

**Economic Governance and Contemporary Global Market Developments:.
Lessons for Africa**

By

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¹ The views expressed in this paper do not represent the views of the African Development Bank

Mr. Chairman,

**President and Chairman, of Council, of the Nigerian Institute of Management Dr. (Mrs)
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Council Members, Fellows, and Members of NIM

Distinguished Invited Guests,

Ladies and Gentlemen.

It is an honour and a privilege to have the opportunity to share some thoughts with you today. The Nigerian Institute of Management (NIM) is the largest body of professional managers, management practitioners, and corporate managers in Nigeria. Members of this august body therefore shoulder an important responsibility for the future development of Nigeria which ultimately will depend on good leadership at the political level as well as effective professional management within the public, private and corporate sectors. Historical experience the world over has demonstrated the importance of solid professional management in the economic performance of countries.

Ladies and Gentlemen,

It's been a volatile few months for global financial markets, driven by almost un-precedented uncertainty amongst investors about the global economy and fears that politicians are unable to fix economic problems. Recent economic data has suggested the recovery in the West may be petering out, feeding renewed worries about the eurozone debt crisis. This, it is feared, could in turn cause a second banking crisis if governments are unable to pay back their debts. The fears have seen global financial markets wipe out gains from earlier in the year. Since 22 July, London's FTSE 100 has fallen 14%, the Dow Jones in New York has shed 15% and Germany's Dax has dropped more than 29%. Last week alone, the FTSE lost 5.6 per cent of its value or £78billion, in the second worst five-day fall this year.

Growth Fears

The key concern for investors is slowing growth in the US and Europe. The International Monetary Fund has warned that the global economy has entered what it calls a "dangerous new phase" of low growth and high public debt and has reduced its growth forecast for the world's advanced economies, predicting GDP growth of just 1.5% this year.

The IMF has further cautioned that the stability of the global financial system has weakened for the first time since 2008, when Lehman Brothers collapsed. In addition, the US Federal Reserve suggested "significant downside risks" to the country's economic outlook, while three US banks - including Bank of America - were downgraded by credit ratings agencies.

The US economy reported no new jobs in August for the first time since 1945 with unemployment remaining at 9.1%. And the US Commerce Department has revised its growth figure for earlier in the year down to an annualized rate of just 1%, after its first estimate of 1.3%. Growth for the first quarter has also been revised down.

In the Eurozone, the picture is not much better.

- The purchasing managers' index (PMI), a closely watched survey of private sector activity dropped to 49.1, from 51.5 last month. A reading below 50 indicates contraction.
- Factory output in the 17 countries that use the euro also fell and business activity in Germany, the bloc's largest economy, came close to stagnation between April and June.
- The French economy was flat during the same period.
- Meanwhile, manufacturing data from several nations added to the gloom, with a slowdown in the manufacturing and service sectors indicated across Europe.
- Manufacturing growth in China has also slowed down, registering its third consecutive month of shrinkage.
- Several Italian banks had their credit ratings downgraded last week, along with eight of Greece's main banks.

Eurozone Debt crisis

The concerns about growth have also fuelled worries about the indebtedness of eurozone states. If economies are not growing, tax receipts fall, making it harder for governments to pay off their debts. So far Greece, Portugal and the Irish Republic have received international help to deal with their crippling debt problems. Last Monday Italy became the latest eurozone country to have its credit worthiness downgraded by ratings agency Standard and Poor's, reflecting increased concerns about its ability to pay back its debts. Italy follows fellow eurozone countries Spain, the Republic of Ireland, Greece, Portugal and Cyprus in having its credit rating downgraded this year. In July, eurozone leaders agreed a second bailout deal for Greece, and also agreed more powers for the European Financial Stability Fund to help countries struggling with indebtedness. This would allow the fund to buy government debt (bonds), offer credit to nations in difficulty and would create a special facility for recapitalising banks. It included a move by private banks to swap existing Greek debt with longer term debt paying lower interest.

But the measures have yet to pass European parliaments and many already fear they are insufficient to tackle potential problems in larger economies such as Spain and Italy. Share falls

have often been led by banking sector shares as investors are worried about what level of eurozone government debt they are holding, and whether this will be repaid. French banks have come under particular pressure as they hold more than 40bn euros (£35bn) of Greek debt, almost four times more than any other country. The Institute of International Finance has said the Greek debt swap deal implies a loss for Greek lenders equivalent to 21% of the market value of their debts. If banks were forced to accept similar or greater losses on the debts of other countries it could trigger a new banking crisis, further de-stabilising the global economy.

