

WIDER Annual Lecture 22

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The Political Economy of Structural Transformation: Has Democracy Failed African Economies?

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Motivation

- My lecture today is influenced by three seemingly unrelated experiences:
 - Economic reforms in Ghana and elections in 1992. Fixing the problem in 1993 and beyond. “We didn’t ask you to win the elections”
 - First visit to Ethiopia in 1994 at the invitation of the Ethiopian Economics Association: “There will never be a change in our land tenure system so long as I remain Prime Minister”
 - Recent visit to Rwanda: Significant improvements without functioning democracy

Presentation Outline

- ✓ Background
- ✓ The Unchanging Structure of Africa's Economies
- ✓ Explaining the Absence of Structural Transformation
- ✓ Making Economic Policy and Development Decisions
- ✓ The New Political Environment and Planning for Structural Transformation
- ✓ Summary and Conclusion

Main Arguments

- The lecture seeks to show that if economic management efforts of the last several decades have not led to structural transformation, it is not simply a question of whether democracy and associated practices are good for Africa.
- The main argument is that African governments have not adapted democracy appropriately for the purpose of building institutions that generate the reforms to support structural transformation.
- Thus, even when governments express interest in long-term development, they manage this interest in a short-term framework and look out for immediate outputs.
- I will argue that appropriate policy and institutional reforms for structural transformation must be anchored in long-term development frameworks and institutional structures.

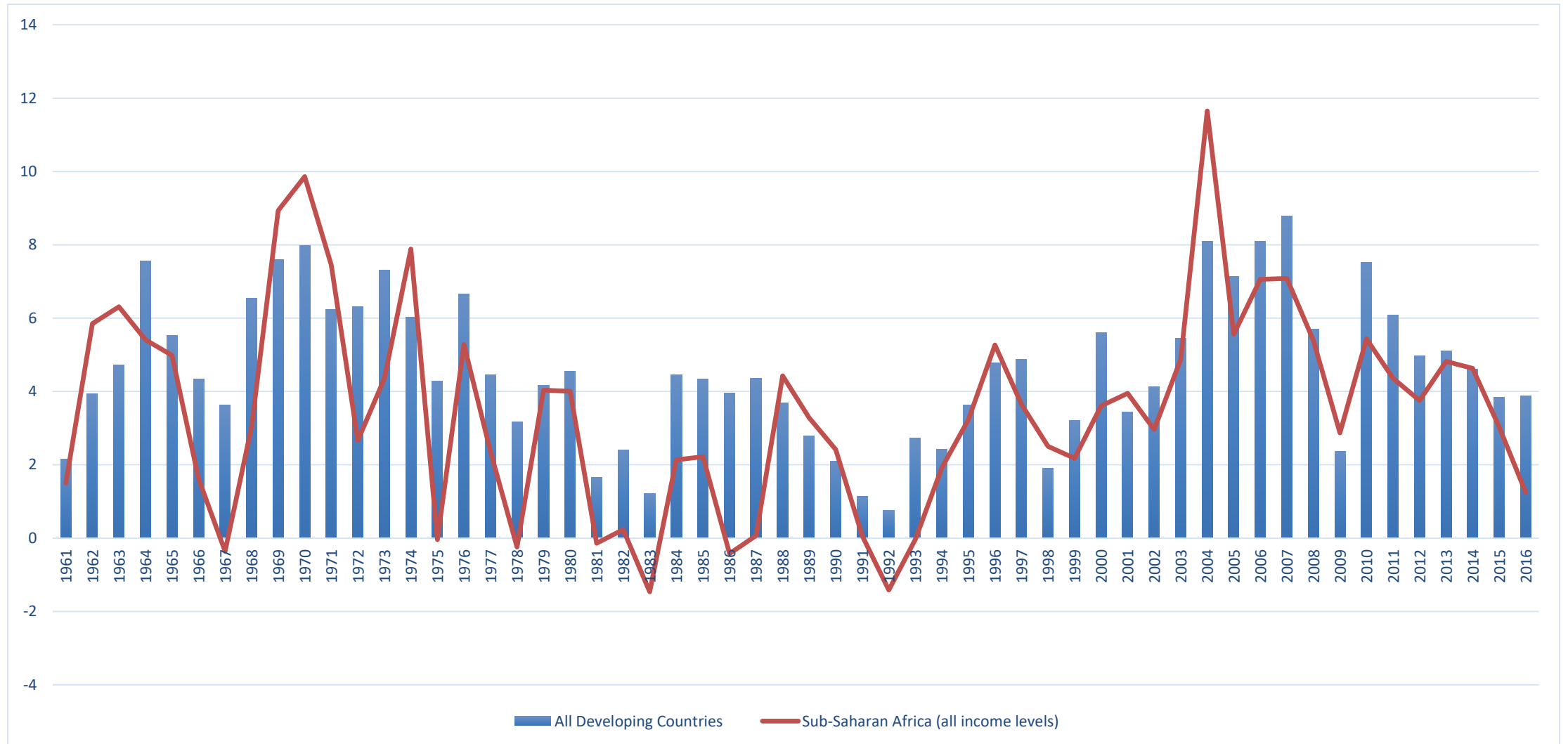
1. Introduction

- The positive stories: Growth in Africa has been good in recent times
- The not-so positive stories: Africa will be home to the largest number of extremely poor people by 2013
- The structural transformation debates: Can Africa survive without structural transformation
- Structural adjustment and after: Did we simply learn to survive?
- Leadership and institutions: Was Barack Obama right?

