

# WHY ARE SUB-SAHARAN AFRICAN ECONOMIES NOT GROWING SUSTAINABLY?

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**Enterprise for  
Development**

Discussion Paper

## About Keith Palmer

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# WHY ARE SUB-SAHARAN AFRICAN ECONOMIES NOT GROWING SUSTAINABLY?

## Summary

High GDP growth rates were sustained across the whole of sub-Saharan Africa throughout the 2000-2012 “long decade”. Some have suggested that the growth trajectory parallels the sustained rapid growth achieved by the Tiger economies in Asia. Others have used the term Africa Rising to suggest that a process of economic transformation has been taking place across the continent. The reality was very different.

Most of the gains were generated directly and indirectly by four simultaneous strong external drivers. The impressive headline growth rates obscured the fact that domestic responses to the external drivers caused a deterioration in the competitiveness of agribusiness and manufacturing. The result was a low rate of private investment, “jobless” growth and, most disturbingly, very few signs of economic transformation away from excessive dependence on production of primary commodities. Agricultural production grew little faster than population growth resulting in a surge of food imports as well as continued loss of market share to competitors in international markets. Industrial output as a share of GDP remained as low at the end of the decade as at the start and manufacturing for export was miniscule.

These weaknesses were in large part the consequence of actions and inactions of host governments in response to the favourable external environment. Despite the buoyancy of fiscal revenues generated by the commodity price boom, public investment to improve and extend infrastructure services was seriously deficient resulting in higher costs and lower productivity of those private sector businesses that needed to use them. Passive fiscal and monetary policy responses to higher domestic demand drove up exchange rates and domestic costs, further eroding the profitability and incentive to invest of businesses producing tradable goods and services, notably agriculture and manufacturing. Passive financial policies facilitated the flow of finance to support investment in businesses producing non-tradable goods and services, while starving producers of tradable goods and services of the finance that they needed to grow. Weak sector policies compounded the disincentive to invest in agriculture and manufacturing despite frequent government statements to the contrary. The result, by the end of the long decade, was that these economies still had among the least competitive agribusiness and manufacturing industries in the world.

In 2013 the favourable external environment deteriorated sharply. The underlying weaknesses were exposed and magnified. In oil exporting countries such as Nigeria the weaknesses are particularly evident; but even in countries with little exposure to the extractive industries, notwithstanding the somewhat higher headline GDP growth rates, the competitive weaknesses and lack of investment in agriculture and manufacturing for export persist. Across the entire region, with current policies, the prospects are for continuing low rates of private investment in competitive industries, even slower growth of formal employment than over the previous “jobless” decade and even more people in “vulnerable” informal employment and absolute poverty.

Major policy shifts going far beyond simply restoring macro-economic balance will be needed if these chronic weaknesses are to be addressed. Limited resources will need to be prioritised to strengthen the productive capacity and competitiveness of businesses producing tradable goods and services. This will only be possible when host governments fully appreciate the nature and magnitude of the challenges their economies face and are willing to effect the necessary changes. At present too many have looked at the headline GDP growth rates and assumed wrongly that all is well.



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# AFRICA RISING?

Much has been written about the rapid growth of GDP in sub-Saharan Africa since the turn of the Millennium. Some have spoken of Lion Economies suggesting parallels with the rapid and sustained growth of the Tiger economies in East Asia. Some have used the term Africa Rising to signal that a process of economic transformation has been taking place across the Continent.<sup>1</sup> The reality was very different.

Over the 2000-2012 period (termed here the “long decade”) the high rates of GDP growth were generated by the direct and indirect domestic responses to four strong correlated external drivers. The impressive headline growth rates obscured the fact that those domestic responses caused, in addition to a consumer boom, deterioration in the competitiveness of agribusiness and manufacturing. The result was a low rate of private investment especially in industries producing tradable goods and services<sup>2</sup> (other than the extractive industries), slow growth of formal employment (“jobless” growth); and, most disturbingly, very few signs of economic transformation away from excessive dependence on low production of primary commodities.<sup>3</sup> After 2012, when the external environment suffered a sharp downturn, these weaknesses were exposed and in some countries magnified.

This paper explains how and why these weaknesses came about. It argues that they were in large part a consequence of the actions and inactions of host governments in response to the unusually favourable external environment. At the end it seeks to explore how governments and donors might act to remove the weaknesses and re-establish sustainable, rapid and inclusive economic growth.

The term sub-Saharan Africa (SSA) is used throughout to refer to all of the economies in the region other than South Africa (which is excluded on the grounds that its economic structure and growth dynamics are very different from all the others).<sup>4</sup> A distinction is made between three groups of economies: major oil and/or mineral exporters; countries with significant exports of both oil or minerals and agricultural commodities; and countries dependent very largely on export of agricultural commodities.<sup>5</sup> Notwithstanding important differences in the composition of their output and exports, it is argued that the pattern of growth and the forces that gave rise to the underlying weaknesses were similar, albeit in different degree, across the entire region.

Extensive use is made of end-notes to maintain an uncluttered narrative, to justify statements in the main text, to note exceptions to general statements and to cite references.

# EXTERNAL DRIVERS OF ECONOMIC GROWTH

## Four external drivers

**F**our simultaneous external drivers drove economic growth over the long decade, three of which were heavily influenced by developments in China.

**Commodity price boom** Starting around the year 2000, and continuing until about 2012, there was an unprecedented, sustained upsurge in the prices of a wide range of primary commodities. The prices of oil and ‘hard’ industrial minerals such as iron ore and copper more than tripled and certain agro-industrial commodities such as palm oil and soya more than doubled (Fig. 1 – top two graphs).

However, the commodity price upswing was not restricted to those commodities (Fig. 1 – bottom two graphs). There were large correlated price increases across a wide range of commodities of major concern to African economies. Cocoa and coffee prices more than doubled. There was a sharp price spike in maize, rice and wheat prices in 2008 and thereafter prices remained at more than twice 2000 levels for the next five years. The gold price rose sharply in the second half of the decade reaching a level in 2012 more than four times higher than in 2000.

This was no typical cyclical upswing; the magnitude and extended duration of the price increases were attributable to a global demand shift attributable in large part to the sustained very rapid growth of demand for industrial commodities from the by-2000 already-large, resource-intensive Chinese economy; and to global supply shifts including the shale oil and gas “revolution” in USA and, especially in the case of gold, the financial crisis.

Since all of the economies in SSA were heavily dependent on exports of primary commodities

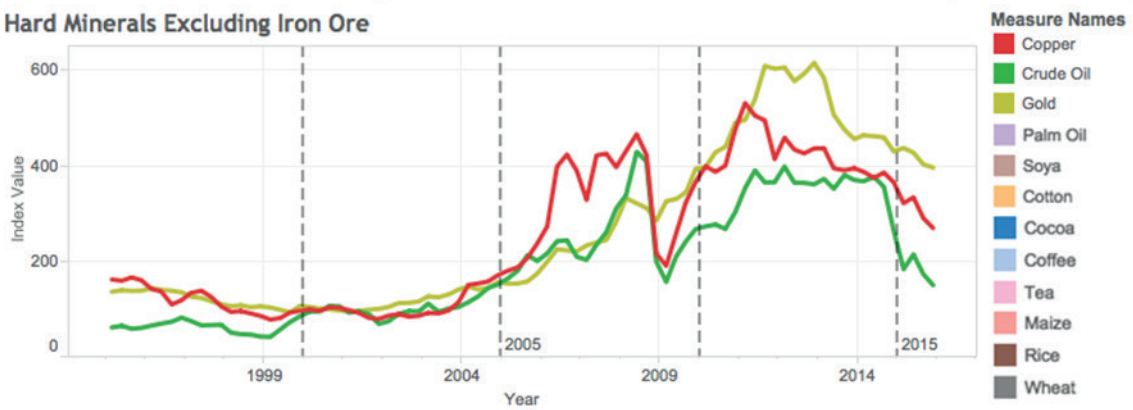
the surge in commodity prices generated huge increases in the value of their exports. Major oil exporting economies saw the greatest gains; in Nigeria annual export revenues increased more than 750% (from about \$18 billion in 2001 to over \$143 billion in 2012). Economies with major exports of ‘hard’ minerals also saw large (if lesser in absolute terms) gains; e.g. in Zambia, a major copper exporter, exports increased about 930% (from about \$1 billion in 2001 to over \$9.3 billion in 2012). Economies with significant exports of both oil and/or ‘hard’ minerals and agricultural commodities similarly saw large increases in export revenues; e.g. in Ghana and Tanzania about 910% and 720%, respectively. Even in economies with little or no mineral exports, the increases in export revenues were very significant; e.g. in Uganda and Malawi 520% and 260%, respectively (Figure 2).

**Large scale capital in flows** A second key external driver was the large-scale inflow of capital to finance exploration and development of oil and hard minerals. The unexploited resource potential of the region had been well known for a long time but interest from international energy and mining companies had been muted until oil and hard minerals prices soared. Then, in response to the expectation that very high prices would be sustained for a long period of time, there was a sharp increase in investment in exploration and development of energy and minerals reserves. Much of it flowed to SSA. It came in part from international oil and gas and mining companies, often located in OECD countries, and in part from Chinese companies, often de facto State-controlled and financed, seeking to secure access to energy and minerals production to feed the Chinese “industrial machine” (just as Western countries had done in decades gone by). Capital flowed into, not only countries with existing mineral production

