



THE AFRICAN CAPACITY  
BUILDING FOUNDATION

FONDATION POUR LE RENFORCEMENT  
DES CAPACITES EN AFRIQUE

# HARD TIMES: THE WORLD ECONOMIC CRISIS AND EMERGING CAPACITY CHALLENGES FOR AFRICA

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ACBF

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This Occasional Paper examines The World economic crisis, emerging capacity challenges for Africa and their implications for ACBF. The reflections and judgments contained in this paper are, however, those of the author and do not necessarily reflect the official position of the African Capacity Building Foundation.

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# **HARD TIMES:** THE WORLD ECONOMIC CRISIS AND EMERGING CAPACITY CHALLENGES FOR AFRICA

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# THE AFRICAN CAPACITY BUILDING FOUNDATION

ACBF is Africa's premier institution in Capacity Building. Established in February 1991, ACBF is the outcome of collaboration between African governments and the international donor community. The major sponsoring agencies of the Foundation are the African Development Bank (AfDB), the United Nations Development Programme (UNDP) and the World Bank. The International Monetary Fund (IMF) became a member of ACBF in 2002. The African Union is an Honorary Member.

ACBF's mission is to build sustainable human and institutional capacity for sustainable growth, poverty reduction and good governance on Africa. The Foundation intervenes in six core competency areas, namely, economic policy analysis and management, financial management and accountability, strengthening and monitoring of national statistics, public administration and management, strengthening of the policy analysis capacity of national parliaments, professionalization of the voices of the private sector and civil society.

Besides intervening directly in the area of capacity development, ACBF also provides a platform for consultation, dialogue, cooperation as well as information and knowledge sharing amongst development stakeholders and partners across the African continent.

The Foundation is present in some 44 sub-Saharan African countries and has committed more than US\$350 million to interventions in capacity development since its inception.

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## ABSTRACT<sup>1</sup>

The world economy has changed significantly in recent times. With greater financial globalisation, there emerged a mistaken perception that 'fathomless' capital was a pattern of this 'new world'. It soon became apparent that the recent financial crisis was a result of fragility in the financial system – in turn a product of limited/lack of transparency in the system. There has been limited understanding as to how the financial markets work – not only in the developing world where skills are in short supply – but more importantly by officials in the United States of America (US), European Union (EU) and Japan despite the fact that these blocks form 80% of global gross domestic product (GDP). Many EU countries have arguably remained highly uncompetitive and not ready to deal with the consequences of the global economic downturn. For policy relevance to exist, countries need to take reforms however painful they may be socio-economically. The paper sheds light on the implications for capacity building/development in Africa given the realities of the New Economic World order – especially new finance regulation issues, new international competition, crisis exit strategies and future technologies. The paper also draws possible roles that can be played by capacity building institutions such as the African Capacity Building Foundation (ACBF) by highlighting four major areas: (a) how the Foundation sources new ideas for capacity development; (b) what approaches to use for resource mobilization and partnerships; (c) how best to organize the work of the Foundation in knowledge sharing; and (d) what aspects need to shift in the operational programs of the Foundation to handle emerging issues. The paper concludes that Africa needs to develop capacity to respond to shocks effectively.

**Key words:** socio-economic fragility, financial globalisation, strategic partnership, capacity development, crisis exit strategies, structural reform.

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## I. INTRODUCTION

The world economy has changed significantly in recent times. With greater financial globalisation, there emerged a mistaken perception that 'fathomless' capital was a pattern of this 'new world'. It soon became apparent that the recent financial crisis was a result of fragility in the financial system – in turn a product of limited/lack of transparency in the system. There has been limited understanding as to how the financial markets work – not only in the developing world where skills are in short supply – but more importantly by officials in the US, EU and Japan despite the fact that these blocks form 80% of global GDP. Many EU countries have arguably remained highly uncompetitive and not ready to deal with the consequences of the global economic downturn. For policy relevance to exist, countries need to take reforms however painful they may be socio-economically. The purpose of this paper is to shed light on the implications for capacity building in Africa given the realities of the New Economic World order – especially new finance regulation issues, new international competition, crisis exit strategies and future technologies. The paper also draws possible roles that can be played by capacity building institutions such as the African Capacity Building Foundation (ACBF).

The paper is divided into seven parts of which this is the first. Section 2 discusses the global recession and the socio-economic pressures it is exerting on industrialised countries – especially the US, Europe and Japan. It is noted that these countries have been under severe financial instability, widening sovereign-debt problems and high unemployment. Because of the huge sums paid to bail out the failing financial sector in these countries, the pursuit of credible medium-term fiscal consolidation has remained paramount. It is argued that, to get the global economy on a path of sustained recovery, the industrialised countries must take measures that restore aggregate demand as well as institute structural changes for sustained growth. Section 3 examines the implications of the recessions for developing countries. It is argued that the uncertainty emanating from Europe and as yet unknown policy reactions to the recent volatility in the financial markets, makes projecting short-term growth particularly difficult. Any development in developing countries to become major growth pole does not mean that their prospects are divorced from those in high-income countries. Slower growth in high-income countries will imply slower growth than might have otherwise been expected in developing countries in the short-term. Section 4 takes stock of the current status of the world economy and Africa's position in it. The repositioning of Africa should be read in light of the fact that there is need for the EU and other developed countries renewal and repositioning in the world economy. Africa also needs to strike new strategic alliances with countries such as Brazil, Russia, India and China (BRICs). The implications for Africa of the current global restructuring process are examined in section 5. Africa can and should develop frameworks to ensure it does not get trap by negative effects of its alliance with the merging powers. Section 6 draws lessons from the various arguments made in the paper to enhance the work of ACBF. Section 7 concludes the paper.

## II. GLOBAL RECESSION AND SOCIO-ECONOMIC PRESSURES IN THE US, EUROPE AND JAPAN

The global recession of the last couple of years has been driven by severe financial instability, widening sovereign-debt problems and high unemployment in industrial countries (El-Erain and Spence, 2010). As Rato (2005) argues: “Global imbalances are, by their very definition, a problem of the global economy”. To resolve and restore global 'balance' requires a collaborative and coordinated international effort to address the underlying causes – especially financial sector and macro-economic fragility. In recent times, the policy measures needed to address the imbalances are generally agreed upon – either by allowing markets to work through more deregulation or addressing market failures through greater regulation of the world economy<sup>3</sup>; what is still lacking or disputed, is the firm implementation of policies measures. So what are these measures?

Because of the huge sums paid to bail out the failing financial sector in the United States (US), the pursuit of credible medium-term fiscal consolidation has remained paramount. The continued financing of the large US current account deficit depends on the future attitude of foreign investors towards American assets. To this end, restoring and maintaining investor confidence in the dollar—and in the strength of the US economy—is key to prevent destabilizing dollar depreciation. A strong commitment to reducing and keeping sustainable U.S. fiscal deficits would go a long way towards achieving that. However, firm implementation of this proposal is critical. The dilemma is how large should that deficit reduction be, especially in view of the current cyclical strength of the US economy, and the need to balance that with importance of lowering government debt ahead of the retirement of the baby boom generation and potential pension crisis.

One could argue that, to get the global economy on a path of sustained recovery, countries such as the US must take measures that restore aggregate demand as well as institute structural changes for sustained growth. In that light, the current EU-wide attempt to reduce the deficit is not sufficient to bail out the economy as the credit market remains tight. Local authorities as a consequence are feverously cutting on essential public services and social commitments.

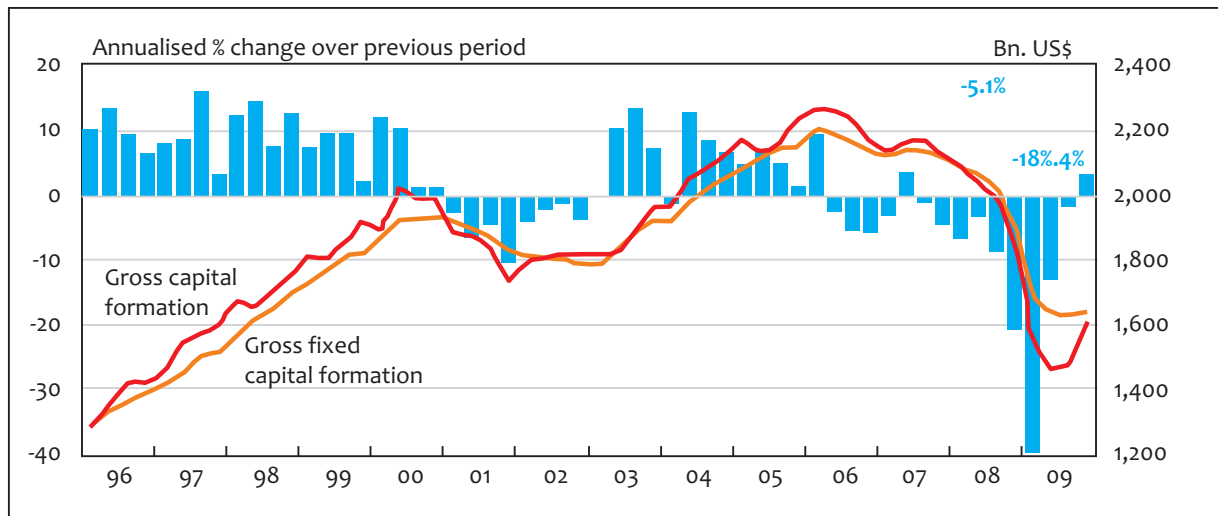
As for the US, exports have fallen as a result of the crisis. There must be growth to allow for cuts in the deficit in the future. Energy security and market diversification are equally important for the US. The role, position, and level of global integration of the US economy grew significantly over the last 20 years and hence its knock-on impact on other countries is more acute in the moment of fragility. The main origin of the crisis was the financial sector in the US, and because of the size of the US economy and the importance of the financial sector in the US economy, the global impact was accentuated. There is need to reform this 'arrangement'. In essence, the financial sector should service the economy and not the economy service the financial sector. Because the recession was primarily an outcome of the imbalance between demand and supply of funds for investments, the imbalance has remained a major negative driver on US recovery. As can be seen from figure 1 below, gross fixed capital formation fell by around 18 percent; and gross capital formation even fell by close to 24 percent.

