africa probably faces much more severe constraints in the real sector, which contribute low total factor productivity growth than East Asia previously did, these constraints might have to be addressed first as a condition for efficient and effective use of credit.

C. Financial sector reforms: curbing government intervention to cure “financial repression”

Bringing about a developmental State necessitates (re)defining the roles for some of the State’s major institutions, or in some respects, adopting new ways of performing existing tasks. One such institution is the central bank, which was used by both early and new industrializers of all stripes to support their development strategies (see box 2). The need to rethink the role of the financial system or the banking sector in development in poor countries is nothing new. Financial sector reforms featured prominently in broader SAPs implemented by most sub-Saharan African economies beginning in the early 1980s. Financial sector reforms, particularly in the commercial banking sector, were grafted onto the main SAPs from about the late 1980s.

The main objective of these reforms was to address “financial repression”, low or negative real interest rates stemming from financial restrictions, mainly government policies that discourage savings and capital accumulation and optimal allocation of resources (McKinnon, 1973; and Shaw, 1973). The reforms therefore aimed at attaining a more effective, robust and deeper financial system via the introduction of market forces, to enable it to support the private sector as an engine of growth in these economies. At the heart of the reforms was the enhancement of the quality of financial services, underscored by positive real interest rates, in order to attain improved savings mobilization and credit allocation. Other objectives were to reduce government intervention in directing

Table 4
Mind the technology gap: East Asia and Africa

A. Technology: diffusion and creation, 1990 and 2004

	Telephone mainlines (per 1,000 people)		Cellular subscribers (per 1,000 people)		Internet users (per 1,000 people)	
	1990	*2004*	*1990*	*2004*	*1990*	*2004*
Developing countries	21	122	*	175	*	64
East Asia and Pacific	18	199	*	262	*	91
Latin America and Caribbean	61	179	*	319	0	115
South Asia	7	35	*	42	0	29
Sub-Saharan Africa	**10**	**	*	**77**	**0**	**19**
OECD	390	491	10	714	3	484

Source: UNDP, 2006.

* Greater than zero but small enough that the number would round to zero at the displayed number of decimal points.

** Data not available.

B. Gross expenditure on research and development (GERD) and research and development intensity/GDP, 1990 and 1999/2000

	1990		1999/2000	
	GERD (billions)	*GERD/ GDP (%)*	*GERD (billions)*	*GERD/ GDP (%)*
Developed countries	367.9	2.3	596.7	2.3
Developing countries	42.0	0.7	158.4	0.9
Latin America and Caribbean	11.3	0.5	21.3	0.6
Africa	**5.2**	**0.6**	**5.8**	**0.3**
South Africa	2.9	1.0	3.6	0.8
Other SSA countries	1.9	0.5	1.1	0.2
Arab States in Africa (N. Africa)	0.4	0.3	1.1	0.2
Asia	94.2	1.8	235.6	1.5
Japan	67.0	3.1	98.2	2.9
China	12.4	0.8	50.3	1.0
India	2.5	0.8	20.0	0.7
NIEs in Asia	8.2	1.6	48.2	1.7

Source: UNESCO, 2004.

credit or setting interest rates, and to increase competition contingent upon liberalized entry and/or removal of other competition-limiting regulations (see Brownbridge and Gayi, 1999).[35]

These objectives were enunciated in new banking legislation such as new financial sector or banking acts, which also re-emphasized the role of central banks as guarantors of the entire banking system through a strengthening of prudential regulation and supervision of banks. Banking supervision, monitoring and control were to be streamlined and improved by training of existing staff and new recruits to enforce new guidelines on higher minimum capital adequacy requirements, lending policies (e.g. which ban insider lending), regular on-site inspections and early intervention in distressed banks.

While the reforms emphasized the application of market principles in the banking sector, they were ambivalent about the independence of central banks beyond a reduction of the influence of Government on its operations, together with a more stringent enforcement of prudential regulation and supervisory requirements. They had far-reaching implications for commercial bank operations, and more importantly for the operations of "development banks", which were forced to comply with the new banking regulations if they took deposits. This led to the abandonment of the original development objectives of these banks. They were forced into short-term credit and service programmes, in contrast to their original objective of medium- to long-term finance[36] (Garson, 2006).

Overall, the reforms have, to different degrees (and with varying levels of success), made the financial sector of these countries more susceptible to the application of commercial principles in their deposit taking, lending and borrowing operations. The reforms are still ongoing in some countries, but the verdict to date suggests that they have not met their original objectives in several areas. Few innovative financial products have been introduced, oligopoly has frustrated competition, and whatever limited entry there has been into the financial sector is concentrated in the urban areas. In the context of privatization of previously state-owned commercial banks and the subsequent closure of the branches of these banks in rural areas, the new financial sector that has emerged from these reforms tends to induce commercial banks to set up in urban areas (now overserved) rather than in rural areas which are underserved, if served at all (UNCTAD, 1996b; Brownbridge and Gayi, 1999). The reforms also facilitated the entry of specialized financial institutions, including non-bank financial

Box 2
The role of central banks in development

The current conception of central banks is that they should be politically independent from Governments, with a functional focus on fighting inflation by means of indirect monetary policy instruments, such as short-term interest rates, to influence the level of economic activity. As Epstein (2005) points out, however, this notion represents only a partial reading of their history. Central banks of all persuasions (say, the Bank of England, the United States Federal Reserve and even the Bank of France and Bank of Japan) have historically all financed Governments, managed exchange rates, and employed various policy measures to support preferred economic sectors.a This was a mission in which all tools of direct monetary policy were considered legitimate, ranging from subsidized interest rates, legal restrictions and directed credit, to moral suasion to promote particular markets and institutions. The historical accounts of various central banks are replete with instances of their engagement in "industrial policy" or "selective targeting".