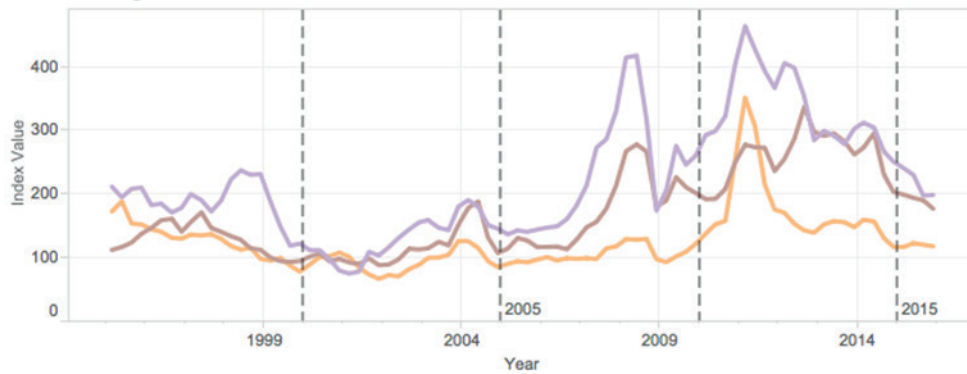


## Nominal Commodity Price Indices, Base Year = 2000 (1995-2015)

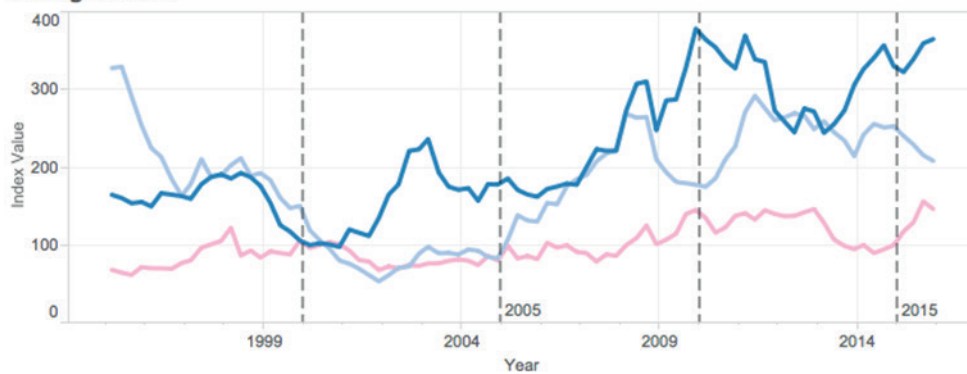
### Hard Minerals Excluding Iron Ore



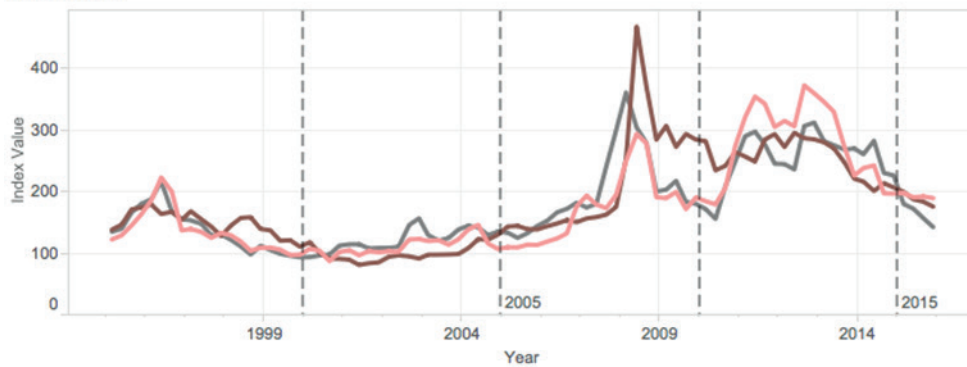
### Industrial Agriculture



### Soft Agriculture



### Basic Grain



**Figure 1** All commodity prices are in dollars base year 2000 taken from IMF commodity price dataset except gold which is taken from Bank of England.

but also into those with good prospects but little or no current production e.g. Mozambique, Guinea and Uganda. These large capital inflows made very little contribution to national income (as explained later) but put upward pressure on exchange rates.

***Cheap manufactured goods imported from China*** A third key external driver was the flood of cheap manufactured goods imported into SSA from China. The low exchange rate of the Chinese currency against the dollar, cheap labour and massive scale economies in manufacturing allowed China to produce and export huge volumes of very cheap manufactured goods around the world. Consumers in sub-Saharan Africa were major beneficiaries. For the first time ever, even low income Africans could afford to purchase a wide range of inexpensive manufactured goods – and vast numbers did so. They acquired a wide range of basic household goods and such former luxuries as cooking stoves, radios, mobile phones, bicycles and in some cases, motorbikes.<sup>6</sup> The downside of this important consumer benefit was the sharply reduced profitability of businesses in SSA seeking to compete with imports from Asia.

***Doubling of aid inflows*** The fourth, rather different external driver was the doubling of aid inflows from OECD donors and rapid growth

from a low base of capital inflows from China (often as a quid pro quo for providing access to mineral resources).<sup>7</sup> In some low income countries aid from OECD donors constituted more than 50% of total government spending by the end of the decade. These foreign currency-financed aid inflows clearly contributed to the welfare of the beneficiaries but an unintended consequence was further upward pressure on exchange rates of recipient countries.<sup>8</sup>

### ***Cumulative impact of external drivers***

The domestic impact of the external drivers was an upsurge in disposable income. Much higher export revenues and cheaper imports created a sort of dollar-financed “helicopter money” generating much higher incomes for the primary beneficiaries *without any immediate increase in investment, physical output or jobs*. The impact was greatest in major oil exporting economies but similar, if lesser, impacts affected every economy across the region.

The responses to this surge in disposable income were to have a profound influence on the development of their economies. Before considering how those influences played out, the focus is next on who the primary beneficiaries were.

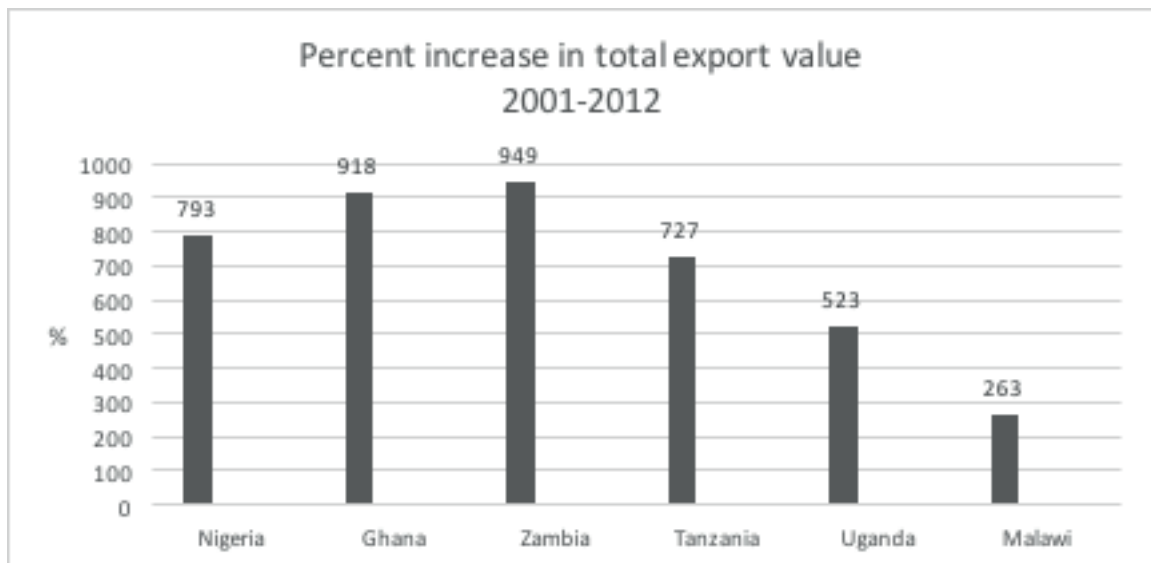
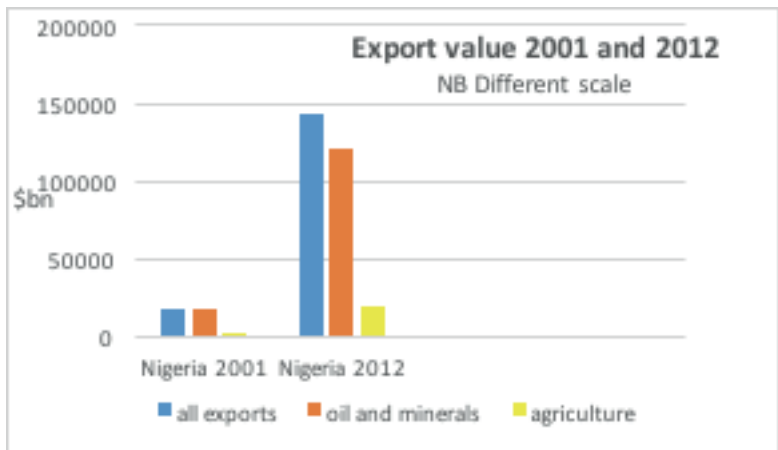
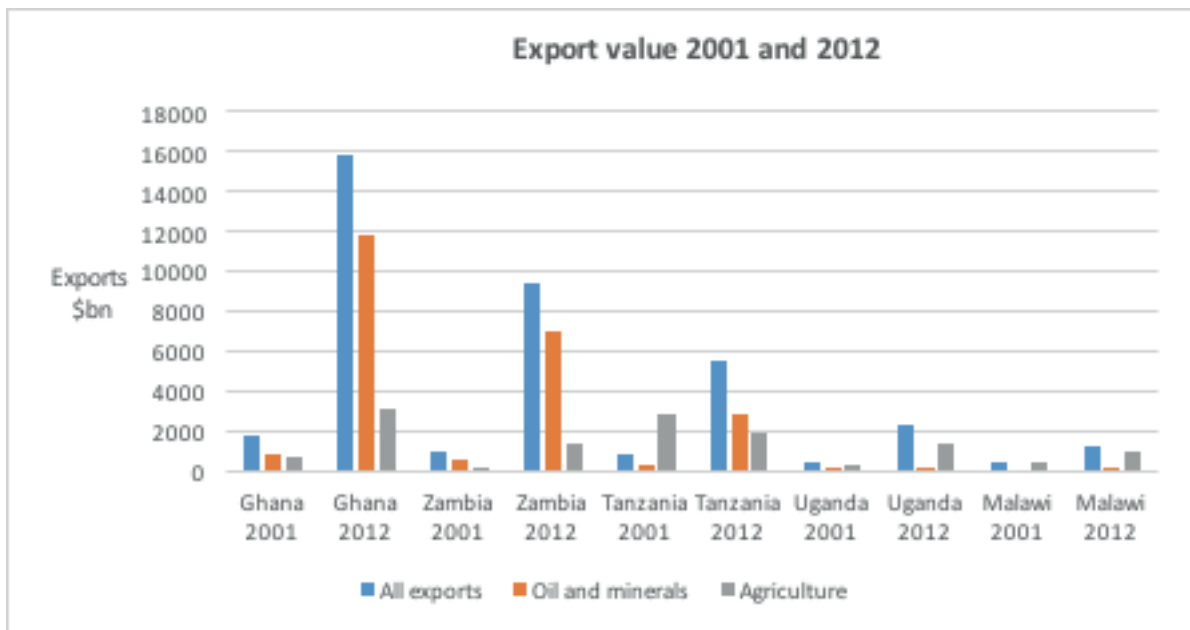


Figure 2  
Source: International Trade Centre [www.intracen.org](http://www.intracen.org)

# WHO WERE THE PRIMARY BENEFICIARIES?

## Primary beneficiaries

There were three major categories of primary beneficiary of the commodity price boom.