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<sup>3</sup>These two polar positions depend on ones 'ideological' outlook of the economy and whether there is big leap of faith in the market mechanism as a driver of economic efficiency.



Figure 1: Investment trend in US



Source: Bureau of Economic Analysis (database)

Indeed, stronger growth in Europe and Japan is a critical prerequisite for unwinding the existing imbalances in the world economy. That is because a major contributory factor to the widening global disparities has been the unbalanced pattern of global growth. Specifically, world economic expansion remains largely driven by Brazil, India and China<sup>3</sup>. In the Euro zone and Japan — with nearly one-quarter of global output— economic performance has been relatively weak, although recent indicators point to positive signs in Japan. There were modest annualised growth rates of 2.7 and 1.3 percent in the second and third quarters of 2009, respectively. The most important drivers for the mild recovery were foreign trade and private consumption. The growth contribution of net exports to GDP growth reportedly mounted to 6.1 percentage points in the second quarter and to 3.0 percentage points in the third quarter. Private consumption increased by an annualised 4.8 and 3.8 percentage points respectively in the second and third quarter. However, investments continued to fall at double-digit rates throughout the year of 2009 (EEAG, 2010).

The EU economy has remained largely depressed for the period of 2008 and 2009/10. Low growth prospects and rocketing debt in many of the EU's 27 nations in 2010 have alarmed financial markets, causing stocks to slide and the euro to fall sharply in value to a four-year low against the U.S. dollar. The EU forecasts for 2010 showed that growth would not top 1.5 percent and the jobless rate would stay close to current highs without reforms over the next five years (World Bank, 2010a). Compared to their share of pre-crisis GDP (i.e. in 2007), the primary deficit in both the Euro zone and the European Union increased by 4.4 percentage points in 2009, increasing from, respectively, 1.3 and 1.5 percentage points in 2008 (see Table 1. below). The differences across countries and the two crisis years are substantial. Whereas the governments in Spain and Ireland already stimulated their economies in 2008, those in Finland and the United Kingdom became more active in 2009. In Italy and Germany, government actions were – relative to the rest of Europe – more conservative. Indeed, a number of countries have rushed to cut their deficits (EEAG, 2010). Italy is, shaving-off an estimated euro24 billion from state spending in an effort to reduce its debt – currently the largest in the EU. Other Euro zone countries – such as Spain, Portugal and Ireland – are sharply curbing budget spending to try and get mounting debt under control amid loss of market confidence in the euro and

<sup>3</sup> Russian performance has remained relatively weak except in the supply for oil and gas.

the ability of Euro zone states to pay their bills. Britain, which does not use the euro, also announced about 6 billion pounds (\$8.7 billion) in budget cuts.

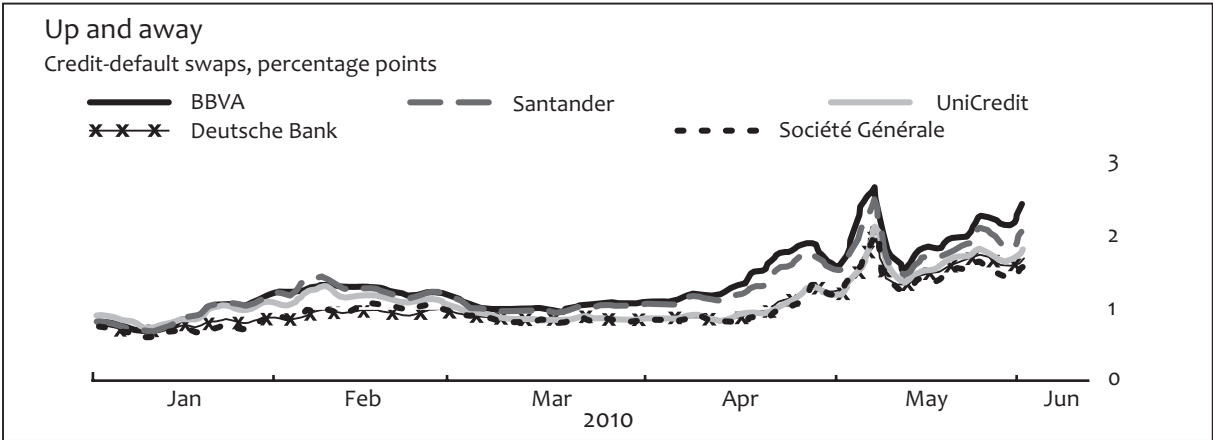
Table 1: Trends in EU deficits 2001-2009

	Gross debt <sup>a)</sup>				Fiscal balance <sup>a)</sup>			
	2001-2006	2007	2008	2009	2001-2006	2007	2008	2009
Germany	64.0	65.0	65.9	73.1	-3.2	0.2	0.0	-3.4
France	62.3	63.8	67.4	76.1	-2.9	-2.7	-3.4	-8.3
Italy	105.8	103.5	105.8	114.6	-3.4	-1.5	-2.7	-5.3
Spain	47.6	36.1	39.7	54.3	0.2	1.9	-4.1	-11.2
Netherlands	50.8	45.5	58.2	59.8	-1.2	0.2	0.7	-4.7
Belgium	97.0	84.2	89.8	97.2	-0.4	-0.2	-0.2	-5.9
Austria	65.0	59.5	62.6	69.1	-1.6	-0.6	-0.4	-4.3
Greece	99.6	95.6	99.2	112.6	-5.1	-3.7	-7.7	-12.7
Ireland	30.1	25.1	44.1	65.8	1.2	0.3	-7.2	-12.5
Finland	42.2	35.2	34.1	41.3	3.5	5.2	4.5	-2.8
Portugal	58.7	63.6	66.3	77.4	-3.9	-2.6	-2.7	8.0
Slovakia	40.1	29.3	27.7	35.1	-2.4	0.0	-1.8	-6.3
Slovenia	27.3	23.3	22.5	35.1	-2.4	0.0	-1.8	-6.3
Luxembourg	6.4	6.6	13.5	15.0	1.5	3.7	2.5	-2.2
Cyprus	66.4	58.3	48.4	53.2	-3.5	3.4	0.9	-3.5
Malta	66.3	62.0	63.8	68.5	-5.3	-2.2	-4.7	-4.5
Euro Area	68.9	66.0	69.3	78.2	-2.4	-0.6	-2.0	-
United Kingdom	40.0	44.2	52.0	68.6	-2.4	-2.7	-5.0	-12.1
Sweden	51.2	40.5	38.0	42.1	0.9	3.8	2.5	-2.1
Denmark	42.2	26.8	33.5	33.7	2.4	4.5	3.4	-2.0
Poland	44.6	45.0	47.2	51.7	-5.0	-1.9	-3.6	-6.4
Czech Republic	28.9	29.0	30.0	36.5	-4.7	-0.7	-2.1	-6.6
Hungary	58.8	65.9	72.9	79.1	-7.3	-5.0	-3.8	-4.1
Romania	19.8	12.6	13.6	21.8	-1.9	-2.5	-5.5	-7.8
Lithuania	20.4	16.9	15.6	29.9	-1.5	-1.0	-3.2	-9.8
Bulgaria	42.8	18.2	14.1	15.1	1.0	0.1	1.8	-0.8
Latvia	13.4	9.0	19.5	33.2	-1.3	-0.3	-4.1	-9.0
Estonia	5.0	3.8	4.6	7.4	1.2	2.6	-2.7	-3.0
EU27	61.5	58.7	61.5	73.0	-2.3	-0.8	-2.3	6.9

<sup>a)</sup> As a percentage of gross domestic product; definitions according to the Maastricht Treaty.

Source: EEAG (2010).

Figure 2: Trends in credit default swaps (CDS) for selected EU banks (January-June 2010)



Source: Markit (based on database for 2010).

So far the financial system has been strained, but it has not broken down completely. This partly reflects the underwriting support that the European Central Bank and other central banks have been offering. The ECB has provided at least €800 billion in loans to banks, much of it in exchange for slightly soiled government bonds and other dubious assets.

### III. WHAT ARE THE IMPLICATIONS OF THE GLOBAL RECESSION FOR DEVELOPING COUNTRIES?

The uncertainty emanating from Europe and as yet unknown policy reactions to the recent volatility in the financial markets, makes projecting short-term growth particularly difficult<sup>4</sup>. The rapid rise in the price of CDSs for highly indebted high-income countries, and the potential for reduced market access for these countries, has prompted both them and other governments to speed up fiscal consolidation programs. Table 2 presents a picture that is consistent with: a more constrained lending environment, more cautious investment and consumer behavior, and with governments assumed to speed up fiscal consolidation efforts by half the amount required to bring debt to GDP ratios to 60 percent of GDP by 2030 (see IMF, 2010a).

Table 2: A slower growth baseline (percentage change from previous year)

	2008	2009e	2010f	2011f	2012f
<b>World</b>	<b>1.7</b>	<b>-2.1</b>	<b>3.1</b>	<b>2.9</b>	<b>3.2</b>
<b>High Income</b>	<b>0.4</b>	<b>-3.3</b>	<b>2.1</b>	<b>1.9</b>	<b>2.2</b>
OECD Countries	0.3	-3.4	2.0	1.9	2.1
Euro Area	0.4	-4.1	0.5	0.9	1.5
Japan	1.2	-5.2	2.2	1.4	1.5
United States	0.4	-2.4	3.0	2.3	2.5
Non OECD Countries	3.0	-1.7	4.1	4.1	4.4
<b>Developing Countries</b>	<b>5.7</b>	<b>-1.7</b>	<b>6.1</b>	<b>5.7</b>	<b>5.8</b>
East Asia and Pacific	8.5	7.1	8.6	7.5	7.4
Europe and Central Asia	4.2	-5.3	4.0	4.1	4.3
Latin America and Caribbean	4.1	-2.3	4.4	3.9	4.0
Middle East and N. Africa	4.2	3.2	4.0	4.2	4.4
South Asia	4.9	7.1	7.3	7.8	7.5
Sub-Saharan Africa	5.0	1.6	4.4	4.9	5.2

Source: World Bank (2010a)

e = estimate; f = forecast

1. Aggregate growth rates calculated using constant 2005 dollars GDP weights.
2. Calculated using 2005 PPP weight.

In this scenario, global growth is expected to be slower due to a weaker expansion in high-income countries, where GDP is projected to grow by 2.1, 1.9 and 2.2 percent in 2010 through to 2012. The more constrained environment also affects growth in developing countries, but to a lesser extent –partly because only a few countries are assumed to implement sharper fiscal consolidation. The weaker growth is also expected to slow the pace of the expansion in global trade, and results in a

<sup>4</sup>Developing country growth is projected to pick up from an estimated 1.7 percent in 2009 to around 6 percent in each of 2010, 2011 and 2012. The apparent steadiness of growth in each of these years belies an anticipated slowing of growth in China, the largest developing economy (from 9.5 in 2010 to 8.5 percent in 2011), as the fiscal stimulus put in place in 2009 begins to be unwound. Excluding China and India, developing country GDP is projected to increase by 4.5, 4.4, and 4.6 percent in 2010, 2011, and 2012 respectively (World Bank, 2010a).

