FINANCING DEVELOPMENT IN AFRICA: DOMESTIC RESOURCE MOBILIZATION AND OTHER INNOVATIVE STRATEGIES

From the African Community of Practice on Management for Development result at the African Capacity Building Foundation (ACBF)

Knowledge Brief N° 5

SYNOPSIS

Africa continues to face enormous development challenges despite increased global efforts at transforming the continent since the late 1940s to early 1950s. The beginning of the twenty-first century brought great hopes for the advancement of the continent with the Declaration of the UN Millennium Development Goals (MDGs) along with the Poverty Reduction Strategies and a series of development aid pacts. Yet, the continent has continued to lag behind; poverty is still on the increase in real terms. The UN Sustainable Development Goals (SDGs) comes in when the continent is still facing continued and enormous challenges with regard to financing development. This has spurred increasing debate as to what is next; which financing solutions will be sustainable for Africa? Therefore, AfCoP had initiated discussion on alternative solutions to financing development in Africa with special focus on building capacity for domestic resource mobilization. This knowledge brief summarises the discussions and ideas shared by the AfCoP members with one of the key messages emerging being the need for building capable and effective states founded on strong accountability systems.

Introduction

Under the auspices of the Africa for Results Initiative (Afrik4R), the African Community of Practice (AfCoP) on Managing for Development Results (MfDR) has held an online discussion on "Financing Development in Africa: Domestic Resource Mobilization and Other Innovative Strategies." Africa has continued to encounter enormous challenges in addressing its development objectives. The dawn of the 21st century ushered in great optimism for the continent's advancement. Developing regions witnessed renewed aid pacts ranging from the Monetary Consensus on Development Financing (2002), to the Paris Declaration (2005), Accra Agenda for Action (2008), and the Busan Partnership for Effective Development (2011) that culminated into the current global development agenda, the New Deal. The strategic frameworks within which these commitments were expressed included the United Nations Millennium Development Goals, United Nations Sustainable Development Goals, African Union Agenda 2063 and the Poverty Reduction Strategy Papers coordinated by the IMF and the World Bank. Yet, Africa's development aspiration has yet to see significant reduction of poverty in the continent. The number of the poor in Sub-Saharan Africa had increased from 268 to 306 million people during 2000-2010 amidst renewed commitment to financing development in the global south.1 It is fact that many countries did not achieve the MDGs as planned; and as this development framework ended by end of 2015, questions have been asked as to what would be the alternative development financing solutions for Africa?

[1] Bangura (2014, p.14).

Domestic resource mobilization is believed to have the potential to play a pivotal role in financing the the sustainable development agenda 20130 of eradicating extreme poverty and minimizing socioeconomic disparities and addressing environmental challenges as well as Au agenda 2063. Interest in domestic resource mobilization in developing countries is increasing and it is becoming an importance source of sustainable and efficient development. Though not a magic bullet or panacea to Africa's development challenges, effective domestic resource mobilization can be leveraged by African countries to improve the sustainability, efficiency, accountability, and ownership of their development results. It has the potential to

(i) Reduce Africa's dependency on external flows, thereby extenuating the damaging effect of resource volatility, and minimizing vulnerability to external shocks

(ii) Give African countries flexibility and greater policy space, increased ownership of development process as well as strengthen the capacity of African States

(iii) Create positive externalities and send optimistic sign to donors and investors, thereby augmenting external resource inflows. Coupled with deployment of other (innovative) financing solutions, hopes could still be high that the continent will overcome its development challenges.

Against this background, AfCoP had decided to launch an online discussion on the aforementioned topic as a means of sharing knowledge, spurring peer-learning and documenting perspectives and alternative financing options for Africa's development. The discussion was specifically focused on:

- Identifying and documenting alternative strategies for financing developing intervention on Africa.
- How can African governments maximize domestic resource potential to sustainably finance Africa's development?
- What policies should government enact to encourage local investment, foreign direct investment to support national development efforts?
- What are the roles of the state and non-state actors to curb illicit financial flows from the continent?

The following sections present results of the discussion, summarized around the issues/ideas identified during the process, supported by the relevant research work.