The **first category** was host governments in those countries where there was major production of oil and/or hard minerals. Although the large increase in prices of these commodities generated spectacular increases in gross income and profit for the companies that produced them, in reality the associated increase in *national* income was very much less. National income generated by a business is the sum of wages and salaries of its employees, profits and rents accruing to the owners and taxes and other fiscal payments payable to government; plus any additional income generated by national businesses supplying it with goods and/or services. Extractive industries operate giant enclave projects within national economies. A high share of payments for inputs, to employees (many of whom are highly paid expert foreign technicians) and almost all net profits are paid, transferred or retained offshore. Hence, the only major contribution to national income from the extractive industries (in the first instance – see below) went to a *single primary beneficiary*, the national government, in the form of fiscal revenue i.e. royalties, taxes, production and profit shares, etc.<sup>9</sup>

As oil prices shot up, so pre-tax profits of the oil industry increased rapidly and fiscal revenue received by host governments increased even more rapidly, benefitting from the fiscal gearing effect associated with progressive fiscal terms. Since oil prices remained high throughout the decade, so did fiscal revenues. Fiscal revenue from ‘hard’ minerals industries e.g. copper and gold followed a similar pattern although, since there was less resource rent to share, the magnitude of the increase was usually much less than in oil exporting economies.

The **second category** was the “elite” which benefited in various ways from “leakage” of fiscal revenues. The term “elite” refers to the small group of individuals that has strong influence over the way government policies are determined and public resources deployed. “Leakage” is a generic term reflecting a variety of practices all of which, in one way or another, result in the transfer of State income and wealth to a very small number of (subsequently) very wealthy individuals. Of course, the concept of “leakage” applies to a whole range of fiscal revenue streams and has been evident for decades including in countries where fiscal revenue from the extractive industries has not been a significant factor.<sup>10</sup> Nevertheless, the sheer magnitude of the increases in fiscal revenue associated with very high oil (and to a lesser extent hard minerals) prices, and the clear evidence of extensive leakage from this particular fiscal revenue stream, identify leakage to the elite as one of the greatest influences on the overall level and pattern of spending, investment and growth in those economies since 2000.

Although by its nature there can be limited direct evidence of the quantum of leakage, available indirect information is indicative. In Nigeria, the largest oil producer in Africa, in 2011 there were more than 15,700 high net worth individuals (HNWIs) - multi-millionaires - with combined wealth of \$82 billion, hence about 0.01% of the population accounted for about 36% of Nigeria’s total individual wealth. According to the former (now fired) Central Bank Governor more than \$20 billion of oil income went missing from the national oil company; and a further more than \$20 billion was allegedly subject to leakage from the Delta region.<sup>11</sup> In Angola, the second largest oil producer in the region, there were more than 6400 HNWIs with combined wealth of more than \$30 billion, hence about 0.03% of the population accounted for about 45% of

total individual wealth. In Zambia, Africa's largest copper producing country, there were about 900 HNWI's with combined wealth of about \$4.5 billion.<sup>12</sup> It seems clear that a very small number (and tiny proportion) of the population appropriated a very high share of total spending power associated with high oil and hard mineral prices.

The **third category** of beneficiary was the owners of businesses operating in agricultural supply chains. Unlike the oil and mining industries, agricultural producers export via long agricultural supply chains. The price received by farmers at the 'farm-gate' is net of deductions retained by market intermediaries e.g. traders, processors and by the State in the form of export taxes, marketing levies etc.<sup>13</sup> Typically there is limited competition in many segments of these supply chains and so intermediaries can capture a high share of the export price. Moreover many host governments across the region extract various taxes, levies and the like from smallholder farmers. Consequently the share of the border price paid to farmers at the farm-gate could be as little as 20% depending on the crop and location. When border prices rose a high share of the price increases could be retained by intermediaries as higher profits and by the State. The share of the price retained by

smallholder farmers and per capita income gains were often small.

## Distribution of primary gains in different countries

The magnitude and distribution of primary gains from commodity price increases were a function of the composition of exports in each country. In major oil exporting countries, the income gains were very large and went almost exclusively to the host government and the tiny elite. In countries with a mix of mineral and agricultural exports the aggregate gains were not as large but still substantial and a high share of those gains went to the host government, the elite and owners of market intermediaries exporting agricultural produce. In countries with predominantly agricultural exports the aggregate income gains were much smaller and somewhat more widely distributed with a higher share going to market intermediaries.

The high share of the large gains that went to government and a tiny elite in many of these countries had an important influence on both the growth trajectories of their economies and on the decisions taken by governments that gave rise to them.

# RESPONDING TO THE EXTERNAL DRIVERS

The surge in domestic spending by the primary beneficiaries induced a marked secondary response from host governments, in markets for non-tradable and tradable goods and services and in financial markets.

## Host governments

**Large increases in fiscal revenue** Most host governments saw large increases in fiscal revenues. The largest were in oil and mineral rich economies but there were significant increases everywhere from higher taxes on exports and imports and in low income countries from rapidly growing aid inflows.

**Higher recurrent expenditure** Despite the exceptional buoyancy of fiscal revenues, very few host governments adopted revenue stabilisation schemes, invested in sovereign wealth funds or started to pay down government debt. Instead a high share of increased fiscal resources was allocated to increase recurrent government expenditure, a high share of which went on increasing the public sector payroll (public sector employment increased more than 40% over the decade) and on increased subsidies, notably on oil products.

**Under-investment in infrastructure** With few exceptions, governments chose not to allocate much of the higher fiscal revenues to fund public investment.<sup>14</sup> Public investment as a percentage of GDP was low; little higher than over the previous decade; and barely half of that investment was spent on improving and extending infrastructure services. Publicly-funded infrastructure investment as a percentage of GDP was less than half that in comparable Asian countries. Moreover, a high share of funding for infrastructure investment came not from domestic resources but from multi-lateral development agencies and the Chinese.

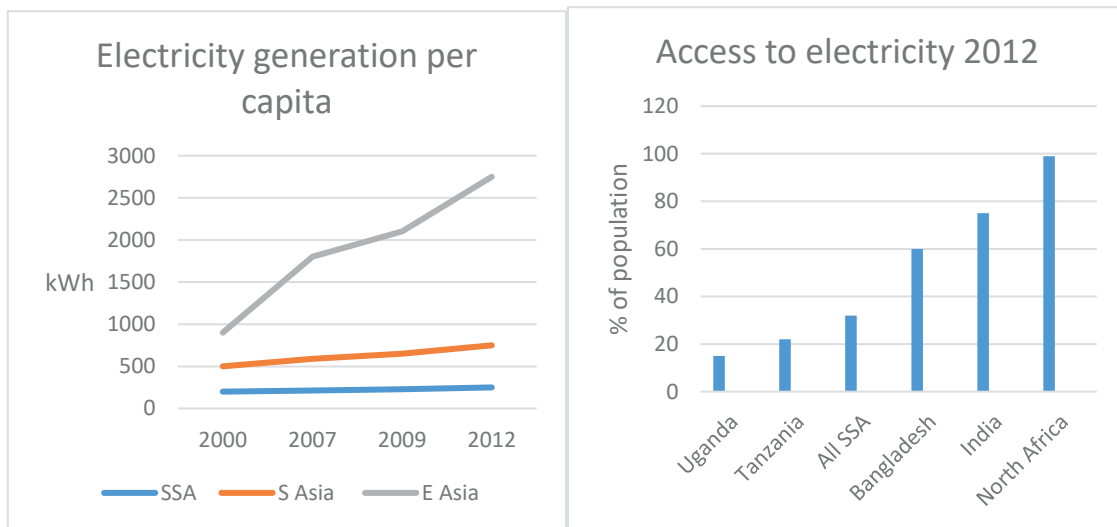
The result was acute under-provision of infrastructure services – electricity, roads and ports, water - at precisely the time when demand for those services was growing strongly. With only a few notable exceptions, by the end of the decade existing publicly-funded infrastructure services were very poor quality, very expensive and there had been no significant improvement in access for the vast majority (Fig 3). Nigeria is just one example where, despite huge increases in fiscal revenues from oil, under-investment in infrastructure resulted in deterioration in the quality of infrastructure services over the decade. In 2012 it ranked 117th in the world compared to e.g. much poorer Rwanda ranked 54th.<sup>15</sup>

Electricity supply was a particular problem. State-owned utilities' fuel costs increased as oil prices rose, squeezing their cash flow. Most governments were unwilling to permit their utilities to increase tariffs for existing (mostly better off) customers to anywhere close to cost-recovery levels.<sup>16</sup> Nor were they willing to allocate more public capital for infrastructure investment. Consequently, the utilities remained almost wholly reliant on (strictly rationed) loans from multilateral institutions and the Chinese. Under-investment was so acute that even existing capacity was inoperative much of the time and system losses were more than double the world average.<sup>17</sup>

The quality, cost and access to infrastructure services were all markedly inferior to those that were available to private sector businesses in developing countries in Asia with which African businesses had to compete.<sup>18</sup>

**Figure 3: infrastructure costs, access and impact on private investment in SSA**

<b>Power tariffs (USc/kwh)</b>	0	USc/kWh	50
SSA	5	-----	45
Other developing countries	5	-----	15
<b>Road freight costs (USc/ton-km)</b>	0	USc/ton-km	15
SSA	4	-----	14
Other developing countries	2-4		



**Impact on private investment**

“Whether for power, water, road freight ...the tariffs paid in Africa are several multiples of those paid in other parts of the developing world”

“Africa’s firms report losing 5% of their sales because of frequent power outages... a figure that rises to 20% for informal firms unable to afford back-up generation”

“In low income countries infrastructure is a major constraint on doing business and depresses productivity by about 40%”

Source: Africa’s Infrastructure A Time for Transformation Africa Development Forum 2010.