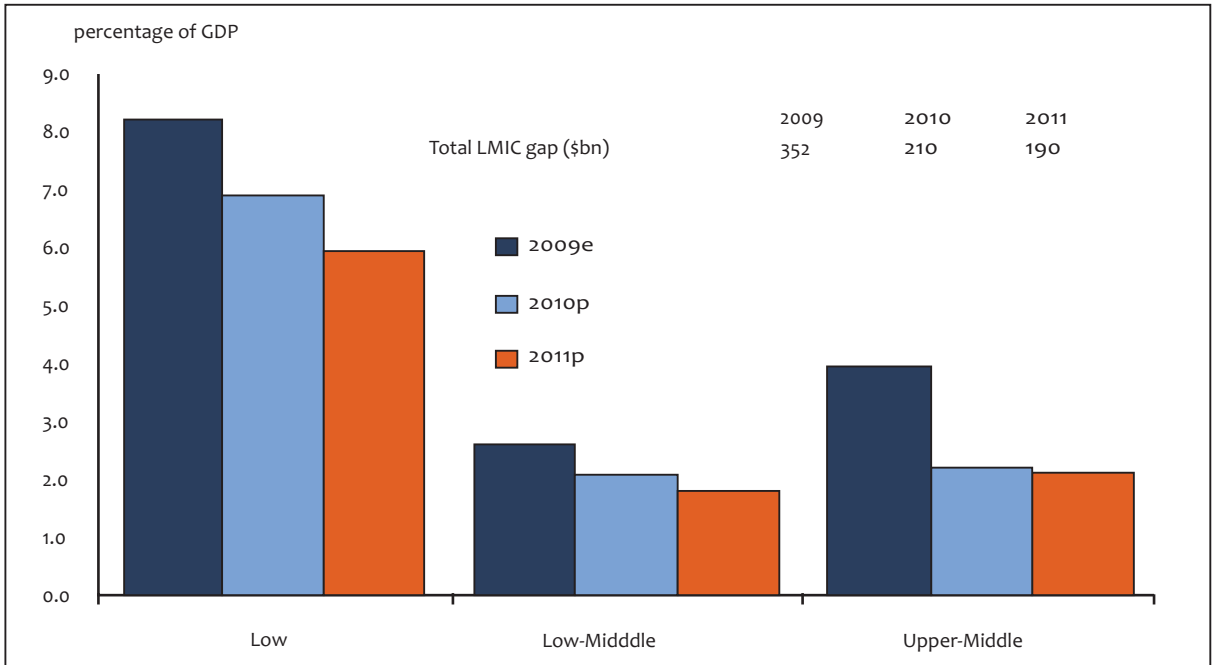
somewhat lower price for commodities and lower inflation. Because the slowdown is concentrated in high-income countries, the share of developing countries contribution to global growth is forecast to rise from 47 to 50 percent over the same period (World Bank, 2010a).

The expected confirmation of developing countries as a major growth pole does not mean that their prospects are divorced from those in high-income countries. To the contrary, slower growth in high-income countries will imply slower growth than might have otherwise been expected in developing countries in the short-term. Failure to deal with high income indebtedness could deprive developing countries of markets for their goods. Increasing developing-country borrowing costs and sharper competition for global savings as well as resultant cut in developing-country investment and growth.

Indeed high external financing needs in a time of sharp retrenchment in capital flows has led to significant current account adjustments and slower growth in several developing countries during 2009. As a consequence, financing needs are forecast to decline from \$1.2 to \$1.1 trillion in 2010 (op cit.). Based on the assumption that current account deficits remain at their 2009 levels (as a percent of GDP), the total external financing needs of developing countries is projected to be in the range of \$1.1trillion for 2010 through to 2012.

Private capital flows to developing countries are forecast to recover modestly from \$454 billion (2.7 percent of GDP) in 2009 to \$771 billion (3.2 percent of GDP) by 2012 (see above). As a result, the ex-ante estimates of the financing gap will halve to \$180 billion by 2012 from \$352 billion in 2009. As a share of GDP, the decline in the financing gap is expected to be most marked for the upper-middle-income countries 1.5 percent and low income countries 1.3 percent (Figure 3). The financial markets annex provides more detail on recent developments.

Figure 3: External financing gaps 2009-2011



Source: World Bank DEC Prospects Group staff estimates (2010a)

Sub-Saharan Africa weathered the global crisis better than was initially thought (IMF, 2010b; UNECA, 2010). In part this is because the hardest hit global markets (consumer durables and investment goods) are relatively small sectors in the region. At the same time, the region's limited financial integration into the global economy diminished the size of the initial shock. GDP growth for the region—is expected to continue to strengthen slowly, driven by higher commodity prices and stronger external demand. Overall the region is forecast to grow by 4.5, 5.1 and 5.4 percent respectively over 2010 – 2012, up from an estimated 1.6 percent gain in 2009 (see table 3 below).

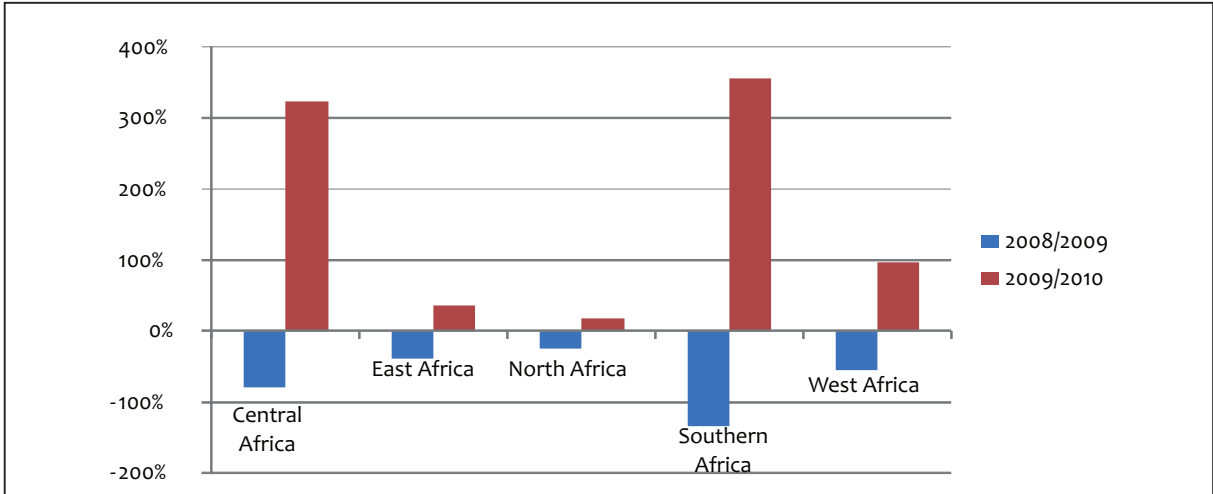
Table 3: Real GDP growth (%)

	2005	2006	2007	2008	2009 (estimated)	2010 (projections)
Africa	5.9	5.9	6.0	4.9	1.3	4.3
Central Africa	5.0	2.6	5.6	4.5	0.9	3.8
East Africa	7.4	6.8	7.5	6.4	3.9	5.3
North Africa	6.0	5.9	5.3	4.7	3.5	4.1
Southern Africa	6.0	6.6	6.7	4.6	-1.6	4.1
West Africa	5.1	5.3	5.9	5.3	2.4	4.7
Oil-exporting countries	6.8	6.0	6.9	5.6	2.5	4.9
Oil-importing countries	4.9	5.9	5.1	4.2	0.5	3.6

Source: UNECA (2010), Economic Report on Africa. Addis Ababa: UNECA.

The interesting feature of the Sub-Saharan Africa growth patterns during and after the global crisis, in addition to the milder than expected impact, is the differentiated pattern of growth across regions. The hardest hit region is Southern Africa with a decline of 135% between 2008 and 2009, followed by Central Africa with a decline of 80%. North Africa had the mildest decline between 2008 and 2009 of 26%; while Eastern Africa posted a decline of 39% and West Africa of 55%. The post recovery patterns are equally differentiated with the fastest recovery in Southern Africa at 356% projected change between 2009 and 2010, followed by Central Africa at 322%. North Africa has the mildest post crisis trajectory with a projected 17% change in real GDP growth between 2009 and 2010; while East Africa is projected to have a 36% change and West Africa a 96% change (see figure below).