Meanwhile, there has also been concern about the US's ability to repay its debts, with Congress agreeing on a deficit reduction plan only at the eleventh hour. This delayed deal also led to the credit-rating agency, Standard & Poor's, cutting the long-term US rating by one notch from AAA to AA+ for the first time.

The financial crisis which started in 2007 is now in its fifth year— it has moved into a new, more political phase (following the subprime, banking and sovereign debt phases). In the euro area, important steps have been taken to address current problems, but political differences *within* economies undergoing adjustment and *among* economies providing support have impeded achievement of a lasting solution. Meanwhile, the United States is faced with growing doubts over the ability of the political process to achieve a necessary consensus regarding medium-term fiscal adjustment, which is critically important for global stability.

US President Barack Obama has unveiled a \$450bn (£282bn) package of tax cuts and spending plans aimed at creating jobs and bolstering the economy. But the plans may not pass the US Congress. European leaders on the other hand are under particular pressure to provide long term stability for the single currency. The issue of eurobonds, which would allow the debt of each country to be guaranteed by all, has also been mooted. But taking responsibility for other nations' debt may prove politically unpopular in countries like Germany. Greek default and exit from the Euro is a potential solution but one that Eurozone politicians are unwilling to seriously consider

Mr. Chairman, Distinguished Ladies and Gentlemen, the discussion thus far points to one fundamental factor underpinning current developments in global financial markets – **Declining Confidence**. As nebulous as this concept may seem, it is nonetheless the glue that holds financial systems and financial markets together. Going right back to the evolution of banking with the goldsmiths, depositors of gold had the confidence that they could retrieve their deposits at any time. Similarly, bank depositors today have the confidence that they would be able to retrieve their cash deposits at any time. The truth of the matter however is that if we all went out tomorrow to retrieve our deposits from banks, the banking system would collapse. We would not do so however because we collectively continue to have confidence in the system. Confidence does not however arise in a vacuum. Confidence in financial markets is based on trust which is ultimately in turn based on good economic governance and management.

In years gone by, countries went to great lengths to preserve confidence in their financial systems. In England for example, so important was maintaining the value of coinage that by 1121 when there was a noticeable decline in the quality of England's silver, all the Mint Masters in England (equivalent of central Bank Governors of the time) were assembled and punished by having their right hands cut off! This was a rather draconian method of monetary control but it speaks to the importance attached to maintaining confidence in the system. Today, however, it is markets that dish out punishment for poor economic governance in addition to prosecutions of wrong doers like Nick Leeson of Barings fame.

The declining confidence in the Eurozone as well as US is the result of the market's assessment that fiscal policy in both regions is unsustainable on current trends. The euro like all common currencies or fixed exchange rate regimes is underpinned by some fundamental rules of economics. One such rule is what is known in economics as the *Impossible Trinity*. This states that a country cannot simultaneously conduct independent monetary policy and pursue a fixed exchange regime if it wants to remain completely open to international capital flows. That principle says that a country must give up one of three goals: exchange rate stability, monetary independence, and financial market integration. It cannot have all three simultaneously. Given that financial markets are steadily becoming more and more integrated internationally, that forces the choice down to giving up on exchange rate stability (i.e. choose a flexible regime) or giving up on monetary independence (choose a hard peg).

The recent experience of some countries in the Eurozone points to attempts to make the *Impossible Trinity* possible. Basically, Greece (and to some extent Portugal, Ireland and Spain) in accumulating unsustainably large debt stocks, have been attempting to pursue independent monetary policies through the back door. This fiscal policy stance of these *Highly Indebted Industrialized Countries (HIICS)* is not sustainable and what is required is economic adjustment similar to the Structural Adjustment or HIPC Programs implemented in many African countries in the 1980s, 1990s and 2000s. Deep cuts will have to be made in government expenditure. The protests that have greeted the attempted imposition of such cuts is evidence of the difficulties the politicians face in pushing through the required adjustments. The United States faces similar problems in adopting any proposed solution to its deficit problem.

It should be noted that Greece (and to some extent Italy) did not quite meet the Maastricht performance criteria for membership of the eurozone. The euro therefore started on the wrong footing in this regard. This should be an important lesson for Nigeria and other members of the West African Monetary Zone. The common currency that is being pursued by members of the zone must be based on a commitment to solid economic fundamentals and the sustainable attainment of the set performance criteria by all member countries. Solidarity is not sufficient to sustain a common currency, only sound policies will.