Brief Historical Account of Development Financing Related to Africa

Hopes have long been expressed for Africa's socioeconomic development alongside other developing regions. This especially dates back to the end of the Second World War, in the late 1940s to early 1950s when development economics emerged with Foreign Aid as instrument for transforming underdeveloped nations. Special reference was made to the success of the Marshall Plan with US resources in the reconstruction of war-turned Europe. Development initiatives that have been documented since then included the UN measures for the economic development of the underdeveloped countries (1951); the equity-through-growth perspective of the 1960s; the MacNamara initiative of the 1970s with the integrated rural development programmes; the structural adjustment programmes of the 1980s and 1990s; and the current initiatives such as the poverty reduction strategy papers and the UN Millennium Development Goals flanked by series of development aid effectiveness pacts.

Yet, suffering has continued in Sub-Saharan Africa (SSA). About 50 percent of the region's population is still poor at a daily expenditure benchmark of US$1.25, which will shoot up to 70 percent if the benchmark of US$2 per day was used. A total of 36 out of the 50 poorest countries in the world are

located in this region. Between 1970 and 2000, the most aid-dependent countries recorded annual growth rate of -0.2 percent; Africa's growth and poverty have worsened despite the fact that over US$ 1 trillion has been provided in aid since the 1940s.2 It is argued that, the latest global development initiatives—the PRSPs, the MDGs, accompanied by series of aid effectiveness pacts—are old wine in new bottle pursuing harmful conditionality on developing economies as experienced with the Structural Adjustment Programmes. As the UN MDGs come to an end with many countries not achieving as much, the question is what would be the solution to sustainable development financing for Africa?

Thoughts on Alternative Development Financing Solutions

The need for a focus on domestic financing

Schools have argued the need to focus the search for sustainable development financing in Africa on domestic resource mobilisation. This viewpoint has gained attention with increased global economic and political crises leading rich countries to focus on their domestic issues. Resources for international cooperation are getting smaller with these developments.

In the following paragraphs, we will highlight perspectives as to how more resources can be mobilised within Africa.

Improved Institutions as Sustainable Resources: Indeed, "questions relating to financing for sustainable development cannot be effectively answered without taking into consideration the institutions through which such financing may be channeled." Quembo Fernando has ably argued this point during this online discussion, as well as Ashraf Ghani and Clare Lockhart in their Fixing Failed State Book. Quembo has argued that the most sustainable development financing is taxation. It is the traditional (and is more predictable) source of revenue for the state. But it requires good institutions and enabling environment to attract both domestic and foreign private sector investment to stimulate economic activities and growth. Ghani and Lockhart have argued that the rule of law and its effective application are leading functions of the state for efficient mobilization and utilisation of resources. "Rules are resources just as finances are resources that the state can use….Without these rules, things would fall apart."

The arguments for taxation relate to the resource curse debate. The curse explains how the ease of accessing natural resources and foreign aid in weak governance systems diminishes the incentive to work hard; to plan better for prosperity; and to industrialize. In these environments, investment in education, technology and economic diversification is low; and accountability to the people is diminished because the share of taxation which would pull them to hold the state accountable is meagre in the state budget, as most of the revenue is either aid, oil, diamonds or other natural assets that are not supplied by the people, so the state may not feel so compelled to account. Good institutions are indeed resources, and with them more can be achieved with less in Africa as elsewhere.

- ***Knowledge as a Sustainable Resource***

Many parts of Africa have continued to witness endemic illiteracy, which has held back growth and undermined sustainable financing in the continent. Paul Romer had raised arguments along these lines long ago, supported by Samson Mangasin in this online discussion. Romer had argued: "Higher living standards result from steadily improving knowledge of how to produce more and better goods and services with ever smaller amounts of physical resources. No amount of savings and investment, no policy of macroeconomic fine-tuning, and no set of tax and spending incentives can generate sustained economic growth unless they are accompanied by the countless large and small discoveries that are required to create more value from a fixed set of natural resources." It is clear here that, education, knowledge, and technological advancement are foundational elements of sustainable domestic development financing, from an endogenous growth standpoint.

[2] Moyo (2009, pp.46-47)

- ***Development of Small and Medium Scale Enterprises (SMEs)***

For developing economies, such as the African Region, this is viewed as a crucial entry point into industrial advancement and sustainable development financing. The role of SMEs is particularly celebrated with regard to the success of the East Asia Economies: -

- It is a well-established fact that SMEs are engines of innovation, entrepreneurship, and economic growth in many developing counties. This was particularly evident in many fast growing East Asian countries where SMEs have played crucial roles in creating jobs, competitiveness, export stability, and growth.