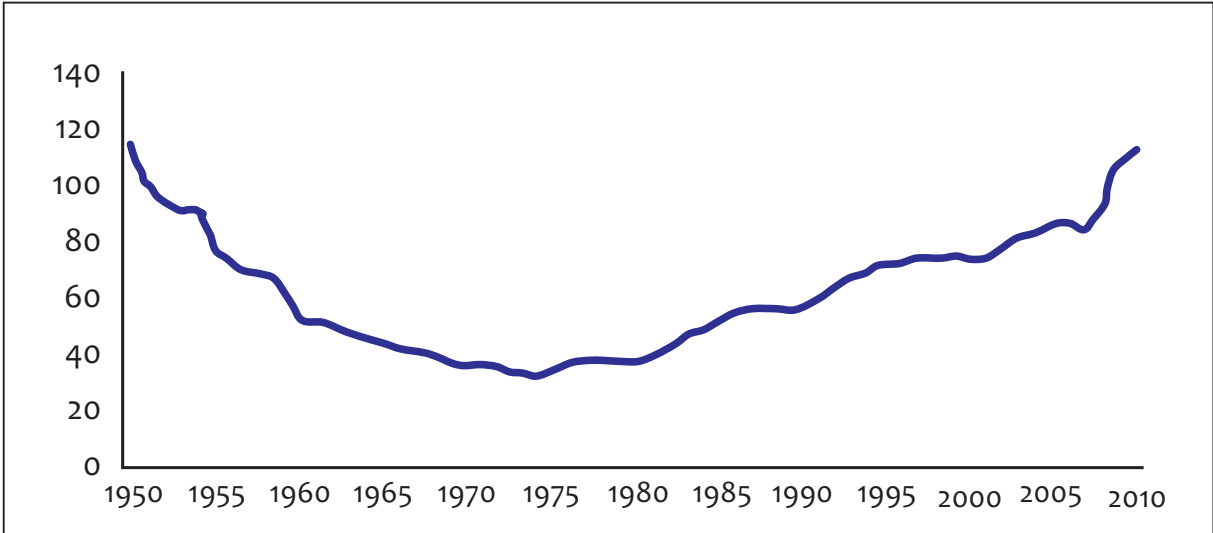
Figure 4: Pre and Post Crisis Economic Growth Recovery in Africa 2008-2010



Source: Calculated using data from UNECA, 2010.

The need to tighten fiscal policy extends well beyond OECD countries with the immediate challenge of removing the crisis-related stimulus measures that were put into place. This is a problem for many high-income countries, where fiscal deficits and debt to GDP ratios have reached unsustainable levels. The G-7's debt is expected to reach more than 113 percent of the group's GDP in 2010 (Figure 5 below), a level not seen since 1950. Bringing debt levels down will be more challenging now than earlier because, in contrast with the war-related debt of the 1950s, today's debt reflects ongoing demands on government coffers that are likely to grow as pension and health liabilities expand with aging populations. The IMF (2010a) estimated that high-income countries will need to cut government spending (or raise revenues) by 8.8 percent of GDP for a 20 year period in order to bring debt levels down to 60 percent of GDP by 2030.

Figure 5: G-7 debt is close to post-war highs (Gross public debt as a % of GDP)



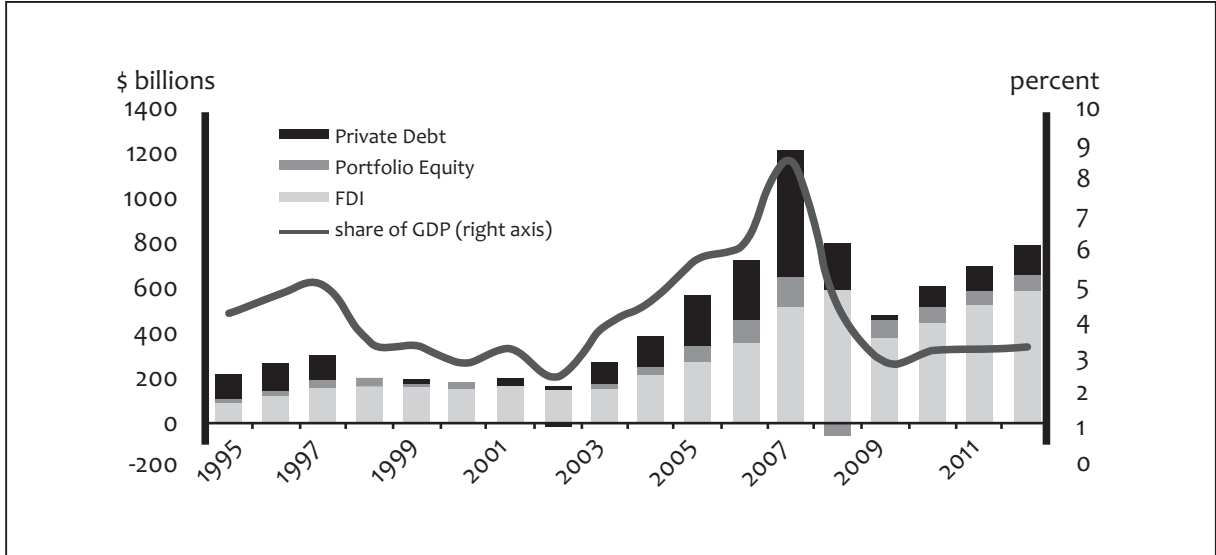
Source: IMF (2010a)

The need to remove stimulus measures among developing countries is generally less pressing. However, some developing countries do face fiscal challenges, including India whose fiscal deficit is estimated to have reached 9.5 percent of GDP in 2009/10, and whose debt represents 77 percent of its GDP. Recognizing the challenge, the government has announced a medium-term adjustment path, which is expected to reduce India's debt-to-GDP ratio to at most 68 percent of GDP by FY2014/15. China also put in place a large stimulus package, but its finances are on a firmer footing, so there is less urgency to removing the stimulus (although overheating could be a strong macroeconomic argument for doing so).

Developing countries, particularly those that rely on official development assistance (ODA) for budgetary support, have come under severe pressure due to reduced aid flows. So far, the crisis has caused government deficits in low-income countries to increase by an average of 1.3 percent of GDP, suggesting that many were able to take advantage of relatively good fiscal positions, and ample reserves going into the crisis to buffer its effects on spending. However, the initial cushions have been exhausted, and the ability of low-income countries to maintain spending in the face of a slow recovery is unclear especially if, as is likely, ODA declines in coming years (World Bank, 2010a). Dang et al. (2009) suggests that ODA could fall by as much as 20 to 25 percent in the current crisis, and with about a decade for flows to recover.

In addition to potentially weaker aid flows, ongoing restructuring in the international financial sector implies significantly less and more expensive financial capital for developing countries for years to come. Private capital flows to developing countries are projected to recover only modestly from \$454 billion (2.7 percent of GDP) in 2009 to \$771 billion (3.2 percent of GDP) by 2012 (Figure 6 below). If the rebound in net capital flows remains muted as expected, there is a real risk that many of the private firms that borrowed heavily internationally in the boom period will not be able to rollover their loans, potentially generating a second-round region-specific crisis. For example, in Kazakhstan, Latvia, Lithuania and Ukraine the repayment on corporate external debt is anticipated to exceed 8 percent of GDP in 2010.

Figure 6: Net private capital inflows will stage a modest recovery



Source: World Bank (2010a)

Increased borrowing of high-income sovereigns on international capital markets will increase demands on global savings, raise borrowing costs and potentially crowd-out developing country borrowers. Already in 2009, the G-3 reportedly issued 5-times more bonds than they did in each of 2005 and 2006. The group's total draw on global saving exceeded \$2.5 trillion more than 7-times the net capital flows to developing countries in that year. Partly as a consequence of this increased borrowing and also because the Federal Reserve has stopped purchasing U.S. long-term corporate bonds and residential mortgages, long-term yields on U.S. treasury securities had been rising, though with the onset of the Greek crisis they have eased in response to “safe-haven” inflows (World Bank, 2010a).

Given the recent experiences of the EU and the US, one could ask in the context of developed countries: a) whether the traditional role of the central bank will continue, and b) what are the possible new roles? Recent history seems to suggest that central bank interventions in the developed economy are generalized especially in attempts to bail out failing financial institutions. Clearly, the traditional role of the central bank needs to be complimented with new and enhanced tools (Blinder, 2010). For example, the European Union (EU) plan includes enhancing financial sector regulatory mechanism and supervisions a Euro 750 million has been set up as a stabilisation fund. In

that sense, policy makers should distinguish financial and macro-prudential supervisions<sup>5</sup>. Macro-prudential surveillance/supervision is a system-wide health check of the financial system to ensure that individual banks are protected from any outbreak of system-wide failures or domino effects of fragility. Macro-prudential supervision takes account of those risks that may affect all, part, or most banks in the system - and not just individual banks. It could be argued that such macro-prudential surveillance would have prevented the emergence of the sub-prime market and the subsequent financial fragility in the developed economies such as the US and EU.

The key to raising growth in the US, EU and Japan essentially remains to be structural reform. Important progress has been made in recent years, including in pension, healthcare, and labour market reforms. The precise future requirements would of course differ across countries, but they should in general focus on further boosting labour utilization, product and service market deregulation, and greater financial market integration. Labour market reform, in particular, will take on added significance with developed countries' rapidly aging population. To sustain their basic social models for the benefit of future generations, Europe, the US and Japan need to create more jobs and maximize labor utilization.

Some of the reforms being debated in the EU, US and Japan include the followings:

**R&D and technology policies** - There is great need to invest in research to allow policy makers to get better understanding of how markets generally, and financial markets in particular work. Strategically, this finance research would allow policy makers appreciate analysis on risk management and scientific innovations. Science training should prioritise the competitive need of the company or society at large. For example, there is need for a common EU technology strategy to remove the current incoherent approach to R&D and the undertaking of innovations.

**Strengthening governance framework** - to allow for greater accountability for and consensus on any policy adopted to reverse the declining fortune of EU and rest of the world economy. There have been numerous calls to institute deregulation of EU economies to avoid autarky and pursue wage freeze in the public sector in certain countries such as Greece, Italy and France to enhance convergence in the Euro zone. EU countries also have to make other significant institutional changes especially those that enhance not only workers rights but also labour movements.

**Consumer protection** - To many commentators, the current recession has “its origins in an asset price bubble that interacted with new kinds of financial innovations that masked risk; with companies that failed to follow their own risk management procedures; and with regulators and supervisors that failed to restrain excessive risk taking” leaving mortgage borrowers misled and over-exposed (Baily et al., 2008). There should be greater consumer protection to allow for less 'moral hazards' from the financial sector with reconciliation of available finance and borrowers' real needs and ability to pay.