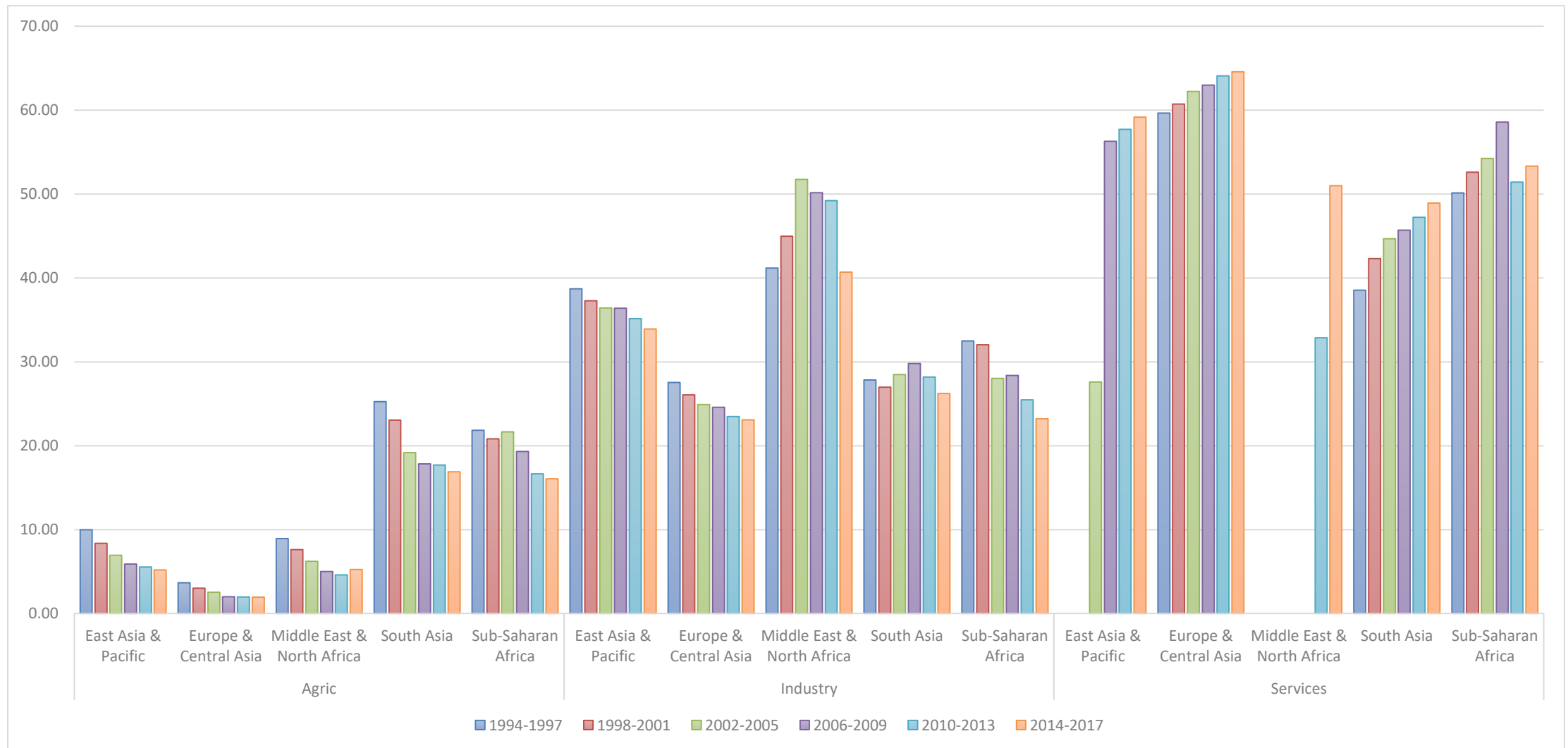
2. The Unchanging Structure of Africa's Economies

- Four essential and interrelated processes define structural transformation in any economy Timmer (2012),. These are;
 - a declining share of agriculture in GDP and employment,
 - A declining rural-to-urban migration underpinned by rural and urban development;
 - the rise of a modern industrial and service economy;
 - and a demographic transition from high rates of births and deaths to low rates of births and deaths.
- This calls for growth that is inclusive and sustainable. The proceeds of such development should be shared fairly in terms of demographics, geographic, vertical and sustainable (now and the future) profiles.
- There is renewed interest in the literature on structural transformation. The literature reflects a growing realization of the relevance of dual economy models other than the Solow model for studying the process of growth in developing countries (Temple, 2005).
- Despite good growth experiences the region still suffers from volatility in commodity prices.

GDP Growth Rate (1960-2016)



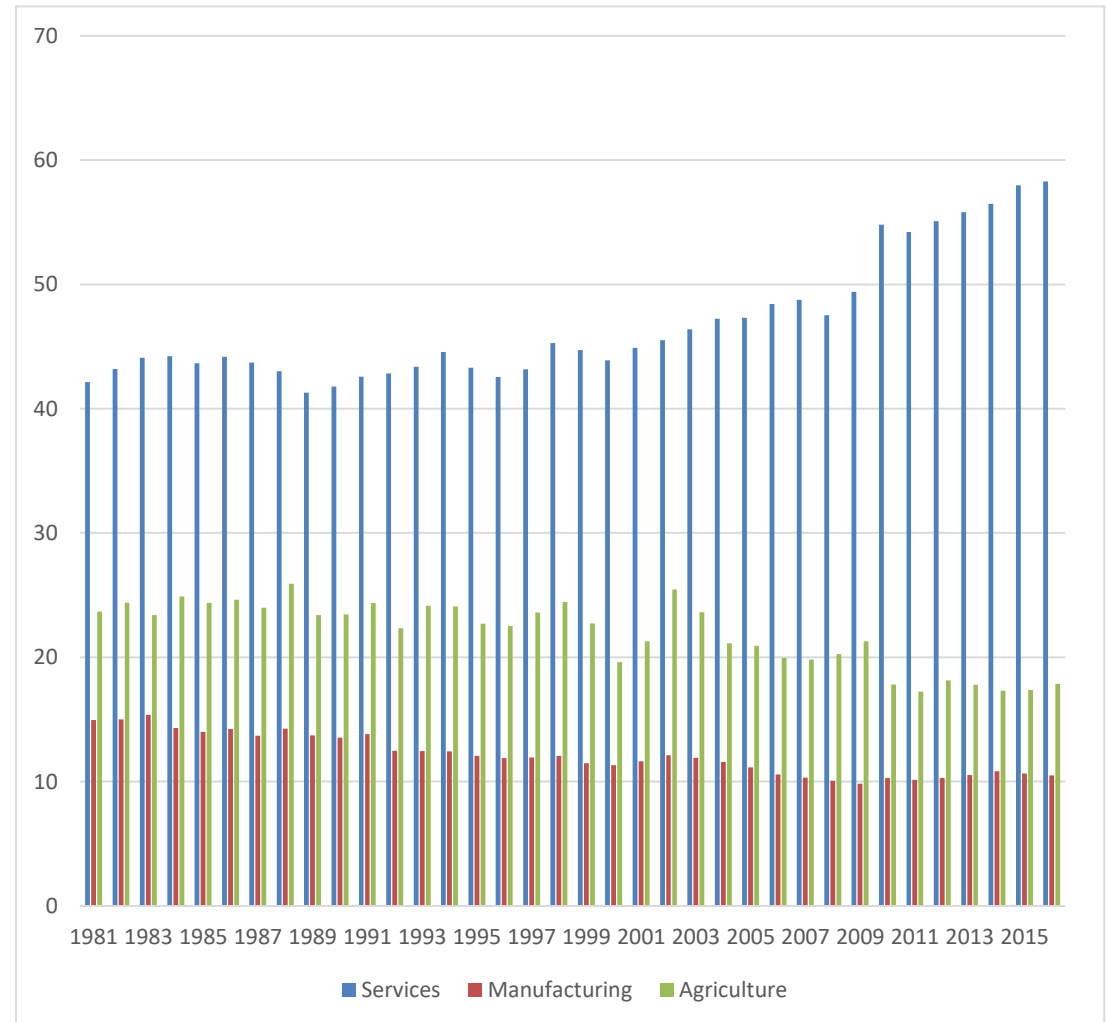
Sectoral Contribution to GDP across Regions (1994-2017)



The Unchanging Structure of Africa's Economies

- Following the structural transformation growth hypothesis, the contribution of the agriculture sector to GDP declined from 23.9% in 1981 to 17.6% in 2016. The contribution of the service sector to GDP increased from 42.1% in 1981 to 58.3% in the same period.
- The manufacturing sector on the other hand had its share drop from 14.95% to 10.49% in that period. On a positive note, raw agriculture export as a percentage of merchandise export declined from 9.5% in 1974 to 2.2% 2014. At the same time, manufacturing export as a percentage of merchandised export increased from 12.04% in 1974 to 23.9% in 2014.