While central banking underwent dramatic transformation in the developing world in the aftermath of World War II, in the late 20th century these banks were used as agents of economic development more extensively in some developing countries than in developed ones. This was partly in response to the concern of Governments to be able to pursue monetary policy designed to promote more rapid economic development and to mitigate excess swings in national money incomes. Most central banks in these so-called "late industrializers" (including the NIEs) in the post-war period continued with their developmental role, i.e. with policies designed to develop their economies, such as selective credit controls, the creation of special credit institutions to cater to the needs of specific sectors (agricultural and industrial development banks), and redistribution of real resources between the public and private sectors. [b]

Some of these policies have been criticized in the last three decades or so, but it is not incorrect to say that central bank support for development in the "late industrializers" is a critical part of their development story. The role of finance, in particular mobilization and allocation of medium and long-term finance for industrialization, was pivotal in their development performance. The "development bank" model, sometimes with the whole banking sector "acting as a surrogate development bank", was deployed in particular to finance investments of targeted industries by channelling long-term credit[c] on concessionary terms. By keeping the effective real interest rates low (in some cases even negative), and using capital controls to keep out hot money[d] (and thereby avoiding overvalued exchange rates), central banks facilitated the realization of the specific development objectives of Governments. These policies were not always successful, but were critical in underscoring the level of economic development attained in these countries in a generation.

The current tendency is for neoliberals to argue that the role of central banks should be the stabilization of the economy by means of "inflation targeting". This assertion does not stand up to historical evidence with either the European early industrializers or in the Asian late industrializers. Historically, central banks have been most effective as vehicles of development (more so in the NIEs or the "late industrializers" than in the developed countries) when used to promote the industrial policies of Governments. The vexing issue is what sort of balance they should maintain between their developmental and stabilizing roles. In the context of poor developing countries, it may not be appropriate for central

Box 2 (contd.)

banks to redefine this developmental role as the promotion of "stock market-based" financial sectors.[e]

Sources: Brimmer, 1971, Amsden, 2001, and Epstein, 2005.

a The Bank of France and the Bank of Japan have deployed credit allocation to support industrial policy, whilst the Bank of England and the United States Federal Reserve have promoted the financial sectors of their economies consonant with the international role of their financial services industries (Epstein, 2005).

b This is particularly the case for China, India, Indonesia, the Republic of Korea, Malaysia, Taiwan Province of China and Thailand in Asia; and for Argentina, Brazil, Chile and Mexico in Latin America (see Amsden, 2001).

c Public finance for this was "off-budget" – non-tax revenues from foreign sources, deposits in government-owned banks, post office savings accounts and pension funds.

d These are inflows of speculative capital that flow out immediately at the least sign of any instability in host economies.

e There is little evidence that these sectors, which have been promoted in recent years in many developing countries, lead to faster growth or indeed more development (Epstein, 2005). To date, the history of stock market development in Africa is not encouraging. Most, if not all, of the 21 stock exchanges on the continent not only have low levels of liquidity and suffer from a lack of integration with regional and global markets, they also suffer from technological and capacity constraints (see UNECA, 2007: 7). And indeed, internal and external financial liberalization (capital account opening) as a means of promoting the development of the financial sector can make developing countries more vulnerable to financial market instability, as was the case in recent financial crises: the East Asian financial crisis of 1997–1998, the financial collapse in Russia in 1998, Brazil in 1999 and in 2002, the Central Asian Republics in 1998–2000, and in Argentina in 1995 and 2001–2002 (see, for example, UNCTAD , 1996, 1997; Griffith-Jones, 1998; Jomo, 2005; Khor, 2005; and Taylor, 2007).

institutions, although the closure of some "development banks" has left some financial service gaps (Garson, 2006). The biggest casualties of these reforms are the "development banks", whose objectives and mission are perceived to be incongruent with the underlying neoliberal rationale of reforms. Some of these banks were admittedly closed because of insolvency (see, for example, UNCTAD, 1996b; Brownbridge and Gayi, 1999). However, it is arguable if an entire policy should have been ditched because of this, or whether an attempt should have been made to restructure their assets, as was done in the case of some commercial banks through non-performing asset recovery trusts.

It cannot be denied that the emerging financial sector does not respond to the financial and developmental needs of African countries. Low levels of savings (held as financial assets) persist, even in those countries that have resumed growth since the mid-1990s. Worryingly, there is excess liquidity in the banking system, which suggests an inability to convert even the low levels of savings mobilized

into investments.[37] Whatever increase there has been in domestic investment, as discussed earlier, has been financed mostly by foreign capital, in particular the resurgence in ODA flows, but also debt relief (McKinley, 2005). There is therefore a need to re-engineer financial institutions in a way that addresses the specific developmental issues in African countries, that is, institutions that fill the void for term finance in the formal sector as well as the financing gaps for small and medium-sized enterprises and other firms in the informal sector. This will require complementary changes in monetary policy stances of individual countries. A starting point may be to revisit the role of central banks in order to see how they can function as the leading development agents in these countries (see box 2 for how central banks were used to promote development in Europe, the United States and the Asian NIEs).

What role for the financial sector in development?

Much of Africa's previously non-competitive, shallow and "repressive" financial system could be traced to the implementation of some of these same policies (as in box 2) entailed in the development bank model by Governments (Brownbridge and Gayi, 1999). However, as illustrated in the case of the NIEs, there was nothing intrinsically bad about these policies (see also next section). The external environment, overall macroeconomic context, quality of governance and associated political direction, and mode of implementation are what make a difference to the outcome of the implementation of this set of policies. Clearly, Africa has made significant progress in attaining macroeconomic stability and improving governance across the region, and is serious about tackling in a concerted manner its development challenges (for example, as expressed in the objectives of the New Partnership for Africa's Development (NEPAD)). A new institutional landscape has emerged pivoted on the African Union (including NEPAD),[38] and the Regional Economic Communities. Coupled with this are new Pan-African governance structures such as the Pan-African Parliament, the African Court on Human and Peoples' Rights and the African Peer Review Mechanism (APRM)[39]. More than 40 African countries have also ratified the United Nations Convention Against Corruption and 18 countries have signed up to the Extractive Industries Transparency Initiative. Thus, these policies now stand a much better chance of yielding the desired outcomes within a strengthened macroeconomic, institutional, and more transparent and accountable environment.