Business surveys repeatedly showed that the poor quality and high cost of infrastructure was one of the greatest impediments deterring investment and slowing growth of private sector businesses. Power, water and road freight tariffs were more than double those in comparable developing countries.<sup>19</sup>

## Market for non-tradables

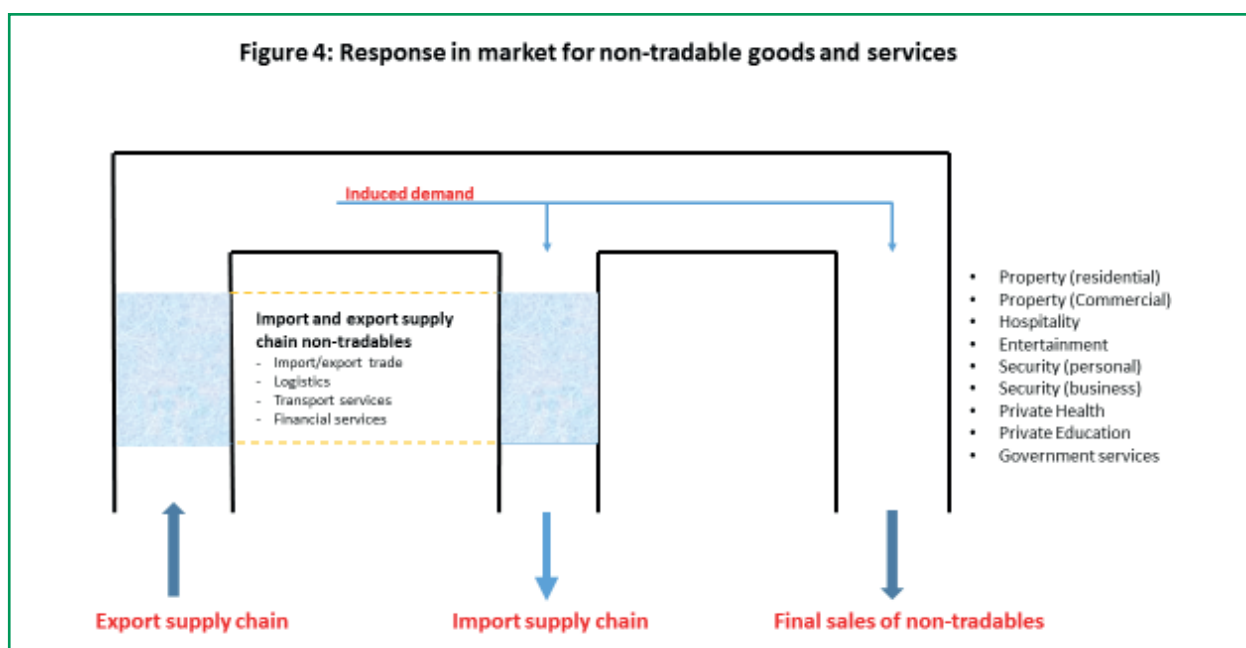
**The consumer boom** The upsurge in domestic spending generated a consumer boom. There was a flood of imports and much higher demand for non-tradable goods and services ('non-tradables'). The higher demand for non-tradables was generated directly and indirectly. Much of the increased *direct* demand came from higher spending by the elite (especially, but not only, in the oil and mineral rich economies). Their spending went on such non-tradables as "high-end" residential accommodation, hospitality, restaurants, entertainment, private health and education and a range of domestic and security services. Additional demand came from higher spending by public sector employees as recurrent government spending increased rapidly (in part as a result of higher donor-funded spending on social programmes such as health and education).

Higher demand for non-tradables was also generated *indirectly* as rapid growth of exports and imports induced strong demand for goods and services produced by businesses operating

in export and import supply chains (Figure 4). Export supply chains include those business activities necessary to deliver products from factory- or farm-gate to domestic or overseas end-markets e.g. storage, processing, wholesale and retail trading, transport services, logistics (warehousing, customs clearance, etc.) and financial services. Import supply chains include essentially the same business activities, typically undertaken by the same firms, to deliver imports from the border to end-customers. All of these businesses in effect produce non-tradables.

**Response in the market for non-tradables** The sharply higher demand induced price increases of non-tradables.<sup>20</sup> Businesses could raise their prices with relative ease because capacity was limited at the start of the decade, demand grew very rapidly, sales were mostly to price inelastic high-end consumers and domestic competition was limited (because typically there were few incumbent domestic suppliers and significant barriers to entry).<sup>21</sup> The combination of rapid growth of turnover as domestic spending power boomed and the ability to adjust prices to maintain high margins resulted in strong growth in profitability of these businesses.

Inflation was particularly pronounced at the top end of the property market where demand for high quality residential and commercial real estate (from the elite, international staff of public agencies and senior managers of private companies) was very strong whereas





initial supply was very limited. By the end of the decade property prices for “ordinary” residential accommodation in major cities across the region rose to levels that were unaffordable for all but a tiny minority of the population.<sup>22</sup>

The market response to strong demand and higher prices for non-tradables was more private investment. There was: heavy investment in high-end residential and commercial property and a related boom in construction and businesses supplying building materials (particularly cement, timber and fabricated metal); investment in a range of industrial and service businesses focused on the supply, finishing, marketing and after-sales service of mostly imported consumer goods; and investment in corporate and high-end personal financial and professional services.

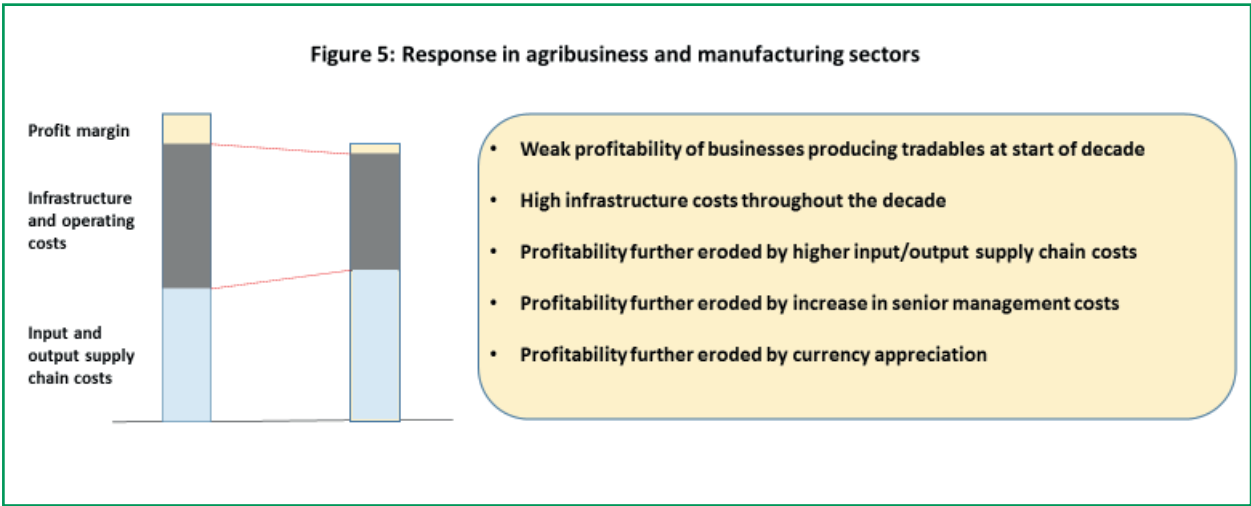
The growth of these businesses created strong demand for well-educated and experienced African senior managers and professionals to take on senior roles in private companies, financial institutions, professional services firms, government and State enterprises, international agencies and NGOs.<sup>23</sup> Since the supply of suitable candidates at the start of the period was very limited, the rapid growth in demand generated inflationary pressure at the top end of the labour market. Employment costs for suitably qualified nationals (some of whom were returning diaspora) increased rapidly; in some business areas e.g. financial services, reaching levels not far short of the cost of employing comparable staff in OECD countries.<sup>24</sup>

The growth of non-tradable businesses and of government recurrent spending led to the emergence of a very small but rapidly growing upper middle class and a slightly larger lower middle class.<sup>25</sup> Their increased spending power induced a further round of consumer spending and more demand for non-tradables, inducing further investment.

Investment in businesses producing non-tradables was particularly attractive because it offered lower risk as well as high expected profits. This was because these businesses could flex prices to maintain margins if faced with unplanned cost increases; a typical example being the extra costs of providing and operating expensive backup electricity generators when grid supply failed.

### Market for tradables

**Response in the market for tradables** The situation facing businesses engaged in production and sale of tradable goods and services (“tradables”) other than the extractive industries – notably agriculture and manufacturing - could not have been more different.<sup>26</sup> They faced higher costs because of inadequate infrastructure; higher costs because higher prices charged by export supply chain intermediaries were passed back, reducing ex-factory or ex-farm gate profitability; and higher costs recruiting senior managers in competition with businesses producing non-tradables. They also faced downward pressure on operating margins as exchange rates appreciated (Figure 5). Unlike businesses producing non-tradables, they could not pass on higher costs



to end-customers, instead profitability and the incentive to invest suffered.

***Agribusiness*** Investment in agriculture had long been seen as a major opportunity to increase incomes and reduce poverty in rural Africa. High international commodity prices and strong growth of domestic demand for food could have been the catalyst for increased investment and higher farm incomes. The opportunity could have been grasped; with very few exceptions, it was not. In most countries investment in primary agriculture by small, medium or large scale farm enterprises was very limited;<sup>27</sup> and there was even less investment to improve productivity and incomes of smallholder farmers.<sup>28</sup>

Infrastructure was a particularly binding constraint. There was chronic under-provision of bulk water supply for irrigation, feeder roads to bring produce to markets and grid-linked electricity supply. Without the necessary infrastructure, yields were much lower and costs much higher than those of producers in the many countries that had better access to agriculture-supporting infrastructure.<sup>29</sup> If farmers sought to finance and provide their own infrastructure they faced much higher costs than competitors whose governments had already provided infrastructure, often free or highly subsidised. Either way farmers' incomes would be eroded.

Supply chains in agriculture are particularly long and competition in trading, transport and processing typically weak. Businesses providing agricultural supply chain services were well-placed to capture a high share of the increase in rising border prices, paying much smaller price increases to farmers at the farm-gate.

Primary agriculture is particularly high risk. In addition to the "normal" risks e.g. weather, pests and commodity prices, there are substantial additional costs and risks inherent in early-stage agriculture.<sup>30</sup> Since few of those risks could be managed or mitigated cost-effectively, investment in agriculture offered investors the unpalatable combination of low expected profitability and high risk.