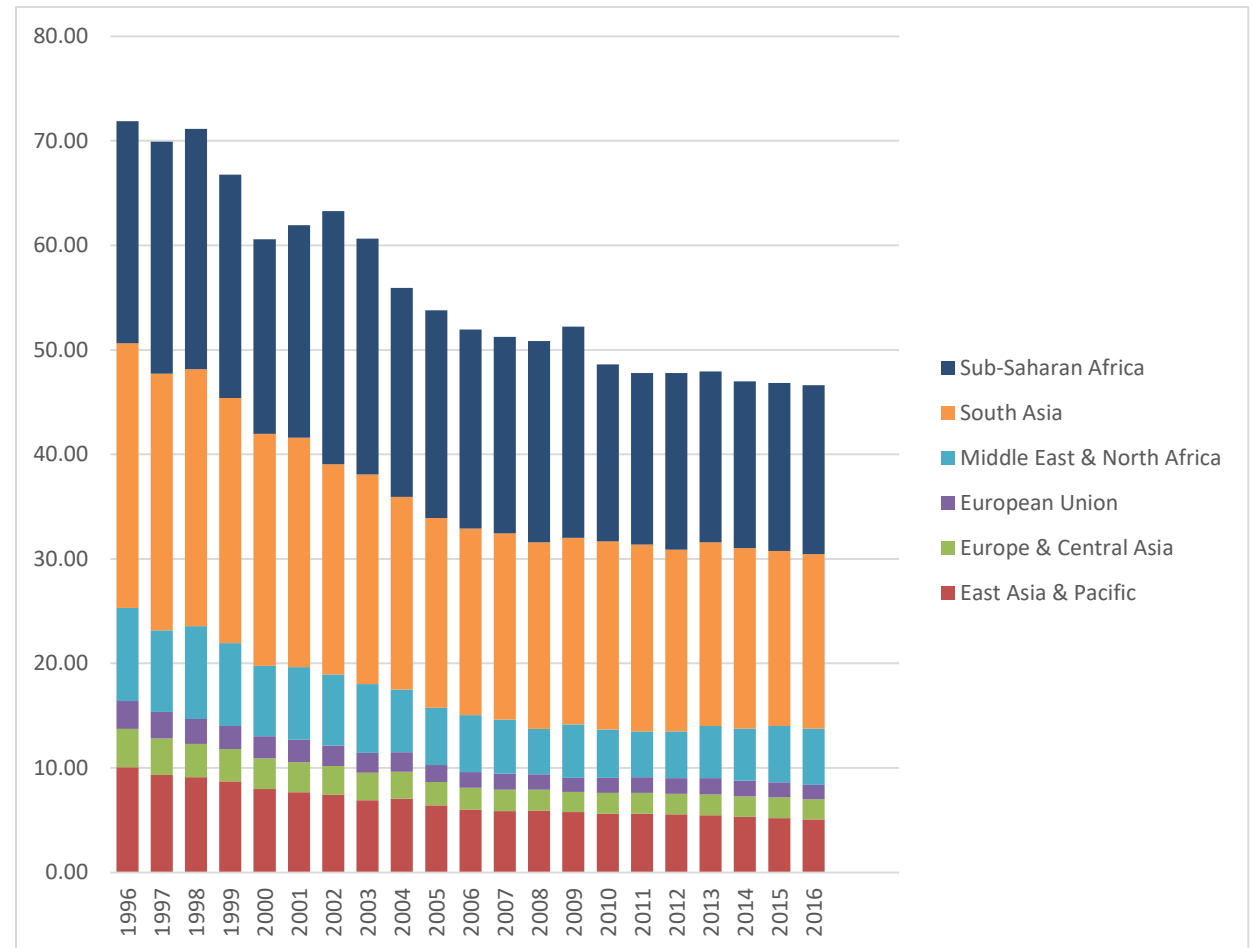
Sectoral Contribution to GDP in Africa (1981 to 2016)



The Unchanging Structure of Africa's Economies

- The share of agriculture to GDP in Africa shows how important agriculture is to national output compared to other regions of the world.

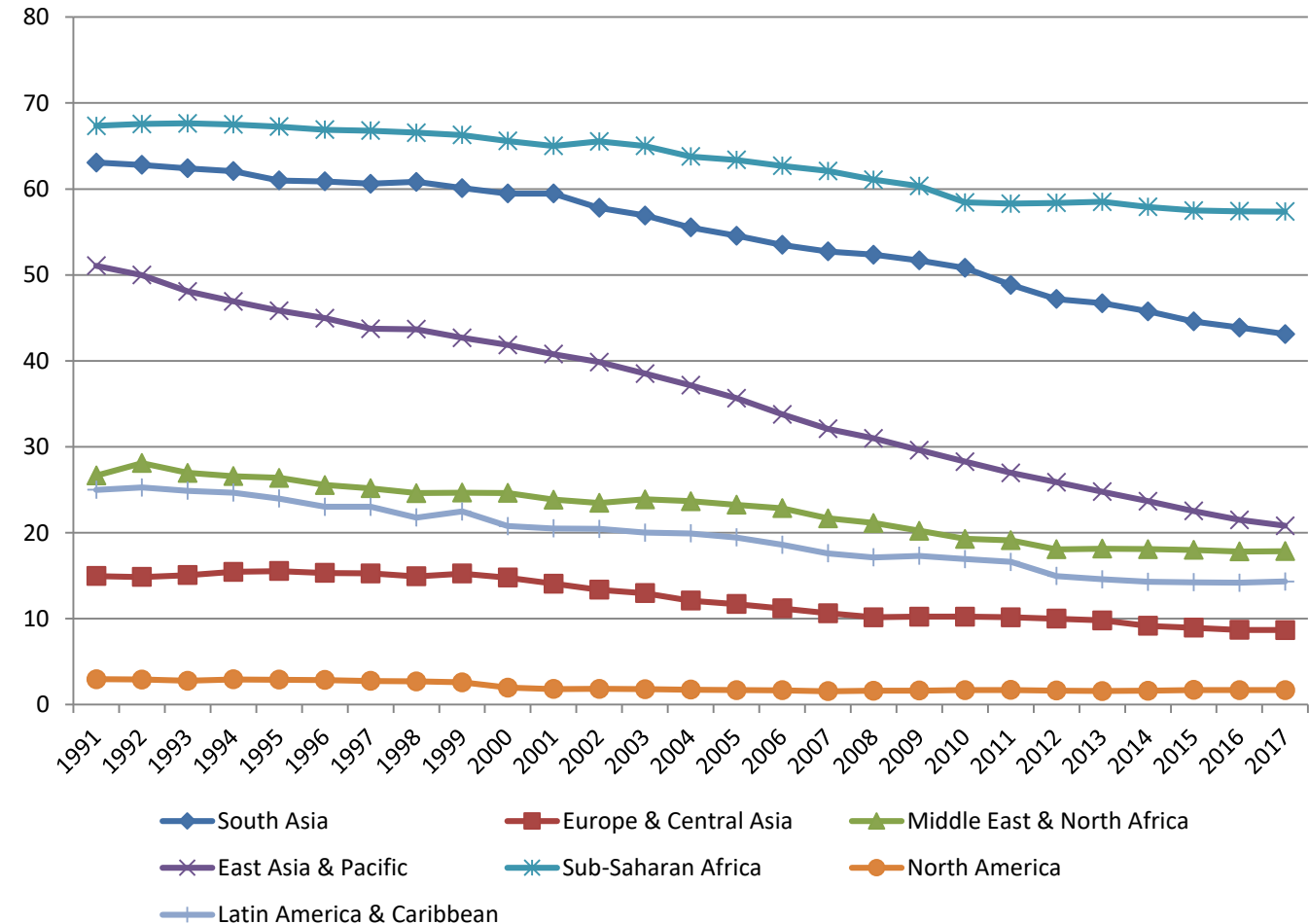
Agriculture, forestry and fishing value added (% of GDP) across regions (1996-2016)