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<sup>5</sup>According to Ryback (2006), macro-prudential management has at least the following four features:

- First, its aims to limit the distress to entire financial systems rather than distress to individual institutions.
- Second, its chief aim is to avoid large and burdensome costs to the economy such as expensive bank bailouts rather than aiming to protect more narrowly the depositors of an individual bank.
- Third, it is based largely on the assumption that at least some of the risks faced by the banking system collectively differ from those faced by individual banks. In other words, the risk to the system is not simply the sum of risks to individual banks.
- And, fourth, it aims to examine risks that arise from the interaction of banks as part of a financial system rather than on a bank-by-bank basis.



Build a framework that will enhance long-term savings to allow for greater future liquidity. The OECD needs to undertake structural reforms of their financial markets to avoid fragility and instability. With respect to the issue of macro-prudential considerations, should focus debates on issues such as: the nature of legislative reform of the banking system, the need to impose taxes on the banking systems, and strike a balance between the needs for liquidity requirements and effective operations of the financial sector.

**Support to SMEs** - The nature of business ownership has a big influence on the speed of expansion. The majority of companies under sole-ownership seemed to have invested and expanded despite the downturn. Indeed, all companies must recognize the importance of marketing/market outreach and product/brand penetration. Providing greater support to SMEs as part of the recovery strategy is crucial as these firms are key in employment creation and generating dynamism in the world and EU economy.

**Financial sector supervision** - The EU needs an effective mechanism for the monitoring and evaluation of operations in the financial sector as well as the compliance of member states with various protocols designed to bring greater convergence; as well as socio-economic and political stability in the Euro zone.

**Demographics and labour market policies** - The population of the OECD has continued to age, thus putting pressure on the fiscus to pay for pensions. The financial crisis has significantly impacted pension systems in these countries forcing governments to make policy changes in response to the increased pension deficits they are facing. The crisis exacerbated the existing financial imbalance in the public pension systems by reducing contribution revenues sharply while at the same time leaving expenditures constant or even higher. The crisis also resulted in a sharp drop in financial asset values which affects pensions provided by funded pillars (Schwarz et al., 2009). There is therefore, need to develop a comprehensive population and labour market policies to deal with the demographic dynamics of the EU and wider OECD. For example, the retirement age could be extended to beyond the age of 65 years.

**Integration and partnerships** - The EU needs to have a united voice in articulating the desire for change in the current financial architecture. In this context, some EU speakers urged for greater multilateralism and common EU purpose when engaged in negotiations of reforms of global governance. Although politicians tend to put their electoral fortunes first, the chances are that without reforms and better government-to-government coordination of policy instruments in the Euro zone, the outlook is one of sluggish growth in the developed countries and strong growth in the BRICs and less developed countries. There is need to gear-up political will to steer the necessary socio-economic governance for recovery.

**Investment policy** - Given the diversity in the strengths of the various EU economies, the Euro zone countries should work out modalities for equitable investments and resource availability especially to ensure resources are allocated more efficiently than been the case. EU as well as the rest of the OECD need to recognize that energy storage solution is going to emerge as the 'industrial' problem of future and therefore invest now in energy security.

**Strengthening macroeconomic management** - There seems to be too much anxiety about the levels of debts in OECD member countries yet there is sufficient historical evidence that high debt-GDP need not lead to country-default as was the case of the UK during the war (260% Debt/GDP ratio).

Indeed, too much risk-awareness may lead to deflation. Some the EU countries are now suffering from 'balance-sheet' recession whereby attempts by market players to cut risks at the same time have generated more volatility. Balance sheet recessions occur because the risks banks face are instead in the balance sheets of their major borrowers, who would have borrowed heavily in foreign currencies even though they have domestic currency cash-flows. Macro-prudential management cannot stop at the traditional boundary of the banking system, but must look at the risks in the non-bank financial sector and at the structure of household and corporate balance sheets. This has not been adequately done in the current EU context. However, central banks authorities have become increasingly aware that monetary stability and financial stability are closely linked. Central bankers now recognise financial stability matter for the achievement of monetary policy goals. For example, as the bond market has become increasingly important as a transmission mechanism for monetary policy; market conditions, the soundness of intermediaries, and the transparency and integrity of pricing have all become relevant issues for the central bank to consider; and

**Industrial and competition policy** - Mergers and acquisitions should not be seen in a negative light as antitrust behaviour but as a mechanism for knowledge transfer and organizational rejuvenation. There is need to improve the way EU companies do business and remain competitive in the face of a down-turn - especially by engendering innovations in technology. There is a strong argument for enhancing patents protection to create more space for business-start-ups and commercialization of inventions. Greater urgency needs to put on enhancing protection of intellectual property rights. Sometimes, what is required is not new technology to enhance efficiency but new applications of existing technology. For example, one could better integrate existing hardware and software as well as enhance technology sharing. Innovation need not come from a laboratory but change in work processes and change management. Both these approaches will make technology cheap and accessible; and for technology to be treated as a service.

A number of lessons could be drawn from the EU and US experiences as to the role of Central Bank in an environment of financial and socio-economic fragility:

- Every central bank needs efficient markets to be able to deliver its traditional roles. Indeed functioning markets are essential to an effective monetary policy.
- However, these roles should include not just the control of inflation but also a multiplicity of variables that allow for macroeconomic stability and growth. Such a role could be socio-political to allow greater integration and unity in the Euro zone. This is the role being played by Federal Reserve in the case of the US.
- Central banks also need greater policy credibility and independence for economies to avoid uncertainty and jittery reactions in financial markets.
- In the context of the EU, the Maastricht Treaty explicitly outlines the traditional and new roles that central banks in the Euro zone should take upon themselves including the fixing of interest rates.
- Central bank intervention is important but should not be intrusive i.e. it should be designed to enhance growth. Interventions/regulation can be based on quantitative and qualitative mechanisms.

- As to current challenges in the EU, price stability is not at stake. However, a number of countries are seeking to restore their fiscal balances and sanity in public finances.
- The priority should however be shifted to deal with the need for countries to share and ensure liquidity and financial stability across the board.
- Weak capacities of central banks and countries to monitor and regulate the financial system may have had direct effects on the development of bubbles in the developed world;
- Some Tobin's tax be levied on bank profits and global flows of finance as has been done in UK during the 2010 budget to control negative capital flows; and
- Can central banks ensure proper functioning of the modern system? The answer may require greater partnerships by all sectors of society including the private sector and government.

The emphasis given to macro-prudential surveillance implies the need to establish regulatory agencies separate from the central bank in order to provide a birds-eye view of the banking system (Nier, 2009). In which case, the statutory mandate to ensure financial sector soundness moves to these agencies and the central bank keeps its traditional concern for the overall soundness of the banking system. The Federal Reserve of US is noted to have succeeded in combining both these roles to ensure that oversight of the financial system did not fall between the gaps in the new institutional structure of surveillance and supervision.

#### **IV. THE WORLD ECONOMY, AFRICA AND THE BRICS : WHAT DOES THE FUTURE HOLD?**

This section attempts to take stock of the current status of the world economy and Africa's position in it. Over the years, sub-Saharan African relations with the Europe and the US have focused primarily on granting access to international markets on the assumption that the ability to trade and take advantage of these markets would follow. Strengthening sub-Saharan Africa's regional markets has not yet received the focus that other African development issues have, despite the power of these markets and regional systems to move goods, services, people and information. Aside from the Economic Partnership Agreements (EPAs), European and U.S. market access for sub-Saharan Africa has been governed mainly by preferential and unilateral market access programs. These programs have produced limited successes concentrated in a few countries and sectors. This is partly due to product carve-outs and complex rules of origin and is compounded by complicated product standards and trade-limiting policies in sensitive industries like agriculture that intersect with the preference programs (Kuhlmann, 2010. Also see Mackie et al., 2010).

Although existing programs do create important market access for the world's poorest countries, this access could be expanded, made longer-term, and simplified to ensure that preferential trade programs can be fully taken advantage of.

Several lessons could be drawn from this experience. First, it is now generally accepted that the best policies are those that are the least complicated and allow markets and other economic-relations to develop organically. Constructing markets through complicated political compromises, or forcing choices before markets have actually developed, limits opportunities rather than creating them. For example under African Growth and Opportunity Act (AGOA), apparel manufacturing has blossomed in some areas, but value-added investment along the supply chain has proven to be difficult to encourage without addressing the underlying conditions that have prevented integrated markets from developing. Under the EPAs, market choices have been required before markets have actually developed (Dowla, 2004). Despite the laudable goal of regional integration, the overlapping regional mandates of RECs have actually limited rather than promoted regional trade and may create narrow, entrenched African lobbies that will make future growth difficult (ACBF, 2007).

Second, policy predictability is essential in investment decisions and needs to be an underlying principle of all preference programs. Setting short expiration dates for preferences has created a disincentive for sustainable, long-term investment. For example, when AGOA was enacted in 2000, it came with an expiration date, both for the program and for its special apparel rule of origin (the third country fabric rule). Both AGOA and the third country fabrics rule have been extended over the years, but without complete certainty that the benefits would continue. This uncertainty has caused instability for both existing and potential investment, and politically it has led to a dynamic that is focused on preserving the status quo, with longer-term gains often pushed to the side (Kuhlmann, 2010; Mackie, et al., 2010).

Third, those sectors with the most economic opportunity need to be the centerpiece of preference programs. Under the various multi-lateral trade regimes, African agricultural products remain subject to the complicated system of quantitative restrictions that governs commodity trade in a number of products, including sugar, dairy, and peanuts, and subjects very poor countries to miniscule or non-existent quotas and very high out-of-quota tariffs that approach several hundred

percent. While the policy debate has often focused on developed country agricultural subsidies as the main barrier to developing country agricultural trade, these non-tariff barriers can actually be more of an impediment to trade than subsidies (Dowlah, 2004). The European experience has shown that competitive producers of these products can see immediate gains once open market access is granted. For example, as a direct result of Europe's announcement of its Everything But Arms program, which granted LDCs duty-free, quota-free access to the European market, Mozambique's sugar trade with Europe went from zero in the year 2000 to over 130,000 metric tons in 2008, with steady increases each year (Kuhlmann, 2010).