In Asia many host governments adopted strong sector policies and programmes to stimulate development of agriculture e.g. price support

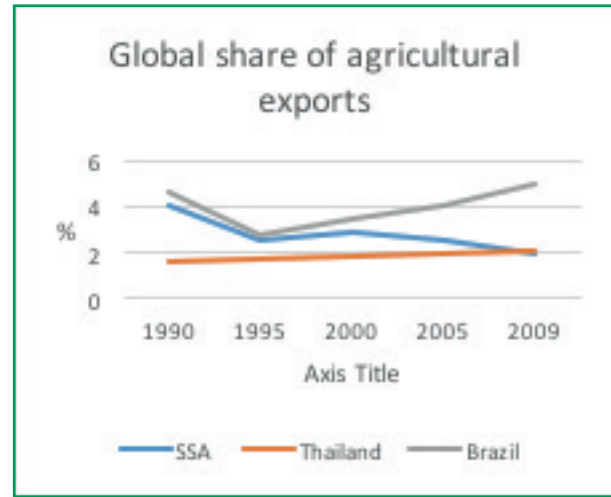
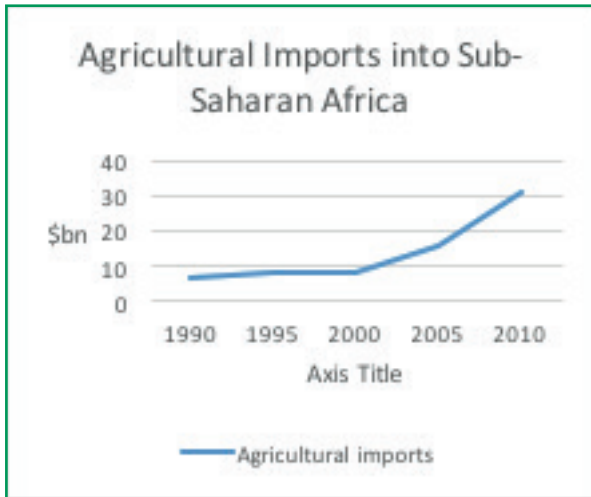
programmes, credit and credit guarantee facilities and/or input and infrastructure subsidies.<sup>31</sup> In SSA few did so. Most price intervention mechanisms were more focused on keeping food prices low for urban consumers than on supporting productivity improvement of farmers. Fertiliser subsidies were poorly targeted and failed to achieve sustained productivity improvements.<sup>32</sup> There was practically no public investment in agriculture-supporting infrastructure and hardly any farm credit or credit guarantee programmes. In fact, rather than support agricultural development, many governments imposed levies and taxes on smallholders, reducing their incomes and their incentive to improve productivity. This lack of government commitment was exemplified by the failure of the vast majority of governments to comply with the pan-African commitments to support agricultural development that they themselves had entered into.<sup>33</sup>

Faced with high costs and risks, fierce competition from overseas and weak support from host governments, it is not surprising that there was little investment in commercial agriculture nor that smallholders' productivity and output stagnated. The consequences of the failure to generate a domestic supply response to the strong growth of domestic and international demand were a surge in food imports and rapid loss of market share to Asian and South American producers in international markets (Figure 6).<sup>34</sup>

***Manufacturing*** Investment in manufacturing industries was even more problematic. In addition to the high domestic costs associated with weak infrastructure and excess demand for non-tradables, manufacturing businesses faced downward pressure on selling prices (from Asian competitors and appreciating exchange rates); and had to operate in a weak governance and regulatory environment with a less experienced workforce.<sup>35</sup> The result was that the share of manufacturing in total value added declined over the decade (from an average of 14% in 1990-99 to 11% in 2000-2011).<sup>36</sup>

A very high share of industrial output was sold in domestic markets, much of which benefitted from a degree of non-tariff protection from imports. More than half of this output came from processing of agricultural commodities, both domestic produce for export and/or

Figure 6



(Source: FAOSTAT and World Bank (2013))

imported produce for sale in domestic markets. A smaller but significant share came from businesses engaged in final-stage production and distribution of imported basic and intermediate goods e.g. chemicals, plastics, metals and beverages; and from businesses providing inputs to the construction industry e.g. cement, timber, fabricated metal. The growth of turnover and profits resulted from the surge in domestic demand generated by the consumer boom but did not generate many new jobs.

There were a few examples of manufacturing businesses that exported in direct competition with imports from Asia e.g. Ethiopia and Tanzania. In Tanzania the relatively rapid growth of manufacturing exports was mostly to inland African countries where (mineral-related) demand was strong e.g. DRC, benefitting from the transport cost advantage over importers from Asia. Even with that benefit, many of these businesses, faced with strong competition from Asian suppliers, operated on very thin margins and had very little access to finance.<sup>37</sup>

In some countries e.g. Zambia, even the transport cost advantage of an inland location could not compensate for the strength of competition from importers; the result was closure of entire industries i.e. de-industrialisation.<sup>38</sup>

Labour-intensive manufacturing for export - the sector that in Asia proved to be the key source

of rapid growth of incomes and jobs – did not even get started. The high domestic costs, ultra-competitive selling prices, weak regulatory and business environment and inexperienced and relatively unproductive workforce made investment in these industries in SSA unviable.<sup>39</sup> Average costs were at least 20% higher than in comparable countries in Asia with which businesses in SSA had to compete;<sup>40</sup> non-fiscal trade-related costs were assessed as equivalent to a trade tariff of 40% compared to 15% in other ACP countries.<sup>41</sup> Almost all countries in the region were in the lowest quartile in a ranking of global competitiveness. There was an almost complete absence of foreign direct investment in manufacturing for export even though wage rates in the region were relatively low. The result was the loss to SSA of the technology transfer, management expertise and access to global markets that had proved so important in many (now middle income) countries in Asia.

Host government support policies were mostly ineffective. Tax holidays and investment promotion centres were never going to address the underlying poor profitability and high risk. There were very few mechanisms aimed at dealing with the key issue, lack of competitiveness. Even efforts to develop manufacturing within Special Economic Zones/ Export Zones in coastal locations, with very few exceptions, failed.<sup>42</sup> By the end of the decade the region's share of global manufacturing exports was less than 1%, just as it had been in previous decades.

## Financial markets

**Availability and cost of capital** The strength of the external drivers generated strong growth of national savings, much of which was in the hands of the elite and/or in retained earnings of businesses producing non-tradables.<sup>43</sup> Although a significant share of the elite’s increased wealth was held or transferred offshore there remained significant amounts of capital available for investment by them in domestic businesses. With the increase in the money supply, the availability of credit from commercial banks also increased and the cost of credit eased for high quality borrowers.

### Financing investment of non-tradables

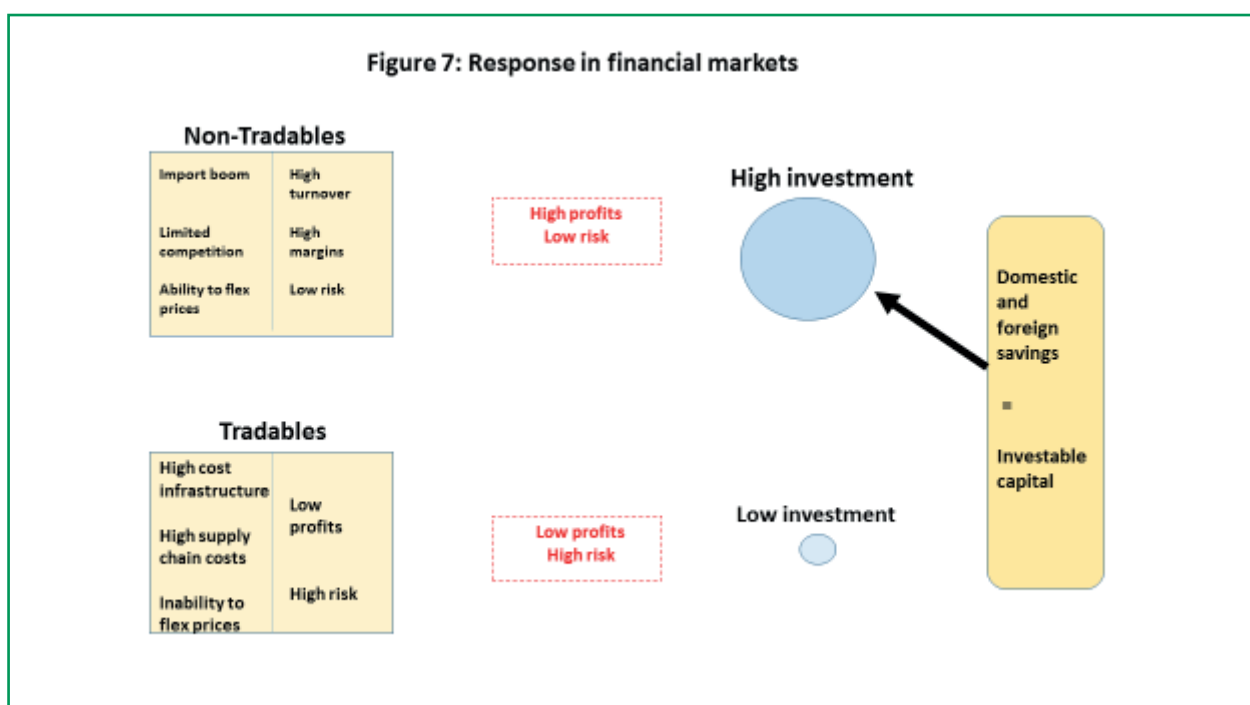
Established supply chain businesses were usually profitable and could finance a high share of their fixed capital requirements out of internal cash flow; and working capital was readily available from commercial banks. Non-tradable businesses needing external finance to grow their businesses found a ready audience among the elite if their opportunities offered high expected returns and low risk. Investment in “high end” residential and commercial property was particularly attractive as rents and capital values appreciated strongly in line with the strength of demand.<sup>44</sup>

**Financing investment of tradables** Exactly the opposite was the case in agriculture and manufacturing for export. Since most

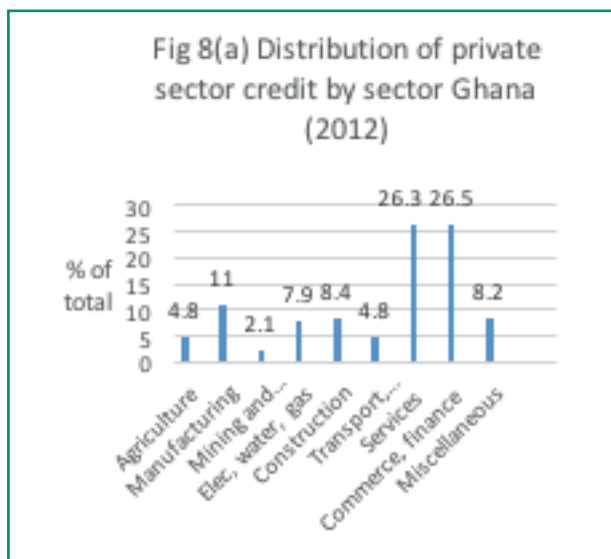
opportunities were early stage and therefore high risk, minimum risk adjusted returns required by financial investors were high. Moreover, many of the businesses seeking finance had limited track records and weak balance sheets. Consequently, few tradable businesses were able to access the capital they needed to develop and grow (Figure 7).

The same pattern was evident in the domestic credit markets. More than 80% of total bank credit to the private sector went to finance non-tradables including trade, services, property and “high-end” household borrowers (Figure 8). Less than 15% went to support manufacturing and less than 5% to agriculture, most of which financed traders to purchase output from farmers, not to farmers to improve their productivity.<sup>45</sup>

**Lack of finance not the real problem** Business surveys in most countries across the region cited lack of finance as one of the greatest problems facing businesses. While true at one level, this is misleading. The problem was rarely lack of finance per se; rather it was lack of sufficient businesses with investment opportunities that met financial investors’ minimum risk-return requirements. There were plenty of such opportunities in non-tradable industries; very few in agribusiness and manufacturing for export.