The Unchanging Structure of Africa's Economies

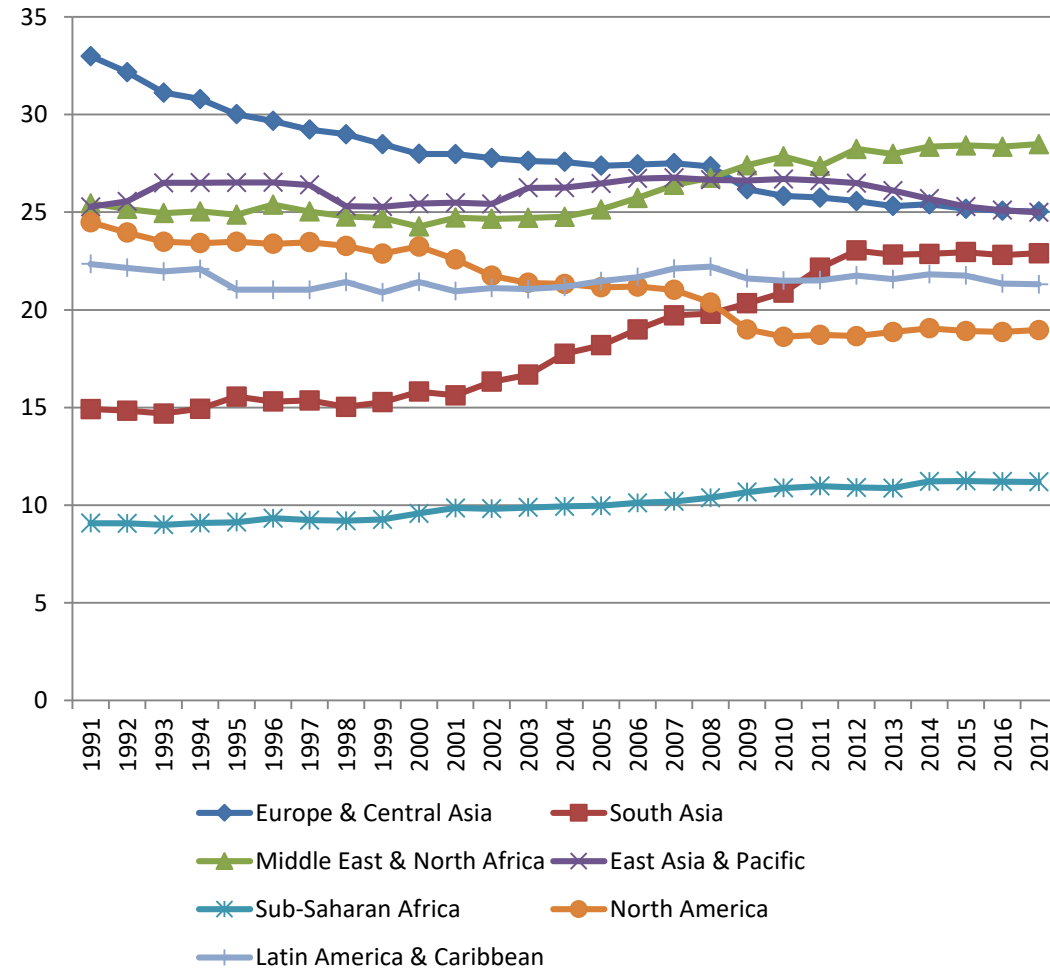
- Whereas in a normal process of structural transformation, labour moves from rural agriculture to urban manufacturing, the case in Sub-Saharan Africa has been different.
- The proportion of the labour force in agriculture is as high as 80% in some countries.
- The high share of the labour force in agriculture is an indication that the potential for structural change to lead to growth and poverty alleviation in Africa is equally enormous.

Contribution of Agriculture to Total Employment (%)