- Small and medium-scale enterprises (SMEs) foster economic diversification. The experience of some East Asian countries such as Taiwan, Hong Kong and Thailand show that SMEs can also play a significant role in transforming the traditional economy into a more value-added and productive economy via vertical diversification. For example, the issue of diversification in Taiwan is conditioned by two key features of the firms that make up its manufacturing sector: an industrial structure based predominantly on small firms, and an outward-oriented trade regime. In 1986, for instance, these firms were responsible for 28.2 percent of total manufacturing output, 40.7 percent of overall manufacturing employment, and comprised of almost 95 percent of the total number of Taiwanese manufacturing firms. The predominance of SMEs has an important effect on the local capacity to undertake Research and Development activities.

- SMEs [in countries such as Hong Kong and Taiwan were known for their] extreme flexibility in rapidly filling even small orders, attention to quality and design, audacious bidding, participation in complex networks of subcontracting, and enhancing international laws such as those regarding intellectual property rights….[and] many textile and clothing products imported by the EU, US and other developed countries today originate from Chinese villages, and some are even produced in farmers' houses.

This strategy will certainly fill critical gaps in African development financing if pursued effectively. It can bring about successful transformation of the agricultural sector and the informal economy using successful SMEs as intermediaries for facilitating the participation of smallholder farmers and informal operators in the supply/value chains through established networks with large firms, fostering forward and backward linkages. This has positive implication for gender and women development noting that a vast proportion of small business operations and farming activities are run by women in Africa.

- ***High rates of gender disparity as development financing potential***

Unlocking Africa's growth and poverty reduction potential greatly owes to the continent's commitment to reducing gender disparity. To the extent that high rates of gender disparity have substantially marked down the continent on the global human development index, closing this gap would translate to opening growth and poverty reduction opportunities. It is noted that countries that have effectively minimized gender biases and promoted women`s participation in socioeconomic activities have recorded spectacular levels of economic growth and poverty reduction. Overcoming cultural stereotypes among other factors constitutes major challenges to efforts aimed at maximising this potential: women`s education has been discouraged in many countries in Africa—e.g., in 2005, women literacy in Chad, Burkina Faso, Guinea, Mali and Niger only ranged from 15 to 18 percent; and teenage pregnancy rates continue to remain high in many others, going as high as 45-50 percent and beyond. Overcoming these structural factors implies releasing growth and poverty reduction potentials for the continent.

- ***Maximising Africa's Demographic Dividend***

With about 45 percent of Sub-Saharan Africa's population below 15 years, Africa's potential to earn demographic dividend, and hence accelerate

its economic and poverty reduction is huge. However, this presupposes minimum investment in healthcare, education, and social protection. The current epidemic crisis in West Africa explains some of the key challenges we need to overcome to maximise our demographic potential. With ageing populations and less young people threatening economic sustainability of other parts of the World, our young and youthful population presents us with a comparative economic advantage in the years to come if the requisite investment in our young population is done now.

- ***The Natural Resource Wealth of Africa***

Africa is still endowed with natural resources. As certain types of resources such as diamonds drawdown in deposit in a number of countries, other minerals such as oil and gas are being discovered. Indeed, the more resource discoveries are made in Africa, the more concerns are expressed about these issues adding to the resource-curse, create worries of the continent for their implication for conflict and worsening of poverty. However, these concerns could be overcome if mechanisms such as establishing sovereign wealth funds and improvement in institutions in general are undertaken. Substantial proportion of such funds can be set aside to support various development programmes such as infrastructural development, education, research and development, and economic diversification through development of SMEs and manufacturing. The establishment of these funds should be underpinned by a state of the art monitoring to ensure probity in their implementation.

Financing from Other Fronts

- ***South-South Cooperation***

Cooperation among developing countries has the potential to substantially alleviate financing problems among these countries. Technical assistance offered within these partnerships can better respond to priority needs in the continent as countries involved may share similar development challenges. Assistance provided with these partnerships can be rapid and more predictable. Strengthening regional economic communities (RECs) is therefore very critical within Africa for fostering south-south cooperation within the region.