**Figure 8** Distribution of private sector credit by sector – Ghana and Kenya



Source: Fig 8(a) Ecobank: Middle Africa Insight Series: Banking, September 2013.

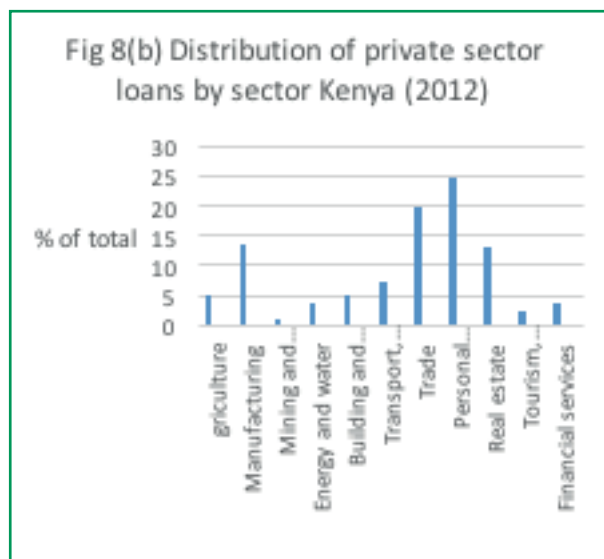


Figure 8(b) Kenya Financial Sector Stability Report Dec 2012.

**Vicious circle** The inability to finance investment in agribusiness and manufacturing was an inevitable consequence of the way that financial markets deploy capital in accordance with expectations about short and medium term risk adjusted returns. The result was that businesses producing tradables were starved of investment. This created a vicious circle where: most agribusiness and/or manufacturing businesses seeking finance were early stage; because they were early-stage they had high costs and risks; hence they could not access finance for investment; hence were unable

to undertake the investment that would have reduced their costs and risks, improved their profitability and ability to access commercial finance; and hence they remained early stage, unfinanceable and increasingly uncompetitive indefinitely.

In Asia a generation ago host governments had responded to this problem by making available long term “patient” development capital exclusively to support private investment in agribusiness and manufacturing for export. In SSA comparable support was not forthcoming.

# WHY SUB-SAHARAN AFRICAN ECONOMIES ARE NOT GROWING SUSTAINABLY?

## Underlying weaknesses

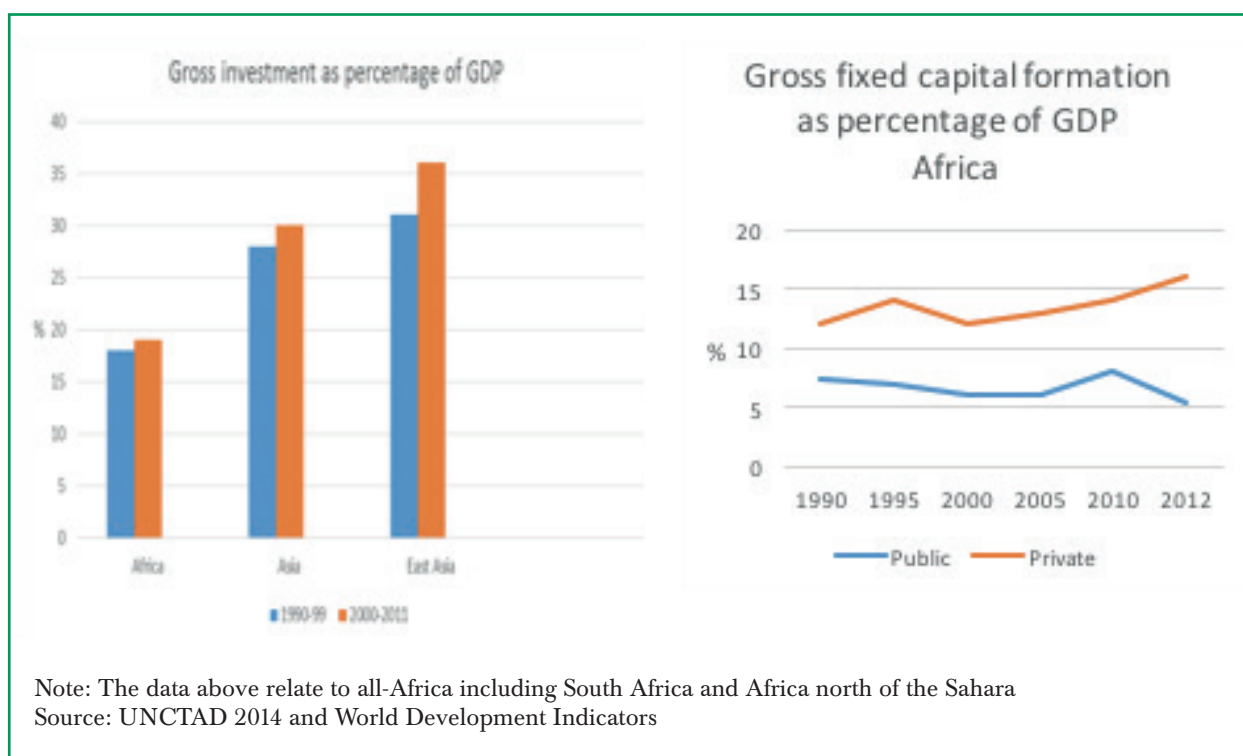
The same responses to the external drivers that generated impressive headline growth rates, the consumer boom and induced investment in non-tradables also gave rise to chronic underlying weaknesses: low rates of private investment, “jobless” growth and lack of economic transformation.

**Low rate of private investment** Private investment as a percentage of GDP was much lower than would be needed to sustain high GDP growth rates in a less favourable external environment and much lower than in comparable developing countries in Asia (Figure 9). This was because the relatively higher rate of investment in the smaller non-tradables sector was more than offset

by the low rate of investment in the (large) agribusiness and (potentially most dynamic) manufacturing sectors. The property and construction boom, full hotels and restaurants, busy shopping malls and explosion of traffic on increasingly congested roads in major cities gave a misleading appearance of an economy-wide investment boom.

There were just a few notable instances where high rates of investment and rapid growth were achieved that were not dependent on the strength of the external drivers, notably tourism and mobile telephones. Tourism, mostly in East and Southern Africa, exploited the advantages of the spectacular natural environment and was focused heavily on “high-end” mostly foreign tourists able and willing to pay extremely high

Figure 9



prices, sufficient to enable businesses to make good profits despite high domestic costs.

The spectacular growth of the mobile phone industry was founded on a novel business model that offered affordable services to even low income African consumers. The consumer benefits were outstanding: more than 300 million African mobile phone subscribers in little more than a decade. However the contribution to national value added and job creation were much more muted; a high share of gross revenue was remitted overseas to satellite service providers, mobile phone manufacturers and as profits and debt service to foreign investors and lenders. Growth was rapid but from a tiny base so the overall contribution to GDP was modest. The high hopes that much improved access to mobile phone services will stimulate more investment, jobs and growth in unrelated industries have yet to be realised.

***Jobless growth*** The slow growth of formal employment similarly reflected the pattern of growth generated by the external drivers. Higher commodity prices and lower prices for manufactured imports increased domestic income without any immediate increase in physical output or extra jobs. The extractive industries accounted for about 60% of the total increase in GDP, yet employed less than 1% of the total workforce throughout. Slow job growth in agribusiness and manufacturing reflected the low rate of investment in those sectors.

The respectable growth (3-4%) of formal employment in non-tradable industries e.g. wholesale and retail trade, construction and communications was a response to the consumer boom. So was the robust job growth in private services but more than half of the extra jobs were in various types of domestic service such as cooks, cleaners, gardeners and drivers and in private security services, almost all on low pay and generating little added value.

The most rapid growth of formal employment was in government and social services (by the end of the decade accounting for half of all the extra jobs created in low income countries), reflecting the large sustained increase in recurrent public spending funded by the commodity price boom and aid inflows (Figure 10).<sup>46</sup>

Not only was GDP growth “jobless” but those jobs that were created were in government and private services - the least productive sectors.

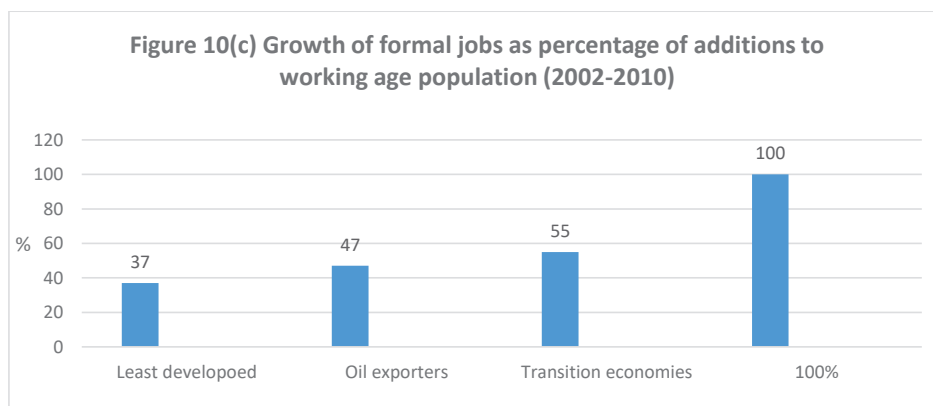
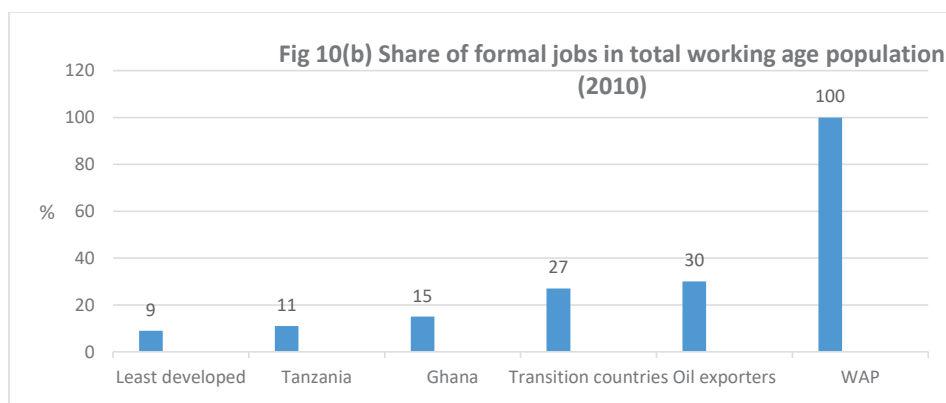
***Lack of economic transformation*** In Asia a generation ago, the Tiger economies achieved profound transformation of their economies resulting in sustained rapid growth of incomes and large reductions in poverty. This transformation was founded on major productivity improvements in agriculture, migration of the growing workforce from rural to urban areas and a high rate of investment and job creation in competitive labour-intensive manufacturing industries.<sup>47</sup>

In SSA there was no comparable transformation. There was little improvement in productivity or incomes in agriculture; low rates of investment and job creation in competitive manufacturing industries; and rapid migration from rural to urban areas but now from low income, low productivity agriculture to almost-as-low income and productivity private services (Figure 11). Rapid migration from rural areas was a natural response to low incomes and poor prospects facing smallholders. When migrants arrived, unless they were lucky or well connected, they found few well-paying job opportunities in government, industry or high-end private services. Instead they encountered high spending by the elite and the small but rapidly growing middle class which generated “trickle down” benefits in the form of greater formal employment in domestic services and further down the food chain in informal urban services.