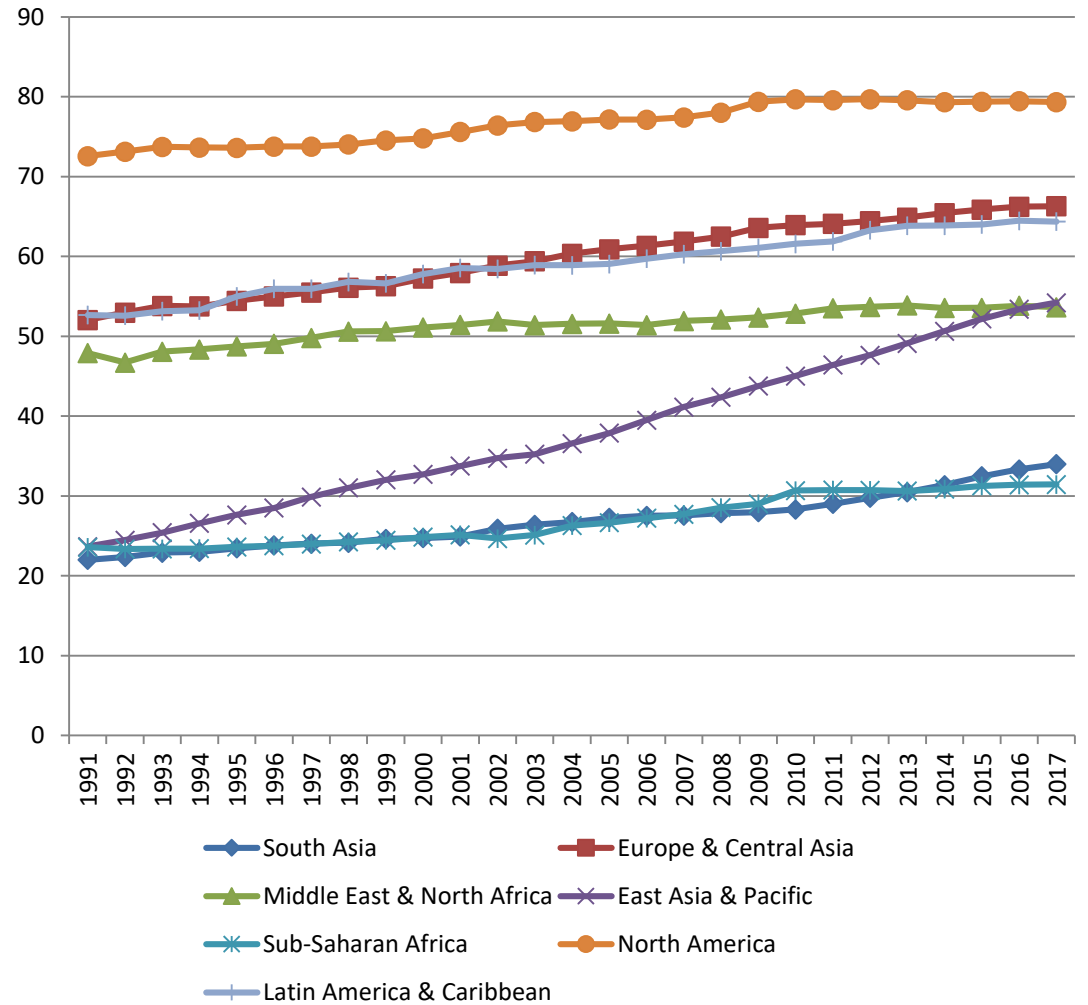


The Unchanging Structure of Africa's Economies

Contribution of Industry to Total Employment (%)



Contribution of Services to Total Employment (%)



The Unchanging Structure of Africa's Economies

- The growth trajectory of Sub-Saharan Africa is missing a very important middle section (the industrial sector with high labour absorptive capacity) in order for structural transformation to occur.
- In almost all African countries, agriculture's share of employment is significantly higher than its share of GDP. This raises important questions about productivity within the agricultural sector.
- According to Rodrik (2014), the trend of labour transition to both the services and the informal manufacturing sectors reverses transformational growth.

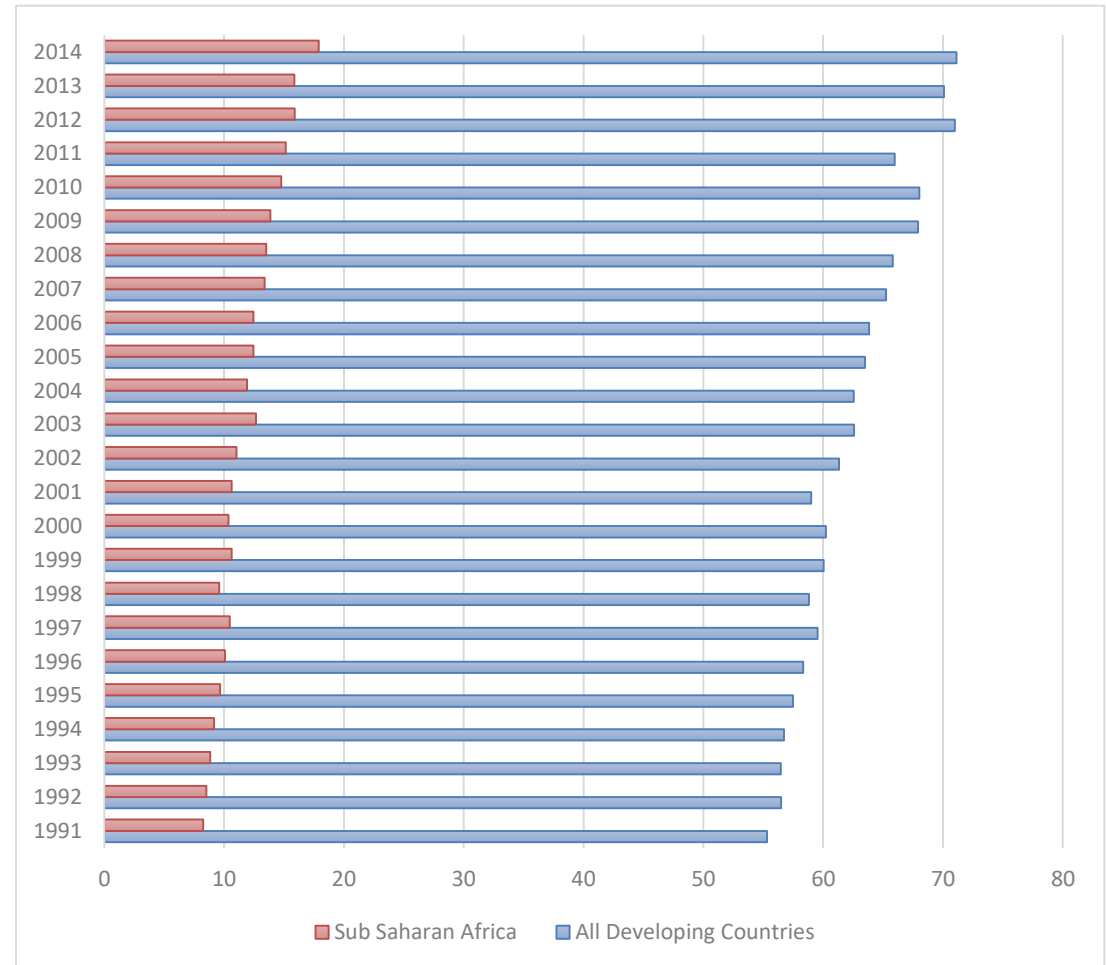
3. Explaining the Absence of Structural Transformation

- Although most African countries have passed laws and instituted policies that encourage development of the manufacturing/industry sector, not much has been achieved. Some of the factors identified include;
 - lack of electricity access (Bhattacharyya 2012),
 - weak institutions (Bratton 2007) and
 - unfavourable business environment (Rodrik 2014 and Gelb et al. 2014).

Explaining the absence of structural transformation

- On electricity access, Chirambo (2016) estimates that less than 40% of the population of SSA have access.
- Rural areas access rate is 17.9% (est)
 - 71.1% for all developing countries.
- Gelb et al. (2014), list factors that prevent Africa from attracting investments into the manufacturing sector as;
 - corruption
 - high cost of power
 - non-enforcement of contracts
 - poor security and transport infrastructure
 - and policy uncertainty as
- Rodrik (2014) calls these factors '**business climate**'

Rural Access to electricity



Explaining the Absence of Structural Transformation

- Following neoclassical growth theory, poor countries would be expected to grow faster than rich countries. By having a low capital-labour ratio poor countries are expected to enjoy higher or increasing returns on investments.
- Rodrik (2014) stresses that since developing countries have access to global markets, they can expand production of tradable goods that they have comparative advantage in quickly to spur growth.
- Based on these assumptions, some economists find it strange that Africa did not take off to catch up with more developed economies. The Solow Model (Solow 1956) predicts convergence based on capital accumulation.
- The divergence in growth performance has led to controversy over policy prescriptions or expectations about their effectiveness. The role of the state, roles of institutions, etc. have become key.