- ***Exploring Issuance of Diaspora Bonds***

Asian countries such as China, Korea, and Taiwan are noted to have hugely benefitted from their population in the Diaspora. Sierra Leone is pursuing this in its current national development strategy, the Agenda for Prosperity, as an alternative non-traditional source of financing development:

Studies have indicated that diaspora bonds have an enormous potential to promote growth and development in Africa. Diaspora bonds are issued by the country to its diaspora to tap into their assets in the destination country, as an alternative to borrowing from other sources. Diaspora bonds are typically used to finance large scale infrastructure development projects in the private sector, and are generally used by a country to implement its development strategy. Moreover, proceeds of diaspora bonds could be earmarked to projects with appeal to the diaspora, such as infrastructure projects, housing and social amenities.

- ***Public Private Partnerships***

Promoting public private partnerships (PPPs) have been identified as part of the emerging innovative development financing that Africa could effectively explore. Special AfCoP online discussion was dedicated to these financing strategies during June 30th to July 21st 2014:

By the 1990s, public utilities—such as road infrastructure, telecommunications, and water and sanitation—had largely failed in attempts to provide these services to citizens through government systems including those in Africa. The causes of undersupply of services through government included persistent inefficiency, weak pricing policies, and corruption. Private managements through establishing public corporations were some of the attempts to redress these deficiencies. A greater shift to ensure further reduction of political influence in service provision was the introduction of more robust PPPs where private operators were

granted exclusive concession to provide and manage services independent of government, and these have been successful in a number of cases in Africa, the N4 Toll Road from Witbank in South Africa, to Maputo in Mozambique being an example.

- ***Broadening Corporate Social Responsibility***

Corporate social responsibility will provide much needed fiscal space for Government to pursue certain programmes. Government will therefore legitimise a corporate social responsibility framework in order to ensure that companies meet their respective responsibilities as required by law.

Conclusion and Recommendations

Lessons learned from development financing since the end of the Second World War suggest that the solution to Sub-Saharan African problems lies in the optimization of institutions. It calls for building capable and effective states founded on strong accountability systems. With this, more can be achieved with less, as witnessed in a number of East-Asian countries some of whom emerged global economic power with a few natural resources. Thus:

- AfCoP and Partners should continue engagement in the region on accountability issues.
- Support educational programmes, small scale business development, and youth empowerment. This is fundamental in the building of the needed critical mass for the development of small scale industries for mass employment, income generation and sustainable mobilisation of state revenues.
- Support in-depth studies on the various financing options and related issues generated in this discussion for better lessons and replication across the continent.
- Organise additional and special online discussions on some of the financial options and related issues highlighted above for deeper insights and better policy responses and engagement with relevant stakeholders.

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Acknowledgement

This knowledge series is intended to summarize good practices and key policy findings on managing for development results. AfCOP Knowledge products are widely disseminated and are available on the website of the Africa for Results initiative (AfriK4R), at: www.afrik4r.org/page/resources .

This AfCOP-MfDR knowledge brief is a joint work by the African Capacity Building Foundation (ACBF) and the African Development Bank (AfDB). This is part of the knowledge products produced by ACBF under the leadership of its Executive Secretary, Professor Emmanuel Nnadozie.

The product was prepared by a team led by the ACBF's Knowledge, Monitoring, and Evaluation Department (KME), under the overall supervision of its Director, Dr. Thomas Munthali. Within the KME Department, Ms. Aimtonga Makawia coordinated and managed the processes of producing the product while Dr Barassou Diawara, Dr Patience Mutopo and Mr. Kwabena Boakye and other colleagues provided support with initial reviews of the manuscripts. Special thanks to colleagues from other departments of the Foundation who also supported and contributed to the production of this paper. The ACBF is grateful to the Africa Development Bank which supported production of this MfDR case study) under grant number 2100150023544.

ACBF is also grateful to Dr Sheka Bangura who moderated the online discussion of AfCOP members from which thisknowldge brief was developed. The Foundation also wishes to express its appreciation to AfCoP members, ACBF partner institutions and all individuals that provided inputs critical to the completion of this product. The views and opinions expressed in this publication are the reflections of the discussants and the moderator. They do not necessarily reflect the official position of the ACBF, its Board of Governors, its Executive Board, nor that of AfDB management board and the secretariats of the AfCOP- MfDR project