Implications of the Financial Crisis for Africa

Ladies and Gentlemen, the current turbulence that is taking place in global financial markets has its roots in the 2007-2009 global financial crisis which occurred against the background of significantly improved growth and macroeconomic performance by African countries as a group over the last decade. GDP growth rates had steadily increased (averaging 6.0% over the last five years), inflation declined to single digits before the fuel and food price crisis in 2008, and external reserve positions improved. These developments were underpinned by structural policy reforms, favourable terms of trade and debt relief.

The global financial crisis could therefore not have come at a more inopportune time for the African continent as many countries were just finding their feet and gaining some traction after decades of economic stagnation and macroeconomic instability.

Initially, the conventional wisdom was that African countries were unlikely to be hard hit or at worst have only minimal impact of the effects of the crisis. This reasoning was principally predicated on among others the following:

- That low-income countries are generally less exposed to the financial contagion than emerging markets, as their financial institutions are not strongly integrated into the global financial system, and because the complex structured financial instruments at the heart of the crisis are rarely used in poor countries.
- That most banks in Sub-Saharan Africa rely on deposits to fund their loan portfolios (which they keep on their books to maturity) and that their inter-bank markets are small .
- That in recent years better macroeconomic policies, debt relief, and favourable external conditions (high commodity prices combined with low interest rates) have contributed to lower external debt ratios in many low-income countries, thus helping them better withstand the effects of the crisis.
- That investors weary of the markets in developed countries may seek opportunities in African and other emerging market economies.

The evidence thus far however suggests that the global financial crisis of 2007-2009 did after all, have significant ramifications for Africa (AfDB, 2009):

There was a significant slowdown in economic growth on the African continent with the onset of the financial crisis. GDP growth declined to 2.3 percent for 2009 (from 5.7% in 2008), resulting in a contraction in per capita income for the continent as a whole for the first time since 1994.

Export revenues also declined following the downturn in global demand and falling commodity prices. Exports from Africa declined by \$250 billion in 2009 with Nigeria and Angola

accounting for one-third of the export decline, driven by oil export revenues. This decline in export revenues in turn resulted in a deterioration of the external positions of several countries with widening current account deficits and declining international reserves. The current account balance declined from a surplus of 2.7 percent of GDP in 2008 to a deficit of 5.3 percent of GDP in 2009, a worsening by 8% of GDP in one year.

The financial crisis also resulted in a deterioration of the fiscal stance of virtually all African countries, with the budget deficit for the continent as a whole of 5.8 percent of GDP in 2009 (from a surplus of 2.8 percent of GDP in 2008), a worsening by 8.6% of GDP on average. Fiscal deficits for instance worsened not only because of the plunge in export revenues but also because of the need to increase social spending and safety nets and to provide the fiscal stimulus required to mitigate the worst consequences of the financial crisis.

Compared to Europe and the United States, Africa's economies appear to have weathered the 2007-2009 global financial crisis relatively well and rebounded in 2010. Growth in Sub-Saharan Africa registered 5.0%, up from 2.9% in 2009. It is further expected to increase to 5.5% in 2011, underpinned by the strong recovery of commodity prices. Recent political events in North Africa and high food and fuel prices are likely to slow the continent's growth down to 3.7 percent in 2011. During this year, it is expected that sub-Saharan Africa will grow faster than North Africa. The African Development Bank, prior to the most recent crisis projected a rebound to 5.8 percent in 2012.

The Nigerian government has maintained relatively prudent macroeconomic policies, strengthened financial institutions and, albeit slowly and unevenly, is undertaking reforms to transform the economy structurally. The reform effort, aided by revenue from high oil prices, has led to significantly improved macroeconomic outcomes, including weaker inflation and strong GDP growth. Real GDP growth rose from 7.0% in 2009 to an estimated 8.1% in 2010. The robust growth in 2010, in the aftermath of the global financial and economic crisis, underscored the resilience of the Nigerian economy and to some extent, the prudence of its economic policies.