Fourth, trade preference programs need to be part of a holistic approach to trade policy with sub-Saharan Africa that effectively couples opportunity-based market access with targeted, systemic policies and assistance programs to address needs and remove barriers on the ground. Building functioning regional markets needs to be a primary goal of both preference programs and accompanying trade capacity building programs and other development assistance (Sako and Kararach, 2007).

The repositioning of Africa should be read in light of the fact that there is need for the EU and other developed countries renewal and repositioning in the world economy. This repositioning is occurring at the time when the world economy, is faced with not just financial insecurity but also terrorism. Arguably, surges in terrorism have been partly the result of EU/US isolation whereby Europe and the US were busy with themselves for the last two or so decades (Mamdani, 2004). In that light, developed countries should review and revise their foreign policies; and have a united approach to partnership with the rest of the world. However, because of the crisis some countries seem to have adopted 'autarkic' approaches as to how they should respond to the current recession<sup>6</sup>.

A number of emerging powers have accelerated their engagement with Africa. The global financial crisis in 2008 provided additional impetus for this trend, especially for China, which notwithstanding the global slowdown, has continued to scale up its engagement on the continent. This has consolidated its position as a partner among African states.

Asia's phenomenal growth in the last two decades and more recently Brazil's has also brought new opportunities for African states. Africa's traditional partners in Europe and the US have sometimes viewed this as a threat to their own influence, and insinuate that these new partners may contribute to a regression of democratic freedoms and good governance on the continent<sup>7</sup>. It may be true that some new actors play by rules different from those of Africa's traditional European and US partners. These rules of 'engagement' are not static. Equally, Africa is neither a single entity nor has been monolithic in its approach to international relations (Cargill, 2010).

But who are these new actors and partners? They fall into three broad categories the first two are: the large (re)emerging powers, led by China India, Brazil and Russia; and smaller countries, such as Malaysia, South Korea and Venezuela. Their interests vary from purely commercial to political and do not always exclude the developmental and altruistic. They may compete with traditional powers for commercial advantage and political influence, but they may also collaborate in peace and security or development (Sidiropoulos, 2010).

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<sup>6</sup> Rogoff (2010-01-05) has argued that in the current crisis, countries need more trade than less.

<sup>7</sup> Chinese attitude to the conflict in Darfur is usually cited as an example.

However, the third group is internal to Africa itself. These are African regional powers, such as Libya, Nigeria, South Africa and Angola. They too are driven by various interests, operate under diverse codes of conduct, and have varying drivers and impacts on African economic development and peace and security (op. cit).

The proliferation of new actors with an interest in Africa has broadened the choices available to the continent in the selection of partners and development strategy. As multi-polarity deepens a development which the financial crisis helped to accelerate the Europeans and the US will find themselves increasingly competing with these new actors for space in areas that have been traditionally their field of operations, as well as in regions where EU and US interests have been reignited by new actors' activities. How the EU and US respond will be crucial to the way their partnership with the African continent is perceived.

As noted earlier, there are crucial areas in which the EU and US have been found to be lacking in sincerity, which makes exploring options with other partners appealing to African states, especially the manner in which negotiations of the EPAs as well as issues related to the multilateral Doha round have been conducted.

The global recession has created new challenges for African states. Attracting investment is becoming more difficult, remittances have fallen, export earnings are down, and supply capacity continues to hamper sustainable economic development. A new global economic architecture is urgently required with Africa as a prominent player.

The BRICs matter to Africa because of their economic weight (Economist Online, June 2010). These are the four largest economies outside the OECD (Organisation for Economic Co-operation and Development) - the only developing economies with annual GDPs of over \$1 trillion (Indonesia's is only half that). With the exception of Russia, they have sustained better growth than most during the current recession and, were it not for them, world output would arguably have fallen by even more than it did. Meanwhile, the BRICs are also increasing their trade with one another: for example, Chinese-Indian trade is expected to reach \$60 billion in 2010 (op. cit). China has also become the largest market for the fast-industrialising countries of East Asia. Unfortunately, China has become the largest producer of carbon dioxide, emitting 6.5 billion tonnes of CO<sub>2</sub> in 2008, or 22% of the world's total. Russia is third and India fourth on this particular roll of shame.

Since the crises in the 1990s, the BRICs have managed to strengthen their external balances and put in place healthy macroeconomic policy frameworks that have ensured more credible conditions (Goldman Sachs, 2009). This healthy structural backdrop has allowed these countries to ease financial conditions aggressively, without the risk of capital flight. Combined with the lack of major banking crises in most of the BRICs (with the notable exception of Russia), this has assisted the recovery process. Despite much criticism<sup>8</sup> of some countries running surpluses during a global recession, strong reserve accumulation appears to have been beneficial. The crisis reinforced the notion that reserves are a 'good thing' for these countries. While Russia saw big draw downs, the BRICs large 'war chests' allowed them to maintain policy independence partly due to the better perceived reserve cover. Indeed, some commentators perceived them as being a source from which world recovery will begin (El-Erain and Spence, 2010).

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<sup>8</sup>See Rodrik (2010) for some of these views.

Foreign assets have also provided cushions against the great recession and helped turn the BRICs into financial powers as well as economic ones. Currently most OECD countries are struggling to rein in record budget deficits and soaring debts, yet the BRICs' public-debt levels are mostly modest and stable (India is a partial exception). Most investment banks offer BRICs funds. Africa has the chance to tap into financial pool.

However, the BRICs sterling macro performance is being translated into different sorts of influence. Perhaps the most important is an intangible one: that of reputation. In some respects, the BRICs share a distinctive view of the world and have been lobbying of the global financial architecture. They have large domestic markets with substantial numbers of poor people, so growth and anti-poverty programmes are higher up their list of concerns than in OECD countries (this is even true in Russia, though to a lesser extent). As the Economist noted, they:

“are trying to diversify their economies. They are innovating... and challenging received notions about globalisation. All have become far more entwined with the world economy. But the BRICs have opened up without the full market liberalisation championed by the “Washington consensus”. In the aftermath of the great recession, this mongrel position commands respect in other developing countries, which want to know how the BRICs did it” (Economist Online, op. cit).

These countries have their own and diverse stories to tell and Africa needs to heed that. In that light, the orthodox attempt for example, to compare India and China as having followed similar reform processes is misleading. One needs to understand the following to appreciate India's rise a major economy in the world today: a) the country's population was turned of the last two decades or so into an asset. This approach is contrary to the orthodox Malthusian approach to demographic changes the rise in population has been accompanied with a rise in the quality of the population thus giving India a large reserve of skilled labour; b) both the saving and investment ratios have risen significantly thus releasing pressure on expansion in the Indian economy; c) inflation has not problem in recent times because expansion in purchasing power has been accompanied with tandem rise in the economy; d) public sector deficits have not been a problem as India has managed to reduce its debt-to-GDP ratio due to an expanding economy; and e) there has been significant infrastructural development - especially in energy, transport and ICT. All these combine to explain the unprecedented growth in the Indian economy over the last few decades.

The Indian economy still faces some challenges: a) there is need to maintain that consensus between the government and private sector which in recent times allowed for macroeconomic stability and sustained economic growth; b) financial reform is needed to allow for greater access to finance from all sections of society; c) there is also need to enhance the distribution of banks especially in the rural areas; d) significant levels of brain-drain especially of young Indians to the USA; and e) there is need to develop mechanisms that enhances project execution and financing.

So what should be the nature of the new partnership among Africa, the EU and other emerging countries such as the BRICs? There are a number of opportunities for partnership especially in areas such as ICT, energy, pharmacy and banking. With specific references to India; the country is a low-cost production hub, has significant levels of ICT decentralisation, secure business environmental condition and high levels of technology absorption. Both China and India also have: a huge market given the big population with rising wealth, an opportunity to access the best products from the rest of the rest of the World and hence an important export market for Africa; and for the entrepreneurs

and investors of Africa, opportunities for investments with high return rates. The African 'clients' would also benefit from: stable financial environment due to effective regulation of the Indian financial sector, good corporate and political governance, stable macroeconomic environment, sectoral diversification and ease-of-doing-business.

But Africa can also learn from China and India. Just like Africa; China and India traditionally suffered from brain drain especially to the US because of financial motivations among young Chinese and Indians as the US has a policy of fully financing the education and retaining these groups. The Chinese and Indian states have been working on a policy of reverse brain drain by creating conditions that attract and retain young graduates in those countries. Both China and India have also worked aggressively to develop mass-market technologies to enhance socio-economic standards and living conditions. There are arguably a number of risks that Africa needs to take into account in striking any partnership with the BRICs. Some of these risks that immediately come to mind are:

- Possible BRICs competition for African markets and natural resources – from our previous discussions, it emerged that there have been significant efforts by the BRICs - particularly, Brazil, India and China to penetrate the African market as well as to have access to its natural resources particular energy-related resources. There are also threats from dumping of cheaply produced, poor-quality and counterfeit goods. The competition can degenerate into a 'cold-war' type of influence whereby African countries were played against each other and dictators were groomed and protected by the cold-war powers.
- Possible divergences in strategic interests – there are also real possibilities that there will emerge divergences in interests between Africa and the BRICs. Indeed it should be noted that Indian and Chinese competition if unchecked can reproduce the old-style colonial trading arrangements Africa has gone through in the past. African industries may need some strategic policy framework to avoid them being suffocated and killed off by Indian, Chinese and Brazilian capital.
- Playing of Africa-BRICs partnership against “traditional” development partners – given that there are possibilities of divergences between the strategic interests of the BRICs and those of Africa, this fact can be used to divide and prevent Africa from continuing to work with its traditional partners - especially the former imperial powers. Africa should keep in mind that, for example, India and China fought a war once to further their divergent strategic interests and these can equally reoccur with serious consequences not just for Africa but also the rest of the world given that both countries are nuclear powers.
- Importing foreign rivalry – many of the BRICs have been rivals. For example, Indian-Pakistan rivalry and military skirmishes, as long as the Kashmir question remained unresolved, could be imported into Africa. Indeed Pakistan in recent times have become the foreground of the battle against global terror as most extremists groomed by Al Qaeda get trained and armed in remote corners of Pakistan and these could be easily exported to Africa. Africa therefore needs to selectively decide on its strategic interests and what alliances to build with not just India, but also Pakistan. The same could be said of Chinese and Russian rivalry.
- Killing off local industries – the BRICs are not just competing among themselves but against locally produced African products. Many products from the BRICs such as textiles, machine tools, electrical goods and chemicals are also produced by some African countries. For example, Stevens and Freemantle (2010) reported rising competition against South African goods from the BRICs. Cheap imports from the BRICs can potentially stifle Africa growth and industrial development.