However, doubts have emerged recently as to whether African countries could sustain their improved growth performance since the mid-1990s without

a clearly defined development strategy. This is because, notwithstanding the recent improvements in economic fundamentals, some problems have persisted in keeping the economies trapped in a low growth trajectory. As discussed in chapters 1 and 2, economic growth has produced only a limited number of jobs in the formal sector, as the extractive sectors leading growth are capital-intensive and have very limited linkages to the rest of the economy. Lending to the private sector has remained limited, averaging about 20 per cent of GDP. Despite financial sector reforms, banks still prefer to lend only to established firms, mostly foreign affiliates, for a variety of reasons.[40] The sale of government debt to finance the budget means that most banks hold their assets in government papers (treasury bills), which carry virtually no risks. The financial sector lacks competition, the result of which is very high interest rates (despite low and falling inflation) and high spreads,[41] which discourage all but the most determined local investors and long-term investments (see also Chapter 2). Banks are also careful to avoid a mismatch between their assets and liabilities; most attract only short-term deposits which could not be used to fund long-term investments in particularly risky environments.

Thus, the outcomes of financial sector reforms in these countries to date are not promising for the emergence of a commercially-oriented banking system that is likely to plug the gap for long-term investment needs. The short supply of term financing will almost certainly continue into the foreseeable future. All these call for a determined government financial sector action or policy in favour of long-term financing and credit provision to the neglected small and medium-sized enterprises and entrepreneurs, for whom access to credit is a problem (see also Chapter 2).

Long-term public debt instruments will not only encourage the financing of public investments in infrastructure, water and energy, but they will also facilitate the management of government debt, just as direct loans to employment intensive sectors (McKinley, 2005) may be an antidote to the region's current jobless growth. Within the current context, this would probably involve a substitution of existing short-term debt with long-term debt in several countries. However, whatever policy is adopted in this specific instance has to be consistent with the overall government monetary policy stance, in particular regarding the level of its fiscal deficits. Also, a clearly-defined policy on long-term financing within the context of an overall development strategy predicated on development banks could provide financing for domestic investors in the Government's strategic sectors (see chapter 4 for a detailed discussion).

In the rural areas, the key to developing financial markets is to find the institutional arrangements which can best overcome the specific types of market failures afflicting these markets.[42] As such, there may also be the need to encourage the growth of different types of non-bank financial institutions to serve those segments of financial markets which are unattractive to the commercial banks. Leasing companies could provide a potentially useful vehicle for short- to medium-term asset financing for small and medium-sized enterprises within an appropriate legal framework, ensuring that they are being subjected to prudential regulation and supervision if they are to mobilize funds from the market (Brownbridge and Gayi, 1999). These could be joint public–private partnerships. Considering the pervasive nature of market failures in rural financial markets, some government intervention to facilitate credit supply to small farmers and rural small and medium-sized enterprises could improve social welfare. If these farmers and entrepreneurs operate in sectors that correspond to priorities, such loans could be subsidized.

Most African economies have attained macroeconomic stability, probably about the only notable achievement of SAPs. Inflation rates declined from double digits during the 1980s to single digits in most countries by the end of the 1990s. By 2004, only three of 52 African countries had inflation rates of more than 20 per cent. In 2006, the inflation rates for 40 of the 52 countries were in single digits, with another 10 posting rates of between 10 and 19.9 per cent (UNECA, 2007: 41). Macroeconomic instability is therefore no longer the main issue for most African countries. And considering the fact that there is a lack of consensus on the threshold at which the negative effects of inflation kick in, Governments would appear to have some leeway in terms of policy. While some studies suggest that this threshold is as low as 10 per cent, others, such as McKinley (2005: 20), indicate that this level could be as high as 20 to 25 per cent.

Despite the outbreak of new civil unrest in a few countries, some of the worst conflicts in the history of the continent have now ended. As discussed earlier, most Governments are now committed to good governance as well as to development within the framework of new pan-African institutional and governance structures. So the chances are that a commitment to enhancing growth, creating employment, and reducing poverty via a loosening of fiscal policy, including directed credit to strategic sectors, is most likely to produce favourable economic outcomes.

The original arguments in favour of liberalizing the financial sector as advanced by McKinnon (1973) and Shaw (1973) still resonate with several economists.[43] On the other hand, some economists support some forms of financial repression, particularly given the economic and political structures, including institutional weaknesses, of many developing countries (and against the background of the experiences of the NIEs).[44] This latter group contends that the removal of one distortion might not necessarily enhance welfare in the presence of other distortions. Similarly, financial liberalization is unlikely to improve welfare much, given the prevalence of information asymmetries afflicting financial transactions and markets (see, for example, Stiglitz, 2000). The recent bouts of financial crises in several emerging economies appear to have vindicated the position of the critics of financial liberalization. Indeed, the poor sequencing of financial sector reforms in Africa[45] suggests that even if the benefits of liberalization were guaranteed, these would depend largely on how reforms were implemented. And the prevalence of financial dualism (as discussed in chapter 1) suggests the need for caution in recommending liberalization policies for countries in the region. This is particularly so because, as observed by Gemech and Struthers (2003), financial dualism has rarely been adequately incorporated in empirical studies on financial liberalization. Nevertheless, some observers have noted that financial liberalization has had a somewhat positive effect on the informal financial sector, and to the extent that fragmentation in financial markets is replaced by segmentation, liberalization could prove useful to these economies (Steel et al., 1997).

In the light of the observations above, it might not be unreasonable that some form of government action to fix the weaknesses of the financial sector in African economies is actually welfare enhancing. This should take the form of flexible monetary policy that aims to create more jobs rather than attaining lower rates of inflation, and the regulation of capital accounts to contain capital flight. Policy measures are also necessary to facilitate the mobilization of domestic resources (e.g. via pension or social security funds) and directing these into long-term, productive, employment- generating investments, e.g. by credit allocation and subsidies (see chapter 4).

These fiscal and monetary policies could be complemented with measures to underpin a profit–investment nexus. This is critical not only to domestic capital accumulation on a self-sustaining basis, but also for channelling capital into strategic sectors that propel the economy onto a higher growth trajectory.

Irrespective of the conclusions on the causative factors of the financial crisis that engulfed the Asian economies in the late 1990s, a major lesson from the crisis is that a strong financial sector is central to the prevention of such a crisis, and to the pace of recovery from it. Prudential regulation of banks and strong banking supervision to ensure the implementation of such regulation are the hallmarks of such a financial system. The capacities of Governments to implement the kinds of policies discussed in this section depend on the quality of institutions, governance and macroeconomic stability.