Explaining the Absence of Structural Transformation: The new structural economics

- Lin (2011) proposed the “new structural economics” as the third wave of development economics, arguing that economic development is an evolutionary process involving industries, technologies, infrastructure and institutional mechanism, in which a “facilitating government” is also indispensable in addition to an “effective market”.
 - According to Lin, the “structuralism”, or the first version of development economics, advocates the construction of an industrial structure identical to that of developed countries and stresses on the role of government while downplaying that of market; the “neoliberalism”.
 - With structural rigidities, the new structural economics believes, failure to develop advanced capital-intensive industries in developing countries is endogenously determined by their endowments. The relative scarcity in their capital endowment and/or the low level of soft and hard infrastructure in developing countries make reallocations from the existing industries to the advanced capital-intensive industries unprofitable for firms in a competitive market.
 - In an increasingly globalized world, Lin sees opportunities for developing countries to counter negative historical trends by diversifying their economies through the building of industries consistent with their comparative advantage in order to accelerate growth and achieve convergence by exploiting the advantage of backwardness in an open, globalized world.

Explaining the Absence of Structural Transformation

- On infrastructure, the new structural economics dictates the need for the state to assume its leadership role in the provision and improvement of hard and soft infrastructure in order to reduce transaction costs on individual firms and also facilitate the economy's industrial development process.
- Historically, all countries that have successfully transformed from agrarian to modern advanced economies, including the old industrial powers of Western Europe and North America, and the newly industrialised economies of East Asia have had governments that played a pro-active role in assisting firms to surmount inevitable challenges. Yet, almost all governments in the developing world have attempted to play this facilitation role at some point, but failed.
- Thus, consensus seem to exist among economic historians on the relevance of the state facilitating structural change and helping sustain it across time and across developed countries.
 - However, except for a few successful cases, governments in most developing countries have failed to play that desirable role.
 - The question that follows is why have structural change and the associated growth eluded most SSA countries?
 - This multi-faceted question raises a number of political economy issues relating to the political will of most governments to pursue the long-term vision of structural transformation when particularly operating in democratic dispensations where electorates generally want results within short term election cycles.

Explaining the Absence of Structural Transformation

- Interestingly, two to three decades ago in Africa reforms came largely as part of the *Washington Consensus* and often had very limited local input. As a result, since structural transformation was not on the donor development agenda it did not get translated into the programmes of various countries pursuing reforms.
- Reform of the public financial management system in most countries however, received considerable attention via budgetary processes and the management of public finances. Very little effort went into linking budget preparation to structural transformation.
- The budget is no more a document for few elites, but a policy document produced through the interaction of the executives, the legislature and citizens (Robinson, 2006).
 - The agency theory states that the principal (citizens) should be able to hold the agent (government) accountable in its budget statements.
 - In a participatory budget process, citizens can be involved in debating fiscal priorities, and directly contribute to the budget formulation, implementation and monitoring (Bräutigam, 2004). However, this has not been the case in all countries in Sub-Saharan Africa where some elected officials (President and Parliamentarians-agent) have little incentives to involve citizens in the budget making process (Rios et. al. 2014).

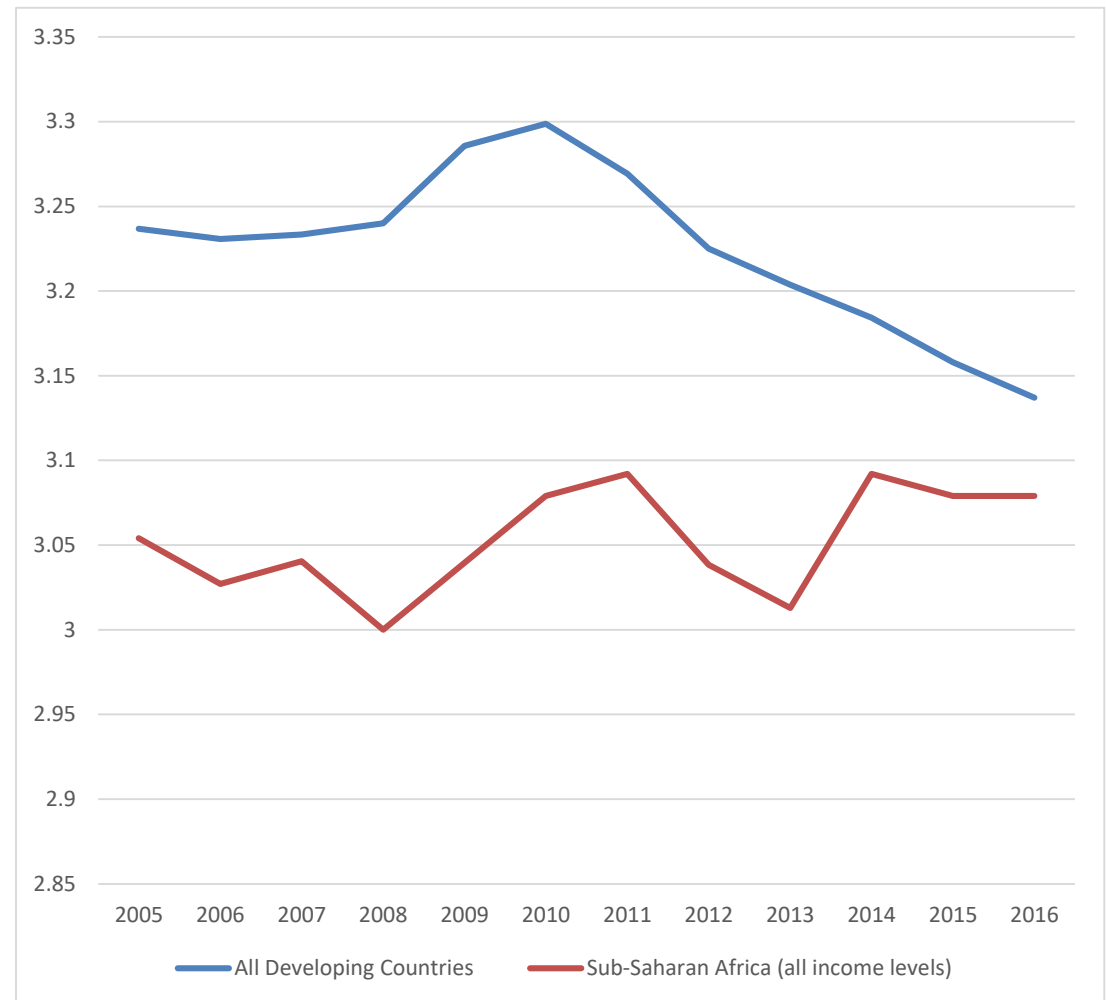
4. Making Economic Policy and Development Decisions

- Preparing for economic reforms in the 1980s and 90s
 - The role of the development partners
 - The role of local intellectuals and other national interests
- Improving budget processes in developing countries
 - Africa inherited its budget framework from the colonial era with little or no modification (Gollwitzer, 2010).
- There is no evidence that improved budgetary processes have had any influence on planning for structural transformation

Making economic policy and development decisions

- Siebritz and Calitz (2006) found many African countries inherited a fragile public finance system that was characterised by a narrow tax base which were made worse by deficiencies in plan formulation and implementation and absence of reliable data (Tarp, 2002).
- These challenges were compounded by high post-independence expenditures. Though some of the expenditures were on important public infrastructure, others were spent on loss-making state enterprises and huge subsidies.
- According to Hameed (2005), countries that have transparent public financial systems have greater financial discipline and have lower levels of corruption as well as better credit ratings.