Africa can and should develop frameworks to ensure it does not get trap by negative effects of its alliance with the merging powers. Among those arrangements are the needs to do the following:

- Strengthening intra-Africa trade and political alliances to reduce dependence on India, China or other economies and polities.
- Regulating BRICs especially Indian and Chinese capitals to ensure that impacts on the economic does not produce immiserising growth and development i.e. growth without poverty reduction.
- Ensure greater control of Africa's socio-economic and natural resources; and
- Developing clear principles and terms under which the BRICs and Africa will continue partnering and ensuring that these reflect the demands of the times.

As noted above, Africa has not been adversely affected by the recent recession as compared to the other parts of the world. Between 2000 and 2008, Africa's annual output grew by 4.9% (adjusted for purchasing-power parity), twice as fast as in the 1980s and 1990s and faster than the global average of 3.8%. Foreign direct investment increased from \$10 billion to \$88 billion more than India (\$42 billion) and, even more remarkably, catching up with China (\$108 billion) (Economist Online, 2010).

Questions have been asked whether the recent African growth is sustainable or is just another bubble. The pessimists have always had three strong arguments: a) that African politics is dysfunctional. Warring strongmen can undo the progress of decades in weeks; b) that the African economy is unduly dependent on the resource sector; and c) that Africa's growth does too little to benefit the poor. But over the past decade or so, all these objections seem to have weakened.

The so called-numerous examples of government failure can now be weighed against examples of sterling success. Because of improved capacity for macroeconomic management, the continent's inflation rate fell on average from 22% in the 1990s to 8% since 2000. For example, the World Bank's annual "Doing Business" report ranked Rwanda as the world's top reformer in 2010, based on the number and impact of steps to promote entrepreneurship there. Mauritius was ranked 17th of the 183 economies covered by the report, ahead of lots of richer countries (World Bank, 2010b).

Africa has depended on its abundant natural resources; and they will be a growing advantage as well as potential cause for conflict in years to come. The hectic pace of growth in the emerging world is not only pushing up commodity prices but also intensifying competition for access to the continent's oil and other minerals. Chinese and Brazilian companies in particular are wooing African governments with lavish expenditure on infrastructure in some instances at the expense of human rights.

Although the natural-resource sector accounts for only about a third of the continent's growth, Africa is producing a growing number of world-class companies outside the resource industry, from South African giants such as SABMiller, the world's second-largest brewer, and Aspen Pharmacare, the largest generic-drug maker in the southern hemisphere, to niche players such as Tunisia's Coficab, one of the world's most successful suppliers of wiring for cars (Leke et al., 2010).

With regard to the poor, Leke et al. (op. cit) point out that, due to rising living standards, some 200 million Africans are expected to enter the market for consumer goods (and may be lifted out of

poverty) in the next five years. Given the current demographic dynamics, the continent's working-age population will double from 500 million today to 1.1 billion in 2040. The Economist notes that consumer-goods companies “ranging from Western giants such as Procter & Gamble to emerging-market car companies such as China's Great Wall and India's Tata Motors are pouring into Africa. Foreign firms are likely to start using Africa as a base for manufacturing as well, as Europe's population shrinks and labour costs in India and China rise” (Economist Online, op. cit).

Africa has been seeing the benefits of what the Economist has called “frugal innovation” (Economist Online, op. cit) inventions that are designed to serve the poor (Mahajan, 2009). Indeed, private sector operations can be focused differently to help drive efforts towards the eradication of poverty in developing countries (Prahalad, 2009; Raworth, et al., 2008). Mobile-phone companies have arguably done more to improve the lives of poor Africans, and are continuing to innovate. For example, Kenya's Safaricom and its rivals are pioneering money-transfer by mobile phone through the M-pesa scheme; and with mobile savings and agricultural-insurance schemes planned as the next areas of innovations. Companies from other emerging markets are also expanding into Africa for example Bharti Airtel, with \$10.7 billion acquisition of Zain Africa, is a world-leader in improving services while reducing costs.

Nor is innovation confined to telecoms. Mahajan (2009) produces a long list of innovators ranging from the design to the distribution of products. For example, Nakumatt, a Kenyan grocery-retailer, is driving e-commerce by allowing people living abroad to buy vouchers for its stores electronically and then transfer them to their African friends and relatives, making remittance payments smoother. Other simple-but-effective innovations include the Jiko, a portable charcoal stove that can reduce fuel consumption by 30%; a foot-powered generator that can be used to charge cell phones and radios; and a \$20 washing machine made from discarded motors and iron. Africa is on the verge of a business revolution. The average gross national income (GNI) per capita across all 53 African nations in 2005 was about \$954, more than \$200 higher than India's. And 12 African nations (out of 53) have a GNI per capita that is greater than China's. Considering Africa's booming population, that concentration of wealth is a huge potential market for companies venturing to invest and trade with the continent (Economist Online, op. cit). From the various opinions and projections as to how the current recession will play out for Africa, three growth scenarios for Africa have been identified by Hanson et al. (2010):

1. **Autarkic/nationalistic** – the continent has a high degree of continental coherence with strong leadership on issues impacting the region. In this scenario, the polity owns the economic growth agenda, and Africans lead innovation. There is strong governance and important leadership and representation of Africa in international institutions and debates. Africa also strongly contributes to the international governance architecture in terms of trade, finance, environment, migration and debt. Africans resolve conflicts and prevent violence and crime and have service solutions (in areas such health, gender, water, education) that are effective. This scenario is “optimistic” and depends on a number of capacities being available on the continent, specifically (a) the capacity to inspire and provide aspirational leadership; (b) the capacity to coordinate, integrate, and manage across sectors, geographies, and generations; and (c) the capacity to engage civil society, the private sector, and the international community on a continental and regional level.
2. **Regional groupings** – here there are some models of success in some Regional Economic Communities (RECs) but with limited continental learning. There is variable quality of democratic and economic governance across countries, even though there are major improvements in a

number of countries. There is differentiated performance across regions, with some RECs showing respectable performance, but others are not. Countries cooperate with each other but cooperation is ad hoc and driven mostly by bilateral strategies. There are few prominent countries driving the external agenda. Development outcomes are visible but uneven, with isolated success in service provision (health, education, gender, water). External aid is driven by external security needs and donor-based evaluations of capacity and need. The second scenario is the “realistic” scenario and is developed on the need for several critical capacities: (a) ability to achieve performance and results while managing interdependency and mastering strategic planning; (b) capacity to make choices and manage investment priorities across sectors and geographies; and (c) capacity to observe, collect, and analyze data.

3. **Continental and global solutions** – the third and last scenario has externally driven states that are acting with little regional cohesion or cooperation. In this scenario, new technologies and business models on a global scale threaten domestic production. Governance standards for the continent are externally set and Africans are under-represented in international forums and debates. The third scenario is “gloomy” and depends on critical capacities to: (a) adapt to changing environments and external pressure, building resilience and the ability to muddle through; (b) capacity to manage risks, negotiate conflicts, and control violence, while coping with external shocks; and (c) capacity to transform agriculture and manage food supply chains.

On Africa therefore, a number of issues need to be noted - the major ones being the following:

- Africa has not suffered the scourge of the recent financial and global economic crisis. This has been because of the relatively weaker integration of Africa into the world economy (IMF, 2010b).
- Because of migration and other demographic factors, remittances had become a major source of capital flow into the continent. This has been slightly dented by the recent financial and economic crisis (UNECA, 2010).
- Given the pressures on the development countries due to the financial and global economic crisis, ODA commitments and flows have equally been affected as these countries struggle to control their public sector deficits.
- As opposed to the Indian and Chinese experiences, Africa has a significant population burden given the high fertility rates and disease burdens. It is only recently that efforts on the continent have been stepped up to enhance the quality of the population. A large amount of resources have been invested in primary education and focus is now moving towards secondary education. What is needed is for Africa to invest more in technical skills in areas such as medicine and engineering to enhance its competitiveness and presence in the global economy.
- Traditionally Africa has focussed on limited markets and commodities for its socio-economic wellbeing. This arrangement has made the continent vulnerable to natural and idiosyncratic shocks. Africa needs to embark on a project of diversifications and greater socio-economic integration. Trade will remain a great driver of growth for sometime to come.
- Africa also needs to move away from the role of being an exporter of primary commodities. There is urgent need to invest in and have a value-addition transition on the continent.

- The last decade (2000 to date) has seen significant reforms in Africa socio-economic and political reforms. These have resulted in macroeconomic and social stability in large parts of the continent. Events of conflicts have increasingly receded and Africa has maintained robust levels of economic growth of over 5% till 2008. However, the figure remained even positive with recent financial crisis.
- The major reforms that Africa needs are in four areas:
  - Greater investments in **infrastructure** to effectively loosen the logistical constraints on the continent and enhance regional integration and trade.
  - Strengthen the process of regional **integration** and spur regional economic growth poles and dynamism.
  - Invest in and build **institutions** that can foster growth and socio-economic transformation for poverty reduction/eradication; and
  - Foster greater **innovation**.
- Africa therefore needs to focus its energy on fostering the four 'I-s': infrastructure, integration, institutions and innovations.
- Other challenges for Africa are: demographic changes, energy security, ICT infrastructure, agriculture and food security, communicable diseases, and leadership and risk management, weak business environment, limited seed capital, potential for conflict especially resource rich-countries, weak trade links and limited skills for trade facilitation, poor logistical networks, poor career planning and development paths; and high youth unemployment.
- Notwithstanding the reforms, Africa is ready for business as shown by the recent results of the Ease of Doing Business Survey conducted by the World Bank. There is increasing recapitalisation of banks and greater governance enhancement to create the space for partnership between Africa and the rest of the world (World Bank, 2010b).
- African economies need to learn quickly how best to regulate and manage their financial sectors and define practical and workable roles for the central banks this could be done as part of fostering the four 'I-s'.