The strong growth in output recorded in 2010 was supported by the expansion in oil production following relative peace in the Niger Delta region, but the key driver of growth remained the non-oil sector. Non-oil growth averaged 8.3% in 2010 and accounted for 84.8% of total GDP. The main growth drivers in the non-oil sector were telecommunications, general commerce, manufacturing, agriculture and services. The communications sector in Nigeria has boomed in the past five years, with growth averaging around 30% per annum, driven largely by the expansion of the Global System for Mobile (GSM). Large inflows of foreign direct investment (FDI) have played a crucial role. The stock of FDI in telecommunications increased more than 200%, from USD 7.5 billion in 2005 to more than USD 18 billion in 2010. The number of mobile-phone lines has increased from less than 19 million in 2005 to nearly 80 million in 2010, with teledensity reaching 54.2 lines per 100 inhabitants. The tremendous progress made in

telecommunications has contributed to an overall improvement in the business climate, benefiting in particular the manufacturing sector, which, in 2010, grew by more than 6% even with shortage of electricity and paucity of credit limiting the potential of the sub-sector.

The performance of the telecommunications sector in Nigeria is not unique. African countries that have similarly opened up their telecommunications sectors to private sector investment have similarly seen significant contributions to GDP growth from the sector. This is a testament to the catalytic role the private sector can play. The question that many African countries (including Nigeria) have to answer is why a successful experience as that in the telecoms sector cannot be replicated in the energy sector.

The global financial crisis has served to emphasize the vulnerability of African countries to external shocks. For African countries, the global financial crisis represents a major development crisis. In the last decade, African countries made significant progress in the areas of economic performance and good governance. The global financial and economic crisis however threatens to reverse the progress that has been made on several fronts. African countries can expect to experience weaker export revenues; further pressures on the current accounts and balance of payment; lower investment and growth rates; increased poverty; unemployment; weaker health systems and more difficulties in meeting the MDGs.

The continuing global financial crisis is also expected to affect aid flows to Africa which rose from \$12.2 billion in 2000 to \$38.2 billion in 2006 (driven largely by debt relief). The financial crisis is a potential “triple whammy” for Africa:

- First, the value of the existing aid commitments has fallen. The value to developing countries of the EU target of 0.56% GNI in 2010 has fallen by nearly \$12bn a year since 2007 as a result in downward revisions to estimates of national income following the financial crisis.
- Second, donors may be less likely to meet their commitments. Available evidence shows that after each previous financial crisis in a donor country since 1970, the country's aid has declined. For example, Japanese aid fell by 44% in the six years after the financial bubble burst in 1990; and Japan's aid has never returned to its pre-crisis level.
- Third, the financing needs of developing countries have increased as a result of slower growth in exports, investment and employment.

Despite recent commitments to improve aid predictability and to scale up official development assistance, progress has been slow and challenges to sustaining these commitments in the current environment are expected to increase. Overtime, official aid flows would decline, while the focus

for raising additional financing for Africa's development should primarily be on domestic resource mobilization supplemented by private capital flows. This is because Africans must ultimately bear the burden of financing their own development, no matter how painful it is. Africa cannot realistically expect that the burden for its development should be borne by others.

Africa faces a large financing gap to meet its development policy objectives in critical areas such as infrastructure, health, education, agriculture, and ICT. Various estimates have been made on the size of this financing gap in the region of a \$20-\$70 billion per annum. China for example invests \$20 billion per annum in its power sector alone.

The critical question for African countries is where all this money going to come from? The estimates and proposals presented thus far generally have an eye on the international community to provide the funding either through Official Development Assistance (ODA) or private capital flows.

At the April 2009 G20 summit in London for example, Africa was looking to the international community to help it out of the financial crisis. As it turns out, notwithstanding some important agreements at the summit, the reality on the ground is that the quantum and quality of additional external financing required by Africa is yet to materialize in any significant way. What is clear is that as a result of the global financial crisis, the developed economies are themselves facing significant economic challenges with high unemployment and declining growth and increased focus on reducing budget deficits. In this economic context, it is at the very least optimistic to expect developed country governments to increase taxes on their populations to meet Africa's financing needs.

Only five countries (Denmark, Luxembourg, the Netherlands, Norway, and Sweden) have disbursed ODA equaling 0.7 percent or more of their GNI. The unweighted average of aid effort in 2004 was 0.42 percent of GNI, while the income-weighted average ODA/GNI ratio for DAC countries stood at 0.25 percent, suggesting that smaller donors are leading the aid effort. Among them, Norway ranked first with 0.87 percent of GNI, followed by Luxembourg with 0.85 percent of GNI. Italy and the United States ranked last with allocations of 0.15 percent and 0.16 percent, respectively. Over a longer time horizon, donors such as Australia, France, Germany, the United Kingdom, and the United States have seen declines in their ODA/GNI ratios.