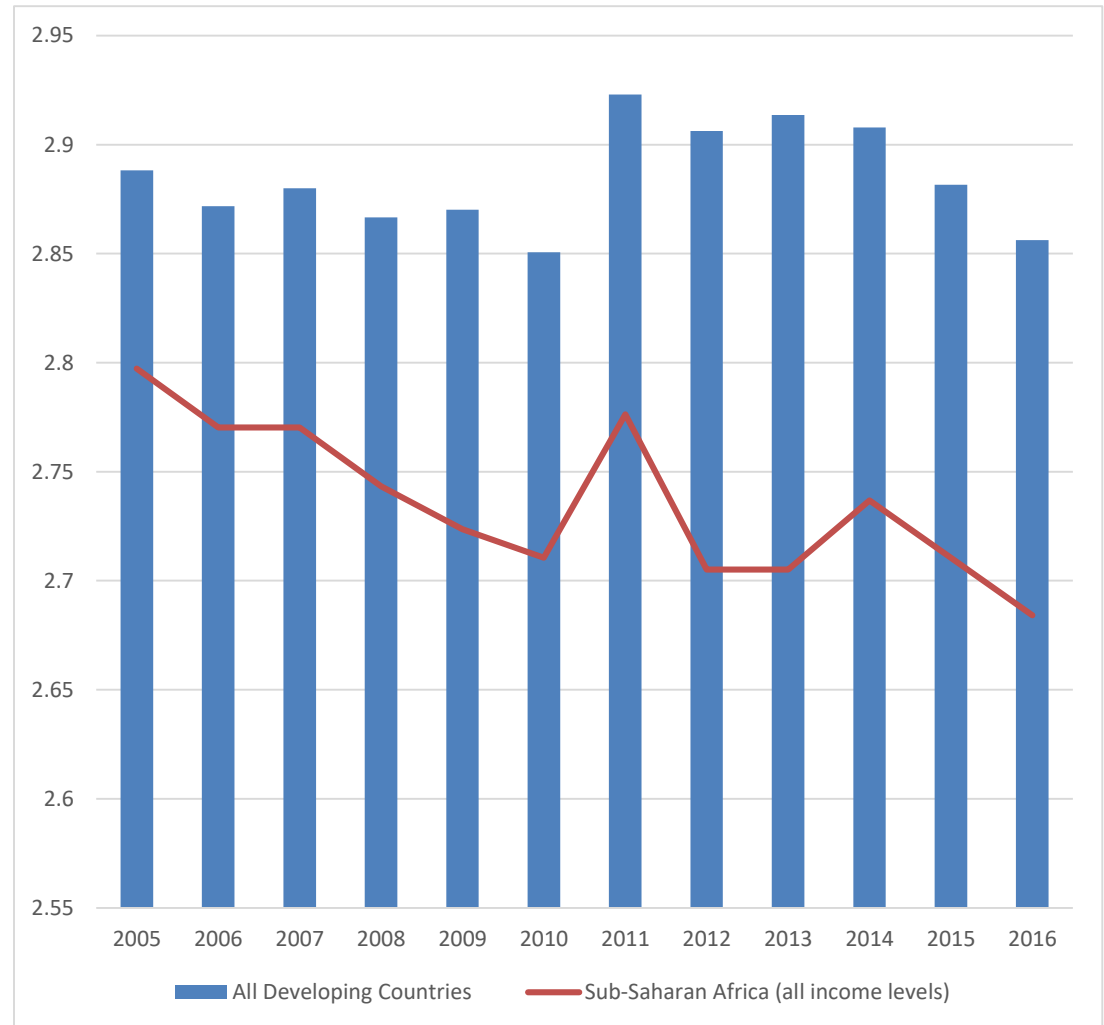
Quality of budgetary and financial management (1=Low to 6=High)



Making economic policy and development decisions

- In a study of 26 SSA countries on budget transparency, De Renzio and Simpson (2013) concluded;
 - only Uganda and South Africa published a full set of 8 budget documents.
 - Botswana, Kenya, Liberia, Mozambique and Tanzania published 6 or 7, not publicizing a couple.
 - At the bottom, Equatorial Guinea published none of their budget documents, while Benin, Rwanda, Chad and Niger published only the approved budget.
- The Transparency, accountability, and corruption in the public sector indicator measures the extent to which public officials, including the executive and civil servants can be held responsible for their actions and use of public funds by the citizens, the legislature and judiciary.

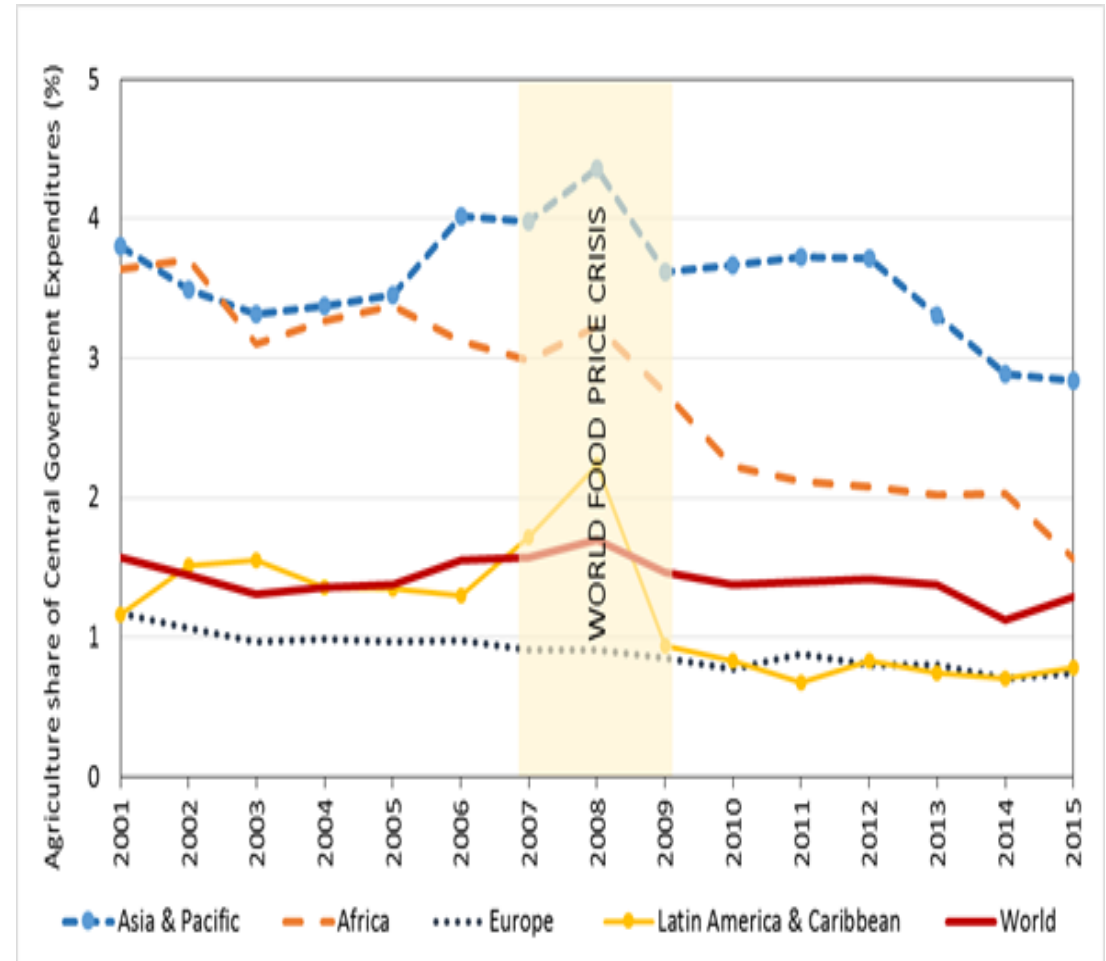
Transparency, sector accountability, and corruption in the public