D. Can Africa nurture "developmental States"?

There have been several attempts to distil lessons from the East Asian experiences for other parts of the developing world, including sub-Saharan Africa (see, for example, UNCTAD, 1996, 1997, 1998; Akyüz et al., 1998; Mkandawire, 2001; and Sindzingre, 2004). In the case of sub-Saharan Africa, several observers have expressed doubts not only about the quality of institutional infrastructure, but also about the capacity of sub-Saharan African States to design, implement and monitor complex and demanding policies such as those that have been at the core of the success of the NIEs. Much of this conclusion is premised on the assumption that African States are too corrupt and predatory, and ruled by rent-seeking or just plain kleptocratic officials who prioritize their private interests over those of the State, and use rents to fund patronage for their constituents.[46]

This view of the African State is prevalent today in the literature and among some African observers and students, but it is distorted. It describes, in a rather sweeping and general sense (and without a critical analysis of their differential performances), the so-called "African State" at a particular historic juncture in the continent's development trajectory – mainly from about the mid-to-late 1970s. In reality, this conception of the "African State" refers, in part, to some States in social and political turmoil, their poor economic performance being just one manifestation of such a State. It is derived from "ideological, paradigmatic and structural shifts in both domestic and international spheres"[47] (Mkandawire, 2001), in particular from the anti-State rhetoric associated with the 1980s' neoliberalism. As such, it is based more on ideological preference rather than a careful analysis of the role and effectiveness of the State (UNCTAD, 2006a).

Africa's economic malaise: domestic policy mistakes?

The extent to which Africa's economic performance could be attributed to the impact of external and internal factors has often been contested. But it appears the role of exogenous factors is often underestimated. This failure to take full account of the exogenous factors as explanatory variables in diagnosing Africa's development malaise has led to a misunderstanding and, as a result, misleading statements concerning Africa's development problem. For example, according to Mkandawire (2001: 303), the World Bank's 1981 Berg Report "…had in many ways misrepresented Africa's economic performance during the preceding two decades … [It] underestimated the enormous importance to African economies of external conjuncture and the role of foreign expertise".

The World Bank identified "structural" factors (evolving from historical circumstances or from the physical environment) and external factors as impeding Africa's economic growth. Nevertheless, in its view, these were exacerbated by "domestic policy inadequacies", to which the main thrust of its policy recommendations were directed (World Bank, 1981), thus laying the foundation for the neoliberal paradigm which was manifested in structural adjustment policies. This emphasis on the internal factors has been traced to the intellectual debate, in which Africa was caught up, within the World Bank (and the economic profession) during the Robert McNamara era.[48] The increasing popularity of the neoliberals in a way led to an uncritical acceptance of the analysis of the Berg Report by most African observers (Mkandawire, 2001; Arrighi, 2002: 30-32). As such, there appeared to be no opposition (or alternative)[49] to the report's policy prescriptions, which held sway on the continent for the best part of three decades, with catastrophic consequences (see, for example, UNCTAD, 2002; Arrighi, 2002: 32).

Historical imprints: volatile mix of external and internal factors

One might not go as far as Sindzingre to repudiate the role of the State in promoting growth in Asia, but one can characterize particular economic outcomes as stemming "…rather from particular modalities and actualizations of the concept of the State, from specific historical trajectories and combination of institutions and individual expectations" (Sindzingre, 2004). The State in much of Africa is a product of competition between colonial powers for access to resources of the continent with seemingly little, if any, concern for already existing societal arrangements revolving around ethnic conglomerations. This

history has left some distinctive imprints on the evolution of States (or post-colonial Governments) in Africa (see also Arrighi, 2002: 24). These States are, as a result, products of certain historical and geopolitical developments which continue to inform the nature of politics, which can be subject to interference and/or manipulation by external powers. But whilst the concept of "State" as in the European context may be foreign to Africa (and "statehood" may be in its infancy, the very basis of the State still being a subject of contention in some countries), there were great expectations of the leaders of the independence struggle not only to end colonial rule but also to deliver as fast as possible on development in the post-colonial African State.

In the immediate post-colonial period of the 1960s and early 1970s, most sub-Saharan African countries had fairly strong Governments that took the task of nation-building and development seriously. Not surprisingly, therefore, they managed to attain and sustain positive and in several cases robust economic growth rates. However, a lethal combination of external shocks (sharp rises in the price oil and collapse in the prices of their major primary commodity exports) triggered economic collapse starting from about the late 1970s. This was the genesis of the African debt crisis of the 1980s and the 1990s. As argued elsewhere by UNCTAD, the commodity-dependent nature of these countries makes them extremely vulnerable not only to declining terms of trade but also to the commodity price variability (UNCTAD, 2003; Sindzingre, 2004).

Within one year, the ratio of exports of good and services to GDP in Africa and sub-Saharan Africa collapsed respectively from 33 and 31 per cent (1974) to 27 and 25 per cent (1975) and never recovered in a sustained manner until 2000. This ratio was much higher in Africa in 1974 (at the time the crisis set in) than in Indonesia (28 per cent), the Republic of Korea (27 per cent) and Thailand (22 per cent). In the ensuing years, all these countries had overtaken Africa, the Republic of Korea since 1981 reaching an export/GDP ratio ranging from 41 to 44 per cent from 2000 to 2005, and Thailand since 1988 reaching an export/GDP ratio of 67 to 74 per cent in 2000–2005, compared with Africa's 33 to 38 per cent over the same period. While Indonesia outperformed Africa from 1997 to 2001, its performance on this indicator since 2002 has more or less been the same as Africa's (see table 3).

In some African countries, the dire economic situation induced political instability, which in turn exacerbated the former during much of the 1980s, thereby increasing the vulnerability of the State to capture by various special

interest groups. The complex interplay of economic and political regress, the outcome of the competition between these domestic forces for the control of State power and resources to serve private ends, consigned several of these countries to a category that was later to be christened as "failed" or "weak" States.