In 2010, about 70% of the total workforce in low-middle income countries and more than 85% in low-income countries were in informal employment either as smallholder farmers or in various informal private services in urban areas; all jobs characterised as “vulnerable”, on very low incomes and generating little added value. Despite rapid GDP growth the proportion and number of people in informal employment increased over the decade (Figure 10c).<sup>48</sup>

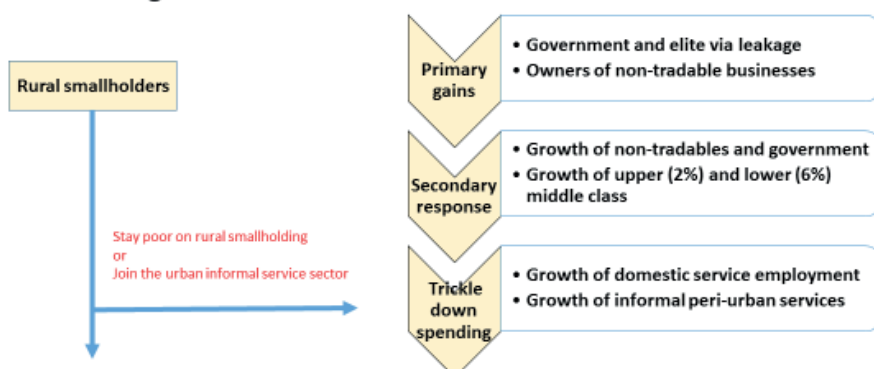
**Figure 10(a) Growth of formal employment by sector and type of economy (2002-2010)**

	Least developed	Transition countries	Oil exporters
Government and social services	50%	34%	11%
Retail, hospitality, finance, business services	13%	26%	34%
Construction	7%	4%	17%
Transport, communications	4%	7%	16%
Agriculture	18%	13%	19%
Manufacturing	8%	15%	2%
Extractives, utilities	<1%	<1%	<1%
Total	100	100	100



Source: McKinsey 2012 and ILO 2011.

**Figure 11: Little or no economic transformation**





## After the 2012 downturn

**Changes in external environment** After 2012 three of the key external drivers of growth went into reverse. There were abrupt large falls in the price of oil and many industrial minerals and some (but not all) agricultural commodities (see Figure 1). There was a sharp fall in capital inflows to finance the extractive industries, this a direct result of the adverse shift in industry perceptions about future prices of those commodities. The catalyst for this dramatic downturn was the slowdown and rebalancing of growth in China compounded by fundamental changes on the supply side of the oil market – not least the shale oil and gas “revolution” in the USA. The fundamental nature of these changes strongly suggests that the current less favourable external environment will persist for quite some time. (Not all commodity prices were similarly affected: cocoa, coffee and gold prices remained strong and maize and rice prices remained firm initially, before declining a few years later).

At about the same time the rapid growth of aid inflows from OECD countries came to an end, offset in some countries by the growth of capital inflows from Asia (mostly China).

**Domestic consequences** The deterioration in the external environment had an adverse but differential impact on economies across the region.

**Major oil and/or mineral producers** In these economies the adverse impact was swift and strongly negative. Much lower commodity prices induced sharp reductions in fiscal revenue, necessitating reductions in government spending and typically further cuts in public investment. Lower export revenues and reduced capital inflows induced sharp falls in exchange rates, imported inflation, an end to the consumer boom and reductions in investment in non-tradables. Contraction of the money supply reduced the availability and increased the cost of capital and credit.

There was little compensating increase in investment by businesses producing tradables despite higher devaluation-induced margins. This was because: the productive capacity inherited from the previous decade was weak, infrastructure services remained poor quality

and high cost and investment capital was even less available and more expensive.<sup>49</sup>

**Economies without major oil and/or mineral production** On the surface these economies appeared to have fared much better. Lower oil prices in oil-importing countries, continuing high prices for certain agricultural commodities and gold and higher capital inflows from Asia (particularly China) in some countries, benefited many of them to a greater or lesser extent. GDP growth rates were higher, exchange rate volatility lower and fiscal deficits more manageable.

However, even in these economies, the underlying weaknesses evident during the boom years persisted. Inadequate and inefficient infrastructure, the high domestic cost structure and inability to raise finance on affordable terms continue to hold back private investment in agribusiness and manufacturing. Even in the few countries where there has been progress exporting manufactured goods e.g. Tanzania, sustained growth has been threatened by continuing difficulties for these mostly-informal businesses accessing growth finance. Consequently, jobless growth and continued over-dependence on primary commodity exports continue unchanged.

## How and why did the weaknesses come about?

The weaknesses came about as a result of actions and inactions of host governments in response to the strength of the external drivers.

**Passive management of domestic demand** drove up exchange rates and domestic costs. Governments could have adopted counter-cyclical policies to moderate exchange-rate appreciation, reduce consumption and contain domestic inflation. They chose not to do so.

**Under-investment in infrastructure** degraded the quality and increased the cost of infrastructure services, thereby reducing the competitiveness of tradable businesses that needed to use them. Governments could have allocated a higher share of rapidly growing fiscal revenues to support improvement and extension of infrastructure services. They could have used active tax and/or user charge policies

to generate more savings to finance more infrastructure investment. Only a few of them did so.

***Inconsistent and ineffective and sometimes perverse sector policies*** weakened incentives for investment in agribusiness and manufacturing in many countries.

***Passive financial policies*** starved agribusiness and manufacturing businesses of the investment capital that they needed to develop and grow. Governments could have devised ways to channel development capital to support private investment in priority sectors. They chose not to do so.

The contrast between the economic policies adopted by governments in sub-Saharan Africa and those adopted so successfully by the Tiger economies in Asia is stark (Figure 12).<sup>50</sup> The success of the Tiger economies was founded on delivery of three key government policies: maintaining competitive exchange rates and domestic cost structures; heavy public investment to develop the infrastructure needed to complement and support private enterprise; and sustained provision of policy support and ample long term low cost development capital for agriculture and manufacturing for export. In most sub-Saharan African countries, government policies were more or less diametrically the opposite.

Why host governments made those choices lies in the realm of political economy. The symbiotic relationship between the elite and government and political pressures on governments to satisfy the demands of their electorates were undoubtedly key influences. The exclusive focus on external and fiscal balance (no doubt encouraged by certain international agencies) rather than deploying a pro-active development strategy also contributed.

## What can be done?

What can be done to address the underlying weaknesses given that the external environment is likely to continue to be less favourable over the next decade?

***Higher rates of investment in agribusiness and manufacturing are essential*** There cannot be rapid sustainable growth of incomes without higher rates of investment in agribusiness and/or manufacturing. As incomes rise, demand for food and manufactured goods rise and the higher demand can only be met by increasing the production of tradables; either to export to enable more purchases of imports and/or to sell to domestic consumers, reducing the demand for imports. If demand for tradables were to increase more than domestic supply, imports would increase, foreign exchange reserves fall

Figure 12: Contrast between African and Asian development strategies

Sub-Saharan Africa	Asian Tigers (a generation ago)
<ul style="list-style-type: none"> <li>• Overvalued exchange rate and high domestic cost structure</li> <li>• Weak public investment in infrastructure – low quality high cost impedes private investment in tradables</li> <li>• Weak, non-existent or perverse sector policies for agribusiness and manufacturing</li> <li>• No access to long term “patient” capital to kick start priority industries</li> </ul>	<ul style="list-style-type: none"> <li>• Maintain competitive exchange rate and domestic cost structure</li> <li>• Heavy public investment in affordable infrastructure to support private investment</li> <li>• Strong sector policy support for agribusiness and manufacturing</li> <li>• Ample long term low cost capital to kick start priority industries</li> </ul>

and the currency depreciate, causing an erosion of real incomes, depressing domestic demand and choking off growth. Since there is only limited scope to grow output of tradable service industries, investment in agribusiness and/or manufacturing is essential if growth of incomes is to be sustained.

It is also essential if there is to be an end to “jobless” growth; and creation of many more “decent” jobs to absorb the rapidly growing working age population. It is similarly essential for generating more rapid productivity improvement without which there can be no rapid sustainable growth of incomes.

***Stimulating higher rates of investment in agribusiness and manufacturing.*** If this is to be achieved, new policies would need to be adopted to improve the competitiveness of priority industries. Design of suitable policies could usefully draw on the successful experience of comparable developing countries in Asia; where a major focus was on support

for agribusiness infrastructure and agricultural credit and provision of long term “patient” funding to support manufacturing for export. However, such initiatives are not painless; often they require more fiscal resources in which case host governments would need to reduce public spending elsewhere in their budgets to maintain fiscal balance. There may be resistance to this but if rapid, sustainable growth is the goal, there is no alternative.

***What can donors do to help?*** Donors can support willing host governments by focusing resources to help them design and implement initiatives that target more private investment in these priority industries. These might include: supporting them to review and improve specific sector policies; adapting existing donor-funded infrastructure facilities to more directly support infrastructure-using agribusiness and manufacturing industries; and adapting and expanding existing “patient” capital facilities so as to reduce the risks and increase investment of private investors in these industries.

# CONCLUSIONS

The Africa Rising story misled. The external drivers generated a short-term consumer boom at the expense of causing a deterioration in the competitiveness and productive capacity of agribusiness and manufacturing. Reversing that trend is essential if sustainable, rapid and inclusive economic growth are to be achieved. If, in the current less favourable external environment, the economies in SSA are to start on the road towards this goal, they will have to implement pro-active development strategies that consistently and effectively support investment and growth of agribusiness and manufacturing for export – not just restore fiscal and external balance and “leave things to the market.”<sup>51</sup> The path to

sustainable, rapid growth will be different in each economy depending on, inter-alia, factor endowment and location but in every case a high rate of investment in agribusiness and/or manufacturing is an essential ingredient.