5. The New Political Environment and Planning for Structural Transformation

- Beyond *Washington Consensus*, what do African nations want to achieve now in terms of development?
- The African Union has set forth Agenda 2063 in which there is the aspiration towards a prosperous Africa based on **inclusive growth and sustainable development**.
- Most African nations emphasize two things in discussions of future development and the well-being of their people.
 - The modernization of agriculture (Aryeetey 2012)
 - And industrialization (Aryeetey and Moyo 2011)

Agriculture share of government expenditures by region, 2001-2015



The New Political Environment and Planning for Structural Transformation

- Whereas African governments committed themselves under the Comprehensive African Agriculture Development Programme (CAADP) to spend at least 10% of annual national budgets on agriculture in pursuit of the MDGs very few of them managed that by 2015.
- In the case of industrialization, similar to agricultural modernization, most development blueprints in Africa emphasize a strong interest in manufacturing and value-added production processes.
 - Most of the effort has often gone into an assortment of tax incentives and infrastructure at export-processing zones or other locations.
- industrial policy which is a coordinated actions of government to reallocate resources to industrial development has had several negative experiences over the post-independence period in Africa.
- Most people that have written about industrial policy for development in Africa have argued on the basis of what has been referred to as horizontal and vertical policies.

Democracy and Economic Decision-making

- Between 1960 and 1982 most African nations were politically unstable. There were 56 attempted and 102 reported coup d'états in 25 countries (Johnson et al. 1983).
- After undergoing economic reforms the number of unstable regimes went down. During the period 2000-2016, there were 19 coup attempts, 11 of which failed (Powell and Thyne, 2016).
- The experience with economic reforms in the 1990s and beyond led to the understanding that the reforms could best be sustained with 'good governance' institutions and practices (Aryeetey 2012).
- Democracy and electoral cycles have been pursued in the region at different speeds and with varying scope and institutions (Olk 2003).
 - Organization of elections in the absence of a democratic system in countries like Angola, Cameroun, Equatorial Guinea, Democratic Republic of Congo among other oil producers is always viewed with scepticism.

Democracy and Economic Decision-making

- Gyimah-Boadi (2004) indicated that the total number of electoral democracies increased from a handful in 1989 to 18 by 2000. Although some African countries delink electoral democracy from political and civil rights.
- The literature on the link between democracy and economic growth is rather mixed.
 - the "conflict scenario": Elected officials take short-term views about policy-making (populism)
 - the "compatibility scenario": "political pluralism, institutional checks and balances and freedom of the press provide safeguards against system abuse or predatory behaviour often associated with authoritarian regimes"
 - the "sceptical scenario": no relationship can be found between democracy and development.

Democracy and Economic Decision-making

- Acemoglu et al. (2014) show that countries that have fully adopted democracy obtained benefits of about 20% increase in GDP per capita over the past 30 years. This translates to 0.6% increase in annual growth. The idea here is that democracy is more likely to lead to the protection of the rights of individuals, including property rights, essential for investment and growth.
- Fosu (2013) studied institutions and African economies and found that countries that have democratic regimes enjoy agricultural productivity and overall growth.
- The sceptical view is driven by the work of Barro (1997)
 - Esposto and Zaleski (1999) have suggested that the fact that there may be more economic freedom under a democracy does not provide any assurance that it will be fully utilised.
 - Essentially those who are powerful enough to capture state institutions are likely to use it to their advantage against the interest of others (Przewoski and Limongi, 1993).
- One of the more analytical sceptical pieces for Africa has come from the work of Kisangani (2006) who utilises a Generalised Method of Moments approach for a 37-country study. Unfortunately the analyses here ended in 1998.
- When Sirowry and Inkeles (1990) reviewed thirteen studies, they found six that supported the sceptical view.

Democracy and Economic Decision-making

- I take the position that it is possible to find all three scenarios of the relationship between democracy and economic growth and development in the region, and even possibly in a country at different points in time. The debate should not be about whether democracy is good or bad for economic growth and development.
 - There are weak democracies that are easily subject to elite capture as in the sceptical scenario. Here many of the oil exporting nations would easily fall into the category. Angola, Equatorial Guinea, Cameroun, Gabon and even possibly Nigeria.
 - The conflict scenario is very widespread as elected governments take short-term views about most things. Ghana, Cote d'Ivoire, Uganda, Zambia, Tanzania, Kenya, and Nigeria show clear elements of this.
 - The compatible scenario in Africa allows governments to pursue programmes that achieve macroeconomic stability and lead to economic growth.
 - Senegal is a good example of a democracy that achieves good results from time to time. Ghana and Nigeria have had good spells of macro stability and growth in the last two decades arising from good policies and somewhat effective institutions.
 - Kenya is a democracy that is able to attain macro stability but with unstable politics.
 - A very interesting outlier in the African story is Rwanda. It is not generally seen as a democracy, but has achieved considerable success in its economic development efforts

Conclusion

- What this paper has sought to do is to show that in Sub-Saharan countries, governments generally know what the long-term aspirations of the people are, but are not always inclined towards pursuing them as this might involve significant short-term costs that they do not believe the people can tolerate or accept.
- There are times when there is no general pressure on the government, whether from within or from outside, to pursue structural transformation in any direct manner.
- In the absence of structural transformation, generally positive economic management attempts lead to generally positive outcomes, even if slower than required or in other developing regions. Reforms in health, education, agriculture and financial management have started yielding fruit in a number of countries.
- When economic policies are perceived to be self-serving, they lead to episodic experiences of growth, poverty reduction and inequality at best.
- Thus African nations have no choice, but to go back to basics, relying on new technologies to pursue structural transformation
 - Modernising agriculture will require new technologies on different sizes of land, irrigation, agricultural credit, etc
 - Industrialising will require governments to be more selective than the literature suggests, partnering with the private sector as appropriate

Thank You