The implementation of SAPs from the early 1980s, whilst restoring some macroeconomic stability, did not start a process of strong economic recovery, structural transformation, nor indeed economic diversification. Throughout much of the 1990s, average economic performance throughout the region was anaemic, averaging about 3 per cent per annum with a sustained recovery starting only from about the turn of the century. Economic growth has since averaged 4.6 per cent per annum between 2000 and 2005. In 2006, the continent's average growth rate was 5.7 per cent, and this is projected to increase to about 6.2 per cent in 2007 (UNECA, 2007).

In sum, several analysts have argued that developmental States are unlikely to emerge from this economic, political and social milieu for a variety of reasons.[50] These include the poor record of economic performance until recently, and "softness" of the African State and its vulnerability to capture by special interest groups, as well as its lack of a development ideology. The other reasons are the dependence of the State on external resources, the lack of technical and analytical capacity, and the changed international environment in which protectionist industrial policies have been outlawed (or have to meet more stringent requirements) under the World Trade Organization (WTO) Agreements (Mkandawire, 2001).

Rereading Africa's economic history

Nevertheless, as observed by several scholars (Bangura, 1992; Mkandawire, 2001; and Arrighi, 2002), a more realistic assessment of the political and economic history of the continent reveals a very different picture from this truncated version. A majority of the first generation of African leaders were preoccupied with development as well as nation-building, to the extent that the post-colonial State in Africa has been dubbed "developmentalist" by some observers,[51] despite earlier criticisms.

Africa's economic performance has not always been as dismal as is usually portrayed in the literature, in particular considering its growth record during the

period 1960–1975 (see, for example, Bangura, 1992: 60–61; and Mkandawire, 2001). An analysis of the development experience in most developing countries (i.e. those that experienced at least a 3 per cent growth in GDP per capita) over this period reveals that 11 of the best-performing 50 countries are in Africa (and nine in sub-Saharan Africa). The fastest-growing developing country up to 1975 was African (Gabon), and Botswana's growth rate from 1960 to 1975 exceeded that of Hong Kong (China), Taiwan Province of China, Malaysia and Thailand (Rodrik, 1997) (see also table 5).

An examination of the growth performance of developing countries from 1967 to 1980 yielded similar results. Of the 27 countries that attained the annual growth rate of 6 per cent over more than a decade (taken as a measure of successful development experience) during this period, more than a third (10) were African. In addition to mineral-rich countries such as Gabon, Botswana, the Republic of Congo and Nigeria, other countries such as Kenya and Côte d'Ivoire also outperformed Indonesia and Malaysia. Most interestingly, much of this growth was driven by domestic savings, which increased considerably in the immediate post-independence period, reaching an average annual growth of 23.5 per cent of GDP between 1971 and 1980. By 1980, about a third of sub-Saharan African countries had saving/GDP ratios of more than 25 per cent. Both savings and investment rates in the high-performing African countries over this period were close to those of the NIEs in East Asia (see table 3). However, these savings and investment rates yielded lower growth rates in the former (Mkandawire, 2001: 304–305), a fact which could probably be explained by lower average total factor productivity growth[52] in sub-Saharan Africa (0.83 per cent) relative to East Asia and the Pacific (1.18 per cent) between 1960 and 1973. GDP growth per worker was also lower in sub-Saharan Africa (1.80 per cent) than in East Asia and the Pacific (3.83 per cent) (see table 6). In addition to this good economic performance, Africa attained significant progress in social and physical infrastructure development over this period.

Africa's economic collapse: an eclectic thesis?

How then did most African countries come to grief from about the mid-1970s onward? As argued by UNCTAD (2004), the two oil price shocks of 1973–1974 and 1979–1980 were a significant factor in the economic collapse (and the subsequent debt crisis) of African countries, the latter leading to deterioration in the external environment which lasted until 1982. The rise in oil prices had an adverse impact on the trade balance of oil-importing countries, not only

Table 5

Per capita GDP growth rates: top 50 developing countries, 1960–1975

(Percentage)

Country	1960–75	1975–89	Country	1960–75	1975–89
Gabon	7.87	-3.40	Ireland	4.02	2.70
Singapore	7.40	5.10	Finland	3.99	2.73
Japan	7.05	3.53	Thailand	3.94	4.72
Republic of Korea	6.47	7.00	Italy	3.89	2.80
Botswana	6.16	6.17	Turkey	3.85	1.23
Greece	6.15	1.73	Iceland	3.80	2.54
Hong Kong, China	6.12	6.61	Belgium	3.78	2.08
Lesotho	6.00	2.15	Norway	3.76	2.77
Taiwan Prov. of China	5.86	6.57	France	3.73	1.90
Portugal	5.68	2.59	Austria	3.71	2.29
Spain	5.66	1.64	Dominican Republic	3.56	1.14
Syrian Arab Republic	5.61	0.30	Canada	3.52	2.57
Malta	5.46	5.39	Togo	3.49	0.22
Yugoslavia*	5.42	1.04	Netherlands	3.48	1.35
Israel	4.98	1.25	South Africa	3.39	-0.39
Swaziland	4.76	-0.86	Mexico	3.37	0.76
Barbados	4.60	2.57	Utd. Rep. of Tanzania	3.37	n.a.
Islamic Rep. of Iran	4.59	-3.60	Côte d'Ivoire	3.30	-1.56
Brazil	4.57	1.27	Jamaica	3.23	-1.35
Morocco	4.27	2.20	Bolivia	3.19	-0.77
Malaysia	4.26	3.82	Nicaragua	3.11	n.a.
Nigeria	4.15	-2.41	Costa Rica	3.05	0.82
Tunisia	4.14	2.25	Sweden	3.05	1.45
Panama	4.13	-0.38	Egypt	3.04	2.93
Ecuador	4.04	0.48	Papua New Guinea	3.02	-1.27

Source: Pen World Tables in Rodrik, 1997.