What about private capital flows? Between 2000-2007, Africa benefited from dramatically increased capital flows as the abundance of global liquidity in search of high yields brought in an increasing number of investors eager to participate in the African growth renaissance:

- Private equity and debt flows reached a record high of \$53 billion by 2007.

- Total foreign claims on SSA economies held by banks tripled to \$205 billion by the end of 2007.
- Bond flows to SSA for example increased by \$7.1 billion between 2006 and 2007 with Ghana, Nigeria, Seychelles, and Gabon issuing bonds internationally for the first time. A few African countries began to contemplate a move towards a greater reliance on international capital markets to finance their development rather than aid.
- Portfolio equity flows reached a value of \$15 billion in 2006 more than double the 2004-2005 levels. However, 88% of the portfolio equity flows went to South Africa.
- FDI inflows to SSA also increased from \$13 billion in 2004 to \$33 billion by 2007, with a concentration in resource-intensive countries- e.g. in 2007 55% of FDI flows went to South Africa and Nigeria.

The financial turmoil has however resulted in a sharp drop in private capital flows since the first half of 2008 as credit conditions became tighter. In fact, not a single SSA country foreign currency denominated sovereign bond has come to the market in the last three years (2008-2010). African countries are also being crowded out of the international capital markets as the developed countries like the U.S. borrow to finance their deficits.

The Case for Domestic/Regional Resource Mobilization

The bottom line is that while external flows (aid, debt relief, FDI and portfolio flows) have an important role to play in closing Africa's resource gap, they are not only insufficient but they cannot also be relied on as the current financial crisis demonstrates. Rather, the focus for generating the additional resources for the type of development that will better position African countries to weather future financial crisis should be on domestic and regional resource mobilization. This is by no means a new insight. In fact, the Monterrey Conference on Financing for Development held in 2002 recognized the critical importance of domestic financial resources for development. The reasons are straightforward:

- Both ODA and FDI are highly volatile; four times more volatile than domestic revenues for example;
- Domestic resource mobilization would improve countries' fiscal and external account positions. For example a priori, if donors provide a loan to finance of capital expenditure of 5% of GDP you start off with a budget deficit of 5% of GDP.

- Increased reliance on domestic resources would also reduce the probability of accumulating unsustainable external debts;
- With no conditionality associated with domestic resource mobilization, African countries can regain the policy space to pursue their development priorities; The reality of the international development game is that one who pays the piper calls the tune.

So if the advantages are that obvious why has domestic resource mobilization not taken center stage in the search for additional resources? The simple answer is that from a policy maker's perspective and the political economy, domestic resource mobilization is more difficult to do than receiving somebody else's tax dollars. The policy maker in many African countries faces the constraint of low incomes, a highly informal economy, low financial intermediation, and the political unpopularity of taxes.

The fact remains however that domestic savings in sub-Saharan Africa (at 17.9% of GDP) is the lowest in any region. This compares with 41% of GDP savings rate for East Asia and the Pacific. Furthermore, volatility of income sources (primary commodities) in Africa also means higher volatility of savings and therefore less predictability of investment. Almost all the recorded savings in Africa is in the form of private savings. Public savings are estimated at averaging 2% of GDP over the last decade.

A Regional Approach to Resource Mobilization

One of the major constraints facing many African countries is the small size of their economies (excluding Nigeria and South Africa). For this reason, it is thought that the potential for generating resources domestically is limited, hence the focus on external sources. The potential for mobilizing funds on a regional level in Africa to finance its development has largely been ignored. This potential is however enormous. The total GDP of all 52 African countries (in PPP terms) in 2008 is just below that of France, making Africa the 8th largest economy in the world if viewed in aggregate. Africa at the end of 2008 has higher net international reserves than India for example. Africa is therefore not a poor continent as an entity.

In the search for additional financial resources to fill the gap, it is time for African countries to recognize that together and with greater effort significant amounts of resources can be generated on the continent from both the private and public sectors. Several proposals have been made on how to increase domestic resource mobilization in Africa but I would like to focus on three: Banking the Unbanked, a region-wide tax and empowering the private sector.