African leaders will only be willing to adopt very different policies if they fully appreciate the nature and magnitude of the chronic weaknesses inherited from the boom years and the crucial importance of refocusing actions and policies to strengthen the competitiveness of tradable industries, thereby providing the underpinning for rapid sustainable and inclusive growth.<sup>52</sup>

## Notes

- 1 See e.g. McKinsey Global Institute 2010 and The Economist Dec 3 2011.
- 2 Throughout the paper the terms “tradable” and “non-tradable” are used. “Tradables consist of ... exports and close substitutes of exports sold domestically ... and imports and domestically produced goods that are close substitutes of imports ... their domestic prices determined by world markets subject only to tariffs ... and the exchange rate”. “Non-tradables consist of all those goods and services the prices of which are determined by supply and demand domestically”. From Corden 1994 which contains a clear exposition of the key concepts underlying economic adjustment in small open economies.
- 3 See e.g. UNCTAD 2014 especially pp. 4-6.
- 4 South Africa is unique in SSA because it is a much larger and more mature economy with a productive commercial farming and agribusiness sector and a diversified industrial sector.
- 5 Among the 20 larger mainland countries in SSA 8 are major oil or hard mineral exporters, 7 have significant exports of oil or hard minerals and agricultural production and/or inflows of capital to finance exploration and development and just 5 are predominantly agricultural producers.
- 6 See ILO 2011 e.g. p. 97 “Consumption in Tanzania reflected changes in [consumer] prices more than changes in income... consumer durables became less expensive ... [and] showed large increases in ownership including radios, mosquito nets, watches..[and] mobile phones”.
- 7 See e.g. African Economic Outlook 2013, ch.2. Capital inflows to host governments from China were often linked to Chinese access to mineral resources and tied to imports of goods and services from China.
- 8 Strong growth of workers’ remittances from overseas were a fifth external driver but most of the remittances went to recipients in North Africa and South Africa; they were much lower in SSA and focused primarily on a few lower-middle income countries. See UNECA 2014 p. 21.
- 9 Essentially the only contribution of offshore oil production to gross national income is the fiscal revenue payable to the host government. For onshore oil production and hard mineral mining, slightly more domestic value added is generated from local procurement and payments to local staff e.g. in the copper industry in Zambia. In SSA as a whole more than 90% of the entire contribution to GNI from these industries came from fiscal revenues.
- 10 See e.g. Wikipedia “Corruption in Kenya.” [wikipedia.org/wiki/corruption\\_in\\_kenya](http://wikipedia.org/wiki/corruption_in_kenya) Also on Kenya, see e.g. Forbes December 1, 2015 “Corruption and tenderpreneurs bring Kenya’s economy to its knees” and on Malawi e.g. BBC World Africa “Cash gate – Malawi’s murky tale of shooting and corruption” [www.bbc.co.uk/news/world-africa-25912652](http://www.bbc.co.uk/news/world-africa-25912652).
- 11 See e.g. Wikipedia “Corruption in Nigeria,” Goodluck Jonathan Administration 2010-2015 [wikipedia.org/wiki/corruption\\_in\\_Nigeria](http://wikipedia.org/wiki/corruption_in_Nigeria) . For further evidence of diversion of State resources for personal gain see e.g. Birgis 2016.
- 12 This information was published in the New Africa Wealth report and cited in Africa Business October 2014.
- 13 The very high deductions levied on farmers by the State (marketing board levies, export taxes etc) in the 1990s were reduced after 2000 but remained at significant levels in many countries (e.g. FAO 2013(1) E.g. in Ghana the State marketing board, COCOBOD deducts 30% of the export price from small farmer cocoa growers (See FAO 2013(2)).
- 14 Ethiopia, Botswana and Rwanda were notable exceptions.
- 15 See Competitiveness report 2013.
- 16 See e.g. Africa Progress Report 2015 and IEA Africa Energy Outlook 2014.
- 17 See e.g. Africa Progress report 2015.
- 18 See e.g. World Bank 2010, Africa Progress Report 2015 and Africa Competitiveness Report 2013.
- 19 See Competitiveness report 2013.
- 20 Strong domestic demand for non-tradables increases their prices in local currency units and relative to the prices of tradables.
- 21 In many non-tradables industries in SSA including import/export/wholesale trade, transport services, agricultural processing and final stage production and packaging of imported intermediate inputs, there is limited competition as a result of a small number of dominant incumbents, significant structural barriers to entry (sunk capital costs and low marginal costs) and/or government policy-linked barriers e.g. constrained access to import licences. Consequently many incumbents have a degree of market power that enables them to adjust prices to maintain attractive rates of profit (See e.g. World Bank 2010 for evidence of market power and high profits in transport services in the region).
- 22 Indicators of maximum affordable income to rent or buy property show that for “ordinary” accommodation in major urban centres families would need to earn in excess of \$50,000 pa which is far beyond the reach of the vast majority of Africans.
- 23 According to the Dean of a major US business school in 2012 NGOs were the most favoured prospective employers of African graduates of its Masters programmes, apparently preferred in many cases to employment in private businesses.

- 24 There was also a “ripple” effect where middle management employment costs escalated as well, widening remuneration between the semi-skilled and unskilled workforce.
- 25 The Pew Research Centre in US reckoned just 6% of Africans qualified as middle class (earning \$10-20/day). EIU Canback reckoned 6.2% earned in the \$10-20/day range and just 2.3% qualified as upper middle class (\$20-50/day). Cited in *The Economist* Oct 24 2015.
- 26 The extractive industries were the exception to the rule because large resource rents were sufficient to pay the high infrastructure, input and labour costs, pay a high share of profits to the State and still leave high profits for the owners. The analysis here differs from the “Resource Curse” literature in that there are four external drivers and the mechanisms that gave rise to under-investment in tradables were not just mineral resource-induced changes in relative prices.
- 27 A notable exception was Kenya where privately financed agriculture-supporting infrastructure and experienced commercial farm management facilitated profitable export of vegetables and flowers into European markets. Other instances of profitable commercial farming include e.g. Zambia (wheat) and Mozambique and Malawi (sugar) all of which benefitted in one way or another from some form of protection.
- 28 See e.g. World Bank, 2008 and World Bank, 2013 (especially p. 29 and Table 4.1). Smallholders’ yields remained very low. Increases in physical output were largely the result of more people working more formerly-unused land. The modest increases in smallholders’ real incomes came not from productivity improvement but from (slightly) higher farm-gate prices and currency appreciation, both factors that depended on continuing favourable external drivers.
- 29 See e.g. Hazell 2011 ‘green revolutions do not just happen, but require considerable and sustained nurturing by the State’
- 30 Almost all agricultural development in SSA is early stage requiring extra costs such as acquiring land rights, preparing virgin land, providing infrastructure, testing crop mix, seed varieties and crop management practices and developing new markets. This takes years of trial and error during which time expected returns will be lower and risks higher than are acceptable to commercial investors. Side selling risk refers to the situation where smallholders receive inputs or credit from a buyer before planting based on a promise to sell the output to them post-harvest but then sell the output to a third party and fail to repay the in-kind or financial credit.
- 31 See e.g. Jayasuriya, S. on agricultural policy reforms in Asia and FAO 2012 on agricultural policies in SSA.
- 32 See e.g. DANIDA 2011/2.
- 33 See e.g. Kreuger 2015 who shows that 80% of the 36 countries signed up to the Maputo declaration (committing them to spend 10% of their budgets on agriculture) failed to comply with their undertakings.
- 34 See e.g. FAO 2011 and World Bank 2013. Note the modest increase in inter-African agricultural trade was generated indirectly by the commodity price boom as strong demand from government and the elite in mineral rich economies stimulated greater agricultural imports e.g. Zambia sales to DRC. The boost to regional agricultural trade may abate now that mineral prices have declined.
- 35 See Competitiveness report 2013.
- 36 See UNCTAD 2014 p.14.
- 37 Even in Tanzania, where there was significant growth of manufacturing for export, the underlying prospects for sustaining export growth were not promising (See Africa Growth Initiative 2014). In Ethiopia although there was some growth of manufactured exports especially shoes and textiles high non-labour costs and low productivity put it at a competitive disadvantage (see McKinsey 2012).
- 38 See e.g. UNCTAD 2014 and Rodrik (2015). Deindustrialisation of the textile industry and the failure to rebuild it was widely observed in e.g. Nigeria and Tanzania, see e.g. ILO 2012, p.65 and Birgis 2016.
- 39 Low labour productivity in manufacturing was in part a consequence of the low rate of investment (absence of learning by doing on the job) and in part the reason why investment in manufacturing was low (despite low wage rates low labour productivity of the inexperienced workforce deterred investment). Furthermore managing the inexperienced workforce required more experienced senior managers, the cost of which rose sharply as demand for senior managers in non-tradable industries increased, eroded further the profitability of these competitive industries.
- 40 See Gelb 2013.
- 41 See e.g. Bridges Africa 2012.
- 42 See e.g. World Bank trade and Competitiveness Global Practice 2015.
- 43 Smallholders had little to save and oil and mining companies remitted overseas all but small working balances. Domestic pension funds were required by their statutes to invest most of their funds overseas or in government bonds.
- 44 In contrast foreign direct investment in tradable industries other than to the extractive industries was extremely limited.
- 45 There were multiple challenges raising finance for early stage agribusinesses especially if sales were in domestic markets because borrowing in dollars exposed them to uncontrollable exchange rate risk and borrowing in local currency was very expensive (20-30% pa) rendering many such opportunities unviable. Similarly since many early stage manufacturing businesses were informal lacking the governance, compliance

and financial management standards and balance sheet strength required by lenders they, too, found accessing finance a struggle.

46 See McKinsey 2012.

47 See e.g. Studwell 2013.

48 See ILO 2011, ch. 4. Informal employment, whether as smallholders or in urban areas, exhibits low levels and slow growth of labour productivity. Productivity in government services cannot be measured but is generally regarded as exhibiting slow productivity improvement. These sectors together make up a very high share of total employment so it is not surprising that overall productivity improvement is low (see e.g. McKinsey Global Institute 2012). Slower productivity growth in agribusiness and manufacturing for export compared to rates achieved in Asia led to relative deterioration in competitiveness (see e.g. Corden 1994).

49 The increased volatility of exchange rates and the increased demand for credit from governments as budget deficits widened both contributed to the reduced availability and higher cost of capital.

50 See UNCTAD 2014 especially ch.3 where a similar case is made for selective support for priority industries.

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