* Encompassing all current and former Yugoslavian countries.

undermining domestic investment, but also triggering fiscal crises in most of these countries. The second shock coincided with sharp rises in real interest rates and the global recession of 1981–1982, which depressed demand for African exports. The terms of trade deteriorated, and the balance-of-payments crisis afflicting

developing countries was exacerbated for oil importers. However, based on the erroneous assumption that quick recovery from the global recession would soon restore the prices of non-fuel commodities, most of these countries resorted to external borrowing to finance fiscal and external imbalances.[53]

For many African countries, there was little room for manoeuvre because of their non-diversified economies, but mostly because of the steep decline in non-fuel primary commodity prices during the global recession of 1981–82.[54] The developmental States of Asia and sub-Saharan Africa have a common feature of external orientation; that is, dependence on external trade to drive their economies. The difference between the two groups was that the Asian economies were more diversified in terms of the technological intensity and composition of exports, whilst their sub-Saharan African counterparts relied almost exclusively on unprocessed primary commodity exports. Paradoxically, therefore, the failure to pursue a labour-intensive "export–oriented strategy" cannot explain the economic collapse of sub-Saharan African countries in the wake of adverse external factors from about the mid-to-late 1970s. These countries, if anything, followed the textbook advice of exploiting their comparative advantage in land-intensive exports (mineral and primary commodities).

Indeed, if there was any "failure" in development policy formulation, it was the lack of a strategy for countries to diversify their economic bases through, for example, an explicit export–investment nexus (Mkandawire, 2001; Arrighi, 2002). As illustrated by the example of the Asian NIEs, progress in increasing the technology intensity of exports is a means of addressing vulnerability and dependence, and remaining on a sustainable growth trajectory (Sindzingre, 2004). Some studies also suggest much of the variance in growth performance during the adjustment period in Africa could be due to differences in productivity and export performance in the industrial sector (Pieper, 2000; Thirlwall, 2004).

The external environment (specifically, the geopolitical context) of sub-Saharan Africa and the NIEs was also markedly different. By virtue of their different geographical locations, the antagonists of the Cold War had different relations with each of these groups, which produced diverse outcomes. Preferential access provided by the United States to its domestic market for its Asian allies was critical in the "take-off" of the region, as were the large amounts of aid it provided. The Korean War, for example, has been described as "Japan's Marshall Plan": over the period 1950–1970, United States aid to Japan averaged $500 million per year. Huge amounts of military and economic aid to the Republic of

Table 6

Economic performance by period and region

(Annual average growth rates, in per cent)

	1960–1974			1975–1984			1985–2000			1960–2000		
	Contribution of growth in education per worker	*GDP per worker*	*TFP**	*Contribution of growth in education per worker*	*GDP per worker*	*TFP**	*Contribution of growth in education per worker*	*GDP per worker*	*TFP**	*Contribution of growth in education per worker*	*GDP per worker*	*TFP**
Sub-Saharan Africa	0.18	1.80	0.83	0.27	-0.76	-1.48	0.30	0.07	-0.08	0.25	0.51	-0.09
Latin America and Caribbean	0.28	2.33	1.44	0.41	-0.62	-1.76	0.32	0.11	-0.27	0.33	0.76	0.00
South Asia	0.25	1.82	0.39	0.34	2.52	1.15	0.37	2.32	1.04	0.31	2.18	0.82
East Asia and Pacific	0.46	3.83	1.18	0.51	3.77	0.71	0.48	4.04	1.58	0.48	3.89	1.21
Middle East and North Africa	0.37	3.75	1.86	0.50	2.50	0.37	0.47	0.92	0.13	0.44	2.37	0.84
Industrialized countries	0.31	3.49	1.75	0.37	1.15	0.01	0.30	1.70	0.80	0.32	2.23	0.96

Source: Extracted from Ndulu and O'Connell, 2003, revised tables 4.2.1, 4.2.3 and 4.2.4.

* Total factor productivity.

Korea, and investment in infrastructure, were linked to the Cold War. From 1946 to 1978, this aid amounted to $13 billion ($600 per capita), whilst aid to Taiwan Province of China totalled $5.6 billion ($425 per capita) (Arrighi, 2002: 30–31).

No such largesse was showered on the economies of Africa. In all, the Republic of Korea received $6 billion of United States economic aid from 1946 to 1978, compared with $6.89 billion for all of Africa and $14.8 billion for all of Latin America over the same period (Arrighi, 2002: 31).[55] On the other hand, sub-Saharan Africa became the theatre for playing out Cold War confrontations. Misrule and usurpation of state power for private gain could be overlooked, and in some cases even condoned, as in Mobutu's Zaire (Arrighi, 2002: 31; Sindzingre, 2004).

These differences in the "initial conditions" between East Asia and sub-Saharan Africa were accentuated further by the differences in legacies inherited in the domains of state formation and national economic integration. Consequently, these huge disparities in post-colonial economic heritage of political–economic configurations were critical in conditioning the coping strategies or abilities of the two regions in the aftermaths of the oil crises (Arrighi, 2002: 24–26). The Bretton Woods Institutions also need to take some responsibility for sub-Saharan Africa's economic misfortunes in the past quarter

century, as evidenced by the disappointing outcome of SAPs. These programmes tended to marginalize domestic capital, with their focus being placed on foreign capital and on privatization (for fiscal reasons) rather than on building domestic productive capacity or empowering the domestic entrepreneurial class.[56] The premature removal of protection in Africa, in terms of duration of import substituting industrialization (ISI) strategies (unlike in Asia) and the absence of policies ("carrots" as well as "sticks") designed to align domestic capital with its developmental role, further undermined the domestic entrepreneurial class.[57] Arguably, the window of opportunity between African independence and the onset of global recession (about 15 to 20 years), was too short for any viable development policy to take shape, or for Africans to learn by doing.

Indeed, it is arguable that the various negative characterizations of the African State have much to do with their economic meltdown starting from about the mid-1970s.[58] The neo-patrimonial State as a theoretical construct has some weaknesses. Certain "clientelistic" practices may be morally reprehensible, but despite recent attempts, there is as yet no robust theoretical framework predicting how they affect the performance of capitalist economies, nor indeed, the extent to which they are pathological to capitalist economic systems.[59] And rent-seeking does not necessarily have to be debilitating to an economic system. If channelled into production, rents can contribute to development in neo-patrimonial States.[60] The issue is that the Asian experience has been idealized to the extent of obscuring the appropriate lessons to be learnt from it. In effect, we have failed to identify correctly the very complex processes that underscore the successful performance of these countries (Mkandawire, 2001). Indeed, this point has been echoed recently by the World Bank in the "Forward" to its recent publication on lessons to be learnt from a decade of reforms: "There was also appreciation and recognition that the complexity and diversity of growth experiences are not amenable to simplistic policy prescriptions. They required more refined and rigorous economic analysis" (World Bank, 2005b: xiii).