Mobilizing Resources From The Unbanked

Domestic savings in Africa are mostly held in the form of non-financial assets and therefore outside the formal banking systems. For many SSA African countries only about 20% of the bankable public have access to a bank account. Financial transactions are dominated by cash payments, with some 90 percent of issued currency held by the non-bank public, with one-third of broad money (M2) being held in the form of currency.

The importance of increasing the supply of savings in the financial system through making financial services available to the population has long been recognized by the developed economies. For example, by 1772, Scotland had established a nationwide banking system. By this time 31 banks were operating in Scotland with branches and agencies covering most of the country making Scotland the first country in the world to establish an almost nationwide system of branch banking. One of the first savings banks in Europe was established in Hamburg in 1778. By 1836 there were 280 savings banks in Germany, and by 1850 they had reached 1,200 savings banks. By 1913, they numbered 3,133 with total assets more than double those of the commercial banks. By 1914, the number of rural credit co-operatives in Germany reached 17,000. The Friendly Society Act was enacted in England in 1793 to encourage savings by the poor. The Savings Bank movement however, started around 1810 with the Rothwell Savings Bank established by Henry Duncan as a bank for the poor widely imitated not only in Britain but also France and Holland. The evolution of the banking system in many European countries saw the rapid spread of banks including savings banks and rural banks targeted at the poor (Davies, 1996).

Wide access to financial services in the developed economies has therefore increased the supply of savings and reduced the cost of borrowing. To improve domestic resource mobilization in Africa, the usual recommendations are for governments to improve the efficiency of tax collections, through reform of the public financial management system, automation of tax administration, stemming capital flight etc. However at the heart of the problem of tax collection in Nigeria and other African countries is the highly informal nature of their economies, underpinned and supported by the predominance of cash transactions as a result of financial exclusion. There is money out there but it is not being used for productive investment because the majority of the population is excluded from the financial system. Unfortunately, most African countries have not made the link between financial exclusion on the one hand and the difficulty of collecting taxes on the other. One of the quickest ways to formalize an economy and therefore to increase the tax net is to bank the unbanked.

This calls for a reform of the payments system that places the unbanked at the centre rather than at the periphery. For this to be effective, the payment system platform must allow both online and offline electronic payment transactions. The traditional focus on online electronic payments by banks automatically restricts participation and enables the dominance of cash payments. For Africa, these electronic payment systems should be designed along the lines of branchless

banking models in collaboration with the private sector to work in the rural environment (without electricity) . If undertaken on a comprehensive scale, financial resources locked up in non-financial assets would be brought into the banking system for intermediation and this could be a significant source of resources (representing potentially 3-5 times what is being currently intermediated in the financial system). Furthermore, to the extent that electronic payment transactions dominate, government can easily collect and assess taxes and therefore enhance domestic resource mobilization.

A Region-wide Tax

The proposal is for African countries to impose on themselves a tax that will generate sufficient resources into a Fund that can be used to finance various critical development initiatives whether in infrastructure, agriculture, ICT or education. These funds can be leveraged to secure private sector participation in relevant initiatives or projects.

A tax on petroleum consumption is one such tax (not a popular tax in Nigeria). Africa consumes about 3,000,000 barrels of fuel a day (2007 levels). An 10 cent per litre tax will yield some \$18 billion per annum, while a 5 cents per litre will yield some \$9 billion per annum. These are not small amounts given the resource gaps. A guaranteed additional \$9--\$20 billion of domestic resources annually, appropriately deployed, can conceivably have a transformational impact in Africa. With this amount of funds mobilized annually, major projects such as the Inga dam power project in DR Congo which can generate sufficient electricity (39000MW) for the continent at the cost of some \$50 billion, agricultural infrastructure, major road and railways and ports linking the continent, can be easily financed.

The tax on petroleum consumption has the advantage that it is one of the easiest ways to get revenue, and the consumption of fuels as a group is relatively price inelastic and income elastic. The revenue yield is predictable. The burden of the tax is also equally shared across the continent and as a carbon-tax it is also environmentally friendly. It will also enhance the fiscal/debt sustainability as well as external payments outlook for the region as a whole.

While petroleum taxes are politically sensitive, it is actually not the case that petroleum products are overtaxed in Africa compared with other regions of the world. The average tax as a share of final prices for premium unleaded in OECD countries in 2009 was 69% while the estimate for Africa is much lower. The tax component of the final price in Ghana averages some 20.4% while that of South Africa is 27.9% and Nigeria is zero. While petroleum taxes are politically difficult to implement, an Africa-wide tax is more likely to be accepted if its uses are specific and supported by value for money analysis.