Given that the OECD, in particular EU, economies remain fragile and there are considerable macroeconomic weaknesses, there is need for global coordination and partnership for reform with the BRICs and low-income countries. For example, there is need for greater macro-economic coordination with and within the G-20 group of countries. This would speed the design of a new financial architecture. The OECD should take a more practical approach to the review of its financial and monetary system.

## V. THE DRIVE FOR GLOBAL RESTRUCTURING AND IMPLICATIONS FOR THE AFRICA:

There are a number of implications of the recent development in the world economy for Africa and how it moves to chart its development course in a turbulent world. Some of the implications are highlighted below:

1. ***Africa and patents management*** – the discussions raised a number of questions on 'innovation management' and how research results are protected as well as disseminated. African countries need to invest in capacity building to protect budding innovations and speed the process of providing patents to new inventions. Industry in the region should be challenged to invest in research, because they have relatively more funds to do so than governments. On the other hand, governments should develop policies for the transfer of research results as well as factoring in the purchase of new equipment and update of research and science skills. This process will overcome the traditional tendency in Africa where indigenous knowledge is equally lost due to lack of documentation.
2. ***Africa and ICT sharing*** – according to the ITU (Zavazava, 2002), infrastructure sharing is an important means of promoting universal access to ICT networks and offering affordable broadband services by reducing construction costs. In light of under-developed markets and the high costs associated with network deployment, carefully crafted sharing policy measures can introduce new forms of competition into the market and stimulate demand for ICT services. The most common forms of ICT-sharing African countries could consider include: infrastructure sharing and collocation; spectrum sharing; interconnection; and unbundling. This would also enhance the competitive edge of African economies in the world economy as well as promote better connectivity.
3. ***Weak marketing and product penetration*** – from the discussions above, it emerged that African products have difficulties in penetrating new markets partly due to weak marketing capacities faced by producers as compared to their EU counterparts. Africa needs to adopt aggressive marketing strategies in order to create globally well known brands from the continent.

Weak training and skills development our discussions also highlighted the importance of training and re-skilling of the labour force. This is more critical in Africa where the focus of training has largely been on numeracy and literacy as opposed to the development of vocational and science skills. These skills are considered as crucial drivers of innovation and technological adaptation and absorption.

4. ***Culture of tracking change/environmental scans*** – it was noted that one of the causes of the financial and global crisis has been the inability of the Euro zone to carry out effective environmental scans and make necessary precautionary adjustments to shocks. Africa equally needs to develop and ingrain in its planning processes the culture to track change and have the flexibility to handle such change.
5. ***Capacity for strategic leadership*** – it is apparent from the discussion that the OECD is strategizing to reinvent itself to stay ahead in global competitiveness and influence. By implication, there is equally need to build the capacity and capability for visionary and strategic leadership across

Africa. It is arguable that without good leadership across the various levels and sectors of the continent, all the other excellent initiatives in Africa will be stifled. Building capacity in good and savvy leadership thus has an enormous return for continent in terms of future social, economic, political, technological and environmental benefits.

6. **Strengthening trade facilitation and integration** – it was obvious from the discussions that Africa should learn from the EU/OECD and the BRICs and create a business environment conducive to entrepreneurship, business linkages, and growth. This means African countries need to, among other interventions, invest in strengthening trade facilitation and regional integration.
7. **Diversification of markets and products** – a World Bank study (Elbadawi et al., 2006) showed African firms face steeper input prices, partly due to distance from cheaper foreign suppliers, and partly because domestic substitutes for importable inputs are more expensive. Africa's poorer institutions reduce its manufactured exports directly, as well as indirectly, by lowering foreign market access and supplier access. Both geography and institutions influence average firm level exports significantly more through their effect on the number of exporters than through their impact on how much each exporter sells in foreign markets. Equally important is the fact that Africa countries need to move away from depending on a few commodities and markets in their global trading arrangements.
8. **Building strong institutions** – one of the reasons for the financial and economic crisis in the Euro zone has been weaknesses in regulatory institutions and pervasive agency-capture as well as lack of consumer protection. The EU needs to build strong institutions that enhance socio-economic and political governance. This could also be recommended for Africa given the wide-spread rent-seeking behaviour and corruption among political and business leaders on the continent.
9. **Enhancing innovation** – as per our discussions in this paper, investing in science, technology and innovation (STI) is crucial for Africa's overall development. Currently under the auspices of NEPAD, there is a target ratio of R&D spending to GDP of 1% for African countries. Africa currently spends at least US\$19 billion on food imports annually yet it has the capacity to be the global food breadbasket. For example, technological innovation in agriculture is crucial in helping African farmers cope with the increasing challenges posed by climate change and any food price increases. The discussions acknowledged the importance of building technical competence; modernising infrastructure as a foundation for technological development; renewing agriculture; stimulating business development and partnerships; energising civil society organisations; and improving the policy environment to promote economic growth through systematic science and technology support. STI is crucial for experimentation, learning and risk taking in the modern globalised economy.
10. **Strengthening risk-management** – from the discussions of the Euro zone experience, it is clear that participation in the global economy also poses significant challenges for the economic management of economies and can lead to major socio-economic and political problems. In particular, the risks of liberalization are particularly high for capital accounts due to the massive size and fluctuating nature of financial flows. Although few countries in Africa are facing the scale of inflows relative to the size of their economies that precipitated the current Euro zone crisis, key lessons concern the importance of developing sound financial systems, appropriate policy and instrument sequencing, avoiding overly rigid exchange rate regimes, caution in financial opening and abilities to manage risks.
11. **Enhancing economic and financial sector management** – the other lesson one can draw from this

experience is the importance of enhancing socio-economic governance and general economic and financial sector management. Policy makers need to make the correct judgments on given macroeconomic stances and their related social and political implications to avoid fragility and general instability. This requires that capacity exist in-country for provisioning evidence-based, unbiased and timely policy advice. African countries also need to find new ways of leveraging development finance and managing ODA resources better.

12. **Enhancing development contracts and natural resource management** – the discussions on the nature of possible partnership Africa can have with the rest of world brought out the importance of building African capacity for development contracts and natural resource management. Economic activity between Africa and the BRICs is on the rise. Much of this activity is concentrated in a handful of African countries and in the extractive industries, such as oil and mining. But increasingly, businesses from BRICs are also pursuing strategies in Africa that are about far more than natural resources: in addition to rapidly modernizing industries, these countries have burgeoning middle classes with rising incomes and purchasing power for buying Africa's light manufactured products, household consumer goods, and processed foods and using its back-office services, tourism facilities, and telecommunications. The differentials in the resource, labor, and capital endowments of Africa and the BRICs make them complementary business partners -- meaning that the current trend will likely be sustained. Any boom in the BRICs is a potentially pivotal opportunity for African countries to move beyond their traditional reliance on single-commodity exports and speed-up value-addition and diversification, especially if growth-enhancing opportunities for trade and investment with the EU continue to be as limited as they have been historically. In that light, the OECD needs to develop new partnership arrangements with Africa.

## VI. IMPLICATIONS FOR ACBF

ACBF can draw a number of lessons from this aforementioned discussion to enhance its activities. These relate to four spheres of the work of the Foundation: (a) how the Foundation sources new ideas for capacity development; (b) what approaches to use for resource mobilization and partnerships; (c) how best to organize the work of the Foundation in knowledge sharing; and (d) what aspects need to shift in the operational programs of the Foundation to handle emerging issues. These are described in more detail below:

- **Getting to Ideas:** From the discussions above, ACBF could identify new ideas that it can to champion for capacity building in Africa as it moves towards the 20<sup>th</sup> Anniversary celebrations. The Foundation could organize a High-Level Forum discussion on many of the emerging issues such as: financial sector regulation, climate change, energy security, managing shocks, etc.
- **Mobilizing Resources and Enhancing Partnerships:** Resource mobilization and the use of networks, is an area where ACBF can learn from other. From discussions, it is foreseeable that traditional sources of development finance i.e. ODA is going to remain under pressure as OECD governments seek to cut their budget deficits. However, net working with the private sector in Europe and elsewhere could provide an alternative source of sustainable finance. ACBF could develop as well as use such networks in its resource mobilization drive.

- **Organizing Knowledge Work:** Knowledge management and the use of networks is an area where Foundation could reconfigure its knowledge management system by strengthening the existence of 'learning' points or community of practice/networks. This could mean transforming the current Technical Advisory Panels and Networks (TAPNETs) and nurturing new networks for which services ACBF could have a cost-recovery arrangement till maturity.
- **Adapting Operational Focus and Programs:** Operational implications and the focus of ACBF programs also need to be reviewed. This would entail a review of ACBF's current products and services to identify areas where new investments could be made. This should be done in line with the possible capacity constraints African countries will face as they get more integrated into the world economy. For example, countries may need capacities to deal with natural and idiosyncratic shocks.

## VII. CONCLUSION

The paper highlighted the need for Africa to develop capacity for strategic thinking and leadership as the EU economies and the OECD broadly, seek to reinvent themselves. Africa needs to work towards developing partnerships and networks that further its development agenda and the goal of poverty reduction on the continent. The new global realities require the adoption of new mindsets and strategic leadership. Primarily, new types of partnerships need to be fostered that engage with Africa, not only through the prism of aid (thus in an unequal relationship of donor versus recipient), but also recognise the diversities in interests of African states. African states also see the opportunities presented by the interest of new actors as a vehicle for diversifying relations, exerting leverage where it exists and taking advantage of developmental projects where these are on offer. Unfortunately, in less democratic and accountable states, such politics may not always have the interest of the population at heart. But the question we should be asking is whether the problem lies strictly with Africa. Equally, ACBF can learn from the discussions to enhance its own business models.



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