The latest attempts by the new institutional economists to attribute the developmental problems of sub-Saharan Africa mainly to a lack of democratic regimes, or a lack of "good governance" (broadly defined) is equally suspect. Some of the earliest developmental States in Asia (the Republic of Korea and Singapore) had authoritarian regimes, although earlier links between authoritarian regimes and development[61] no longer appear credible. On the other hand, democratic regimes do not seem to have a monopoly on fast economic growth and development (e.g. the world's largest democracy, India, has started to

experience high levels of growth only recently). Neither do States with strong centralizing tendencies fail to develop, as the case of China illustrates. There is some consensus, however, that in the long run democratic dispensation through opening the political space for a much greater participation of the citizenry and civil society organizations would be most likely to allocate resources in ways that best address the needs of the population.[62]

To sum up, much of the explanation for Africa's economic and political development appears to have been conjectural, rather than robust and rooted in the actual economic and political history of the continent. External factors and institutions have had a much larger sway on Africa's economic and political fortunes than is usually acknowledged. Sometimes, these have had direct adverse consequences for the nature of political and economic governance in some countries, although this is not to absolve entirely the internal debilitating (economic and political) dynamics which were spawned by some of these processes. Overall, a propitious external environment often leads to positive economic outcomes in many African countries. Indeed, African countries proved capable of attaining solid growth rates in such circumstances in the 1960s and early 1970s. And they are poised to seize the opportunity once more, as evidenced by the green shoots of high growth on the back of high commodity prices, underpinned by a strong export demand from Asia, debt relief and, recently, increased aid. Moreover, such recent growth performance can only be improved upon and sustained if African countries promote diversification and increase the technology intensity of their exports.

Considering the improved macroeconomic management as reflected in good macroeconomic fundamentals across the continent (lower levels of inflation and lower fiscal deficits, together with low albeit slowly rising domestic savings), this would appear to be the right moment to nurture the developmental States. The commitment to good governance underpinned by the APRM of NEPAD/African Union, and increasing democratic dispensation, should in all probability support such a State and help ensure that its policies are not hijacked by a minority to serve its selfish interests. Recent analyses confirm that the so-called first order problems – institutions, macroeconomic stability, trade openness, education and inequality – may no longer be binding constraints in Africa (see, for example, Johnson et al., 2007). This highlights the need for policy space, which could be used by countries themselves to identify their priorities and specific challenges, and then design a development strategy that responds to these.

However, there are limits to the comparisons (and perhaps lessons) that can be drawn between the NIEs and Africa. Current conditions in Africa and those initial conditions in the NIEs in the 1950s and 1960s (particularly in the rural economy) may share some similarities, but there are also significant differences. The fact that African economies have suffered from almost a quarter century of stagnation and de-industrialization, and associated informalization of the economy, also suggests caveats for any simple notion of replication of development strategies (UNCTAD, 2006a). At present, most African countries are unable to design their own development strategies because of severe restrictions on their policy autonomy stemming from two main sources. Donors fund a large proportion of the government budget, in some cases more that 50 per cent, so they have a large sway on what policies could be implemented through conditionalities and moral suasion. Secondly, most of these countries are members of WTO, and are therefore constrained by the "single undertaking" commitment entailed by this. An upshot of this is that policy options exercised by the NIEs are no longer available for use by other developing countries, as they are absolutely proscribed. Only a limited number of these policies could be implemented under well-defined and very restricted circumstances.

E. "Policy space" – what to do with it?

Over the past quarter century, the neoliberal economic logic that dictated unbridled liberalization policies has contributed to growing inequality in many parts of the world, including even in some of the new emerging economies (Wade, 2004; Broad and Cavanagh, 2006). The number of people living on less than one dollar per day increased not only in sub-Saharan Africa over this period, but also in Latin America and the Caribbean. In sub-Saharan Africa, the number of people living on less than one dollar per day increased from 167.5 million to 298.3 million between 1981 and 2004; in Latin America and the Caribbean, the number increased from 39.4 million to 47 million over the same period (Chen and Ravallion, 2007).[63] The growth rates of poor countries during the periods of trade liberalization, 1980 to 2000, were much lower than in the period when markets were less open, 1960 to 1980 (Broad and Cavanagh, 2006; Rodrik, 2001a; Easterly, 2001; Arrighi, 2002; Wade, 2004).[64] The view has been echoed by other scholars that "… the real economic performance of countries that had recently adopted Washington Consensus polices … was distinctly disappointing" (Krugman, 1995).

Indeed, as argued by Rodrik, much of the evidence produced on total factor productivity growth supporting the idea of more dynamic inefficiency under an import-substituting regime than under an outward-oriented one is "simply incorrect". This is because "… as an industrialization strategy intended to raise domestic investment and enhance productivity, import substitution apparently worked pretty well in a very broad range of countries until the mid-1970s" (Rodrik, 2001a: 17). As discussed earlier, this was the case in several African countries.

To Rodrik, the ISI approach fell out of favour not only because of the economic collapse of many developing countries following this approach in the 1980s, but also because of the influential studies of some economists (for example, Little et al., 1970; and Balassa, 1971).[65] The ISI economies collapsed due to their failure to adjust their macroeconomic policies to a number of external factors after 1973, including the breakdown in the Bretton Woods fixed exchange rate system, the two major oil shocks, and the commodity boom and bust cycles. Thus, trade and industrial policies were not the real culprits (Rodrik, 2001a), and should therefore not have been the focus of the neoliberals. This is consistent with the observation of others that the cause of the African crisis during this period was "… due primarily to structural and conjunctural processes of the global economy…" rather than to "bad" polices and "poor" governance (Arrighi, 2002: 33). In his analysis of the stagnation in developing countries over almost two decades (1980–1998), Easterly also concludes that worldwide factors (increased world interest rates, debt overhang and growth slowdown in the industrial world, among others) may have contributed to their stagnation. "… [P]oor policies are not a plausible candidate for explaining the lost decades. Polices either got better or remained the same throughout the period, 1960–1998" (Easterly, 2001: 12).