With funds from such a petroleum consumption tax forthcoming, Africa will also be able to negotiate on a more equal footing with countries like India and China who are able to obtain tremendous leverage by dangling \$5 billion as investment in the continent or canceling debt worth \$1.3 billion. In the present circumstances a Minister of Finance in a country with gross international reserves of \$400 million facing the prospect of a \$2 billion Chinese government concessional loan will probably not be able to sleep let a lone think straight. What leverage does the Minister have in the negotiations?

The case for such a fund is more imperative as Africa has now become the new frontier for natural resource discoveries with keen interest from countries like the USA, China and India. The management and administration of such a Fund can be worked out in consultation with member countries.

Empowering the Private Sector

Many African governments have continued to pay lip service to enhancing the role of the private sector in the development process. Challenges have persisted in sectors like energy, water, health, education, transportation, agriculture etc. since independence. For over 90% of African countries have not a single one of these basic challenges has been resolved. Attempts by Government (with limited resources) to resolve all these challenges has resulted in fiscal dominance and the crowding out of the private sector in most cases. One of the keys to dealing with the problem of fiscal dominance and its threat to macroeconomic stability is empowering the private sector to deliver projects and services that can be done more efficiently by it or in partnership with government. Many projects, properly structured will elicit private sector participation and reduce the burden of that expenditure on the budget. Ultimately, governments should always ask the question: “*Why can't the private sector undertake this project?*” or “*How can a private public partnership be structured?*”? For the private sector to play its proper role however, it is important that the rule of law prevails, property rights upheld, and contracts respected and political witch-hunting and vindictiveness avoided.

Some private sector businesses collapse simply because of a change of government. Uncertainty about the rule of law or the respect for property rights informs the desire of private foreign investors in Africa to have the “blessing” of governments before undertaking any investment. While this may provide good photo opportunities for some African governments, it is symptomatic of an underlying problem of uncertainty over property rights. After all, how many foreign investors (with Investments that dwarf those in Africa) troop daily to meet with President Obama or Prime Minister Cameron? At the same time domestic investors are denied the very incentives foreign investors are given as though they do not face the same risks. To reduce the overall cost of doing business, there should be a level playing field for domestic as well as foreign investors in terms of taxes, duty-free waivers, etc. The laws should be clear and applied

fairly to all domestic and foreign businesses. Without the private sector being assured of this type of certainty in the business environment, African countries cannot expect the low interest rate regime that prevails in the more developed economies given the risk premium that will be attached to operating in African business environments.

Unwritten Rules of the Game

Mr. Chairman, Ladies and Gentlemen,

International development is very competitive and therefore countries try to wrest a competitive advantage at every turn. Unlike the game of football where the rules are clearly defined for all participants, not all the rules of the international development game are written down. Indeed, economists are still searching for some of them. African countries are therefore able to compete on relatively more equal terms in sports like football than in the game of international development, where there are so many unwritten rules that countries have to figure out for themselves. A unique identification number, an address system and financial inclusion (banking the unbanked) are basically some of the key unwritten rules for overall development.

No donors have thus far required that countries put in place Address Systems, Unique IDs, etc. in place as conditions for aid for example. African and other developing countries have to put these systems in place themselves as a matter of priority and urgency. to support the wider goal of economic development, growth with stability, and jobs. In the presence of such market failure, there is an important role for the State, working with the private sector, to put in place some of these efficient rules or norms that underpin any modern society.

Conclusion

Ladies and Gentlemen,

In conclusion, I would argue that African policy makers must not see the on-going global financial crisis as yet another opportunity to bring out the begging bowl. Rather, the financial crisis presents an opportunity for African Governments to rethink Africa's financing options for strengthening their economies and making them more resilient to shocks of this nature in the future. While aid will remain a critical part of the financing envelope in the foreseeable future, and private capital flows will always be important (and should be encouraged), there is a strong case for a renewed focus on domestic resource mobilization.

In addition to improving domestic tax collection, this can be achieved by inter alia increasing the level of intermediation in financial system through financial inclusion of the unbanked and the

move away from cash payments towards electronic payments (online and offline) in the economy. Furthermore, there is a need to adopt a regional approach to resource mobilization. In this regard, initiatives such as a region-wide petroleum tax or other similar taxes should be explored. There is also a need to empower the private sector to assist government in service delivery.

Thank You For Your Attention.

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