While China and India have recently been the "new recruits" to the neoliberal cause because of their phenomenal growth performance since the 1990s, the experiences of these two countries are anything but lessons in the application of neoliberal economics. Neither of these countries pursued the Washington Consensus blindly. Rather, each reserved some markets to the domestic firms whilst selectively and carefully opening up others. This policy was accompanied in each case by a targeting of resources for land reform, education and other national goals. Thus, the substantial drop in extreme poverty in both countries has been attributed to government policy and not simply to external orientation of the economy (Broad and Cavanagh, 2006).

Contrary to popular perception, advocating the use of government policy to correct some of the egregious excesses of the market is not tantamount to a return to statism or protectionist economic policies. Rather, it is a call to move away from preoccupations with policies based on the ideological divide of "laissez faire" and "dirigisme" to a set of more refined and eclectic policy measures that combine features of both, but tailored to the specific development challenges or circumstances of each country. In other words, it is a move to a kind of "à la carte development policy menu". Some policy measures under this menu would perhaps fall foul of the WTO Agreements, which define current global trade rules. Nevertheless, these agreements are not cast in stone, and several development economists and trade experts have been calling for their review to take into account the peculiar situations prevailing in poor countries (see, for example, UNCTAD, 1998b: 63–84; Das, 2005). There is also some flexibility in these Agreements, although highly restricted in some cases, that poor countries, including those in Africa, could exploit to serve their development objectives. African countries need greater "policy space" to be able to design and implement these policies. Effective rolling back and/or rationalization of conditionalities by the Bretton Woods Institutions would also ensure that space vacated by the WTO Agreements is not encroached upon.

How then should African countries use this "policy space"? No doubt, in attempting to take advantage of the space to be vacated by the multilateral financial institutions, there is the need for caution and avoidance of a return to the "bad old days" that set in immediately after the economic collapse of the late 1970s. For a start, these countries must seek to rely as much as possible on their own resources for investment in the medium term, which suggests greater efforts at domestic resource mobilization[66] and a gradual reduction of dependence on external resources, namely ODA. There is only a perfunctory reference to domestic resource mobilization in NEPAD, without elaborating any specific actions to address it (NEPAD, 2001: 44–45). Both the MDGs and NEPAD give more importance to foreign aid, FDI, ODA, debt relief and trade to attain their objectives. The point is that whilst all these are important, there is a need for a "domestic driver" if a self-sustaining growth and development process is to be realized. Greater domestic mobilization will not only reduce excess reliance on aid and FDI, but will also create a legitimate policy space in which "ownership" is actualized by channelling both aid and investment into fast-growing sectors with huge multiplier or spillover effects for the whole of the economy.

Furthermore, making effective use of this policy space will also necessitate the formulation of a national development (or industrial) strategy that identifies clear objectives, spells out policies to attain them, and has effective monitoring mechanisms to ensure that policy targets are being met. This strategy for rapid self-sustaining growth and development has to be four-pronged. Policies must be designed to promote enhanced domestic resource mobilization; encourage domestic investment; and engender a profit–investment nexus, as well as an export–investment nexus, as a basis for rapid capital accumulation and an export promotion platform. Considering the failure of market forces to promote all these objectives (à la SAPs), attaining them would almost certainly call for more active roles for Governments in the policy area.

F. Concluding remarks

A simple replication of the East Asian developmental State, even if there were such a thing, would not do. As a matter of fact, there is no such thing as the East Asian model of a developmental State that could be recommended to Africa. Indeed, the intrinsic differences among the Asian experiences underscore the importance of "trial and error" as an important ingredient of policy formulation and implementation in developmental States. This process should benefit from constant monitoring and the feeding of the lessons learnt from monitoring into new policies to overcome earlier shortcomings.

The initial conditions are not only different between African countries at present and the NIEs of the 1950s and 1960s, but also different among individual African countries. The global economic context of the 1950s and 1960s, both for the NIEs and for Africa, is also radically different from the current environment. The Cold War has ended, and security concerns are now focused on terrorism; the General Agreement on Tariffs and Trade (GATT) has been replaced with the WTO, whose agreements are binding on all members under its "single undertaking" principle; and there have been major advances in science and technology, including in ICT, which could facilitate "leapfrogging" for the laggards. While the cynic might argue that these developments pose severe challenges for poor developing countries, the optimist might see in these development opportunities worth exploiting.

Thus, whilst we have argued for the nurturing of some form of developmental States in Africa, an acknowledgement of this diversity in initial conditions would call for different policy strands within the context of an overall strategy of a developmental State. Such a strategy should seek to exploit the opportunities in the current global setup, whilst implementing policies that limit the associated costs that inevitably reduce the net benefits. As mentioned, each country should pursue strategies within the context of its own institutional (economic, political and social) arrangements. The challenge for Africa (as for other developing countries), therefore, is not how to copy any model, but how to create "capitalisms" adaptable to the unique opportunities and development challenges in each country (see, for example, Wade, 2003) in an attempt to increase the net benefits.

A challenge of good macroeconomic management is maintaining macroeconomic stability whilst shifting the economy onto a higher growth trajectory, irrespective of the roles played by the private and public sector. Several conditions are indispensable for such an effective macroeconomic management. These include a pro-investment environment predicated on political stability, policy predictability and consistency, and a robust legal and regulatory framework. A competent and technocratic civil service that is independent from politicians, to prevent undue influence in decision-making, is also important, as are coalitions between the domestic entrepreneurial class and the ruling elite. Equally significant is the oversight role of civil society in preventing abuse and misuse of power and/or state resources, and guarding against state capture by narrow business interests. Obviously, it is both more difficult and critical to fulfil these conditions in a developmental State than in other types of States, considering that the "trial and error" nature of policymaking in such States might undermine policy predictability and continuity, and increase the vulnerability of the State to capture by the elite.

The important thing, however, as mentioned earlier, is that a developmental State must be committed to a "development ideology" as a long-term predictable strategy. The escape of sub-Saharan Africa from poverty may be more challenging in the present circumstances than for East Asia, but fatalism is unwarranted (Johnson et al., 2007), and the means of escape could yet be found in the "developmental States" paradigm.