II. The Great Sub-Saharan Africa Growth Takeoff: Lessons and Prospects

Overview

For the first time since the 1970s, a large number of countries in sub-Saharan Africa are enjoying high rates of per capita income growth. And growth episodes are showing some signs of unusual persistence. Sustaining and even accelerating high growth, and extending it to low-growth countries, is critical if the region is to achieve its overriding economic objectives: raising living standards and reaching the Millennium Development Goals (MDGs).

This chapter starts by characterizing the current growth takeoff: In what type of countries has growth accelerated? Is it all about natural resource extraction? To understand what is driving the acceleration—and thus what may be needed to keep it going and broaden it—the chapter then looks more closely at the high-growth countries. The discussion is organized around five themes: (i) initial income, endowments, and geography; (ii) conflict and extreme governance failures; (iii) the external environment, including terms of trade changes, FDI, and aid; (iv) macroeconomic policies; and (v) structural reforms. The extent to which growth in sub-Saharan Africa has benefited the poor is also discussed. Finally, an overview is provided of strategies and policies that can help sustain high growth.

The chapter does not attempt to present new statistical analyses of growth or even a comprehensive review of the vast literature. Rather, it draws on recent comprehensive studies, applying them to explain the current growth takeoff. It finds that

- *Sub-Saharan Africa has enjoyed a remarkable growth takeoff since the mid-1990s.* Average growth rates approach those of developing countries elsewhere, and current growth in the region is in some ways more persistent than in any previous postwar period. There is little evidence of an inescapable poverty trap. The fast growers are a diverse group, including resource-rich and landlocked countries and resource-poor countries that have not had large gains in their terms of trade.
- *Sustained growers in sub-Saharan Africa have gotten the critical basics right and avoided major policy failures.* Most of those that are getting ahead have achieved macroeconomic stability, including stable and low inflation and debt sustainability; pursued sound economic policies; and reinforced their institutions.
- *Recent African success stories also demonstrate that governments need to play a proactive role but that there is no simple recipe for achieving high growth.* Countries need to choose policies that allow them to benefit from what is happening externally, preserve macroeconomic stability, promote effective public and private investment, and ensure that all share in the benefits of growth, which must include improvements in health, education, and the other areas addressed by the MDGs as well as income. Moving toward growth trajectories that emphasize value added and nontraditional exports—paths that characterize most sustained fast growers in other regions—is not easy, but it can be done.
- *Higher aid has been part of the story for fast growers that have not benefited from large resource rents, providing room for higher social spending and public investment and promoting or at least being*

Note: This chapter was prepared by Andrew Berg, Paulo Drummond, and Chad Steinberg, with research assistance from Gustavo Ramirez, and editorial assistance from Emma Morgan.

consistent with fast growth. However, as the Commission on Growth and Development's recent *Growth Report* notes, fears that large increases in aid may also undermine exports are "difficult to prove, but difficult to dismiss" (p. 77). It is therefore important that the sectoral allocation of aid reflect country priorities, especially productivity-enhancing investments.

- *High growth cannot be taken for granted.* Previously, boom-bust cycles, exogenous shocks and conflicts, and the inability to channel resource wealth into sustainable growth and productive investments all worked to derail what were considered promising growth trajectories. The current period presents new challenges, as Chapter I makes clear, but stronger policies and fundamentals should allow countries to sustain growth. For example, higher levels of reserves should help sub-Saharan Africa oil importers absorb higher fuel prices, at least temporarily.

- *Growth in Sub-Saharan Africa has benefited the poor and reduced poverty.* On average the poor are seeing proportional rises in their incomes. Countries are making progress—though still not enough—toward achieving the other MDGs. Resource-rich countries need to make a special effort, however, to convert income gains into progress toward the MDGs.

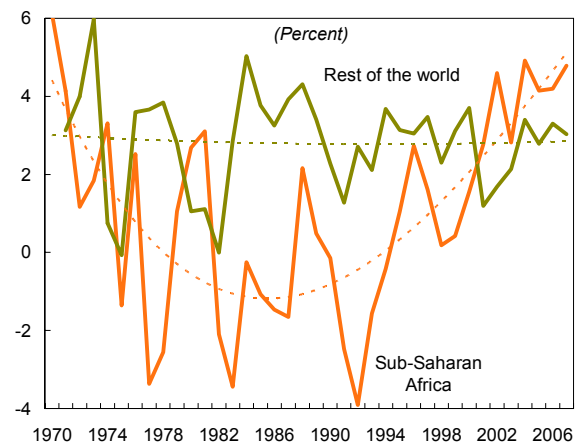
The Post-1995 Growth Takeoff

Economic growth in sub-Saharan Africa has increased markedly since the mid-1990s. For the region as a whole, real GDP grew at an average rate of 5 percent between 1995 and 2007, and real per capita GDP growth averaged about 2 percent over that same period. This is a remarkable turnaround from the 1980s and the first half of the 1990s.

The pickup in sub-Saharan African growth seems to be more than a side effect of higher world growth. Like that in the emerging markets discussed in the April 2008 *World Economic Outlook*, sub-Saharan African growth is not decoupled from world growth, because year-to-year movements are related to world growth (see Chapter 1), but it has *diverged* from world growth, in that the longer-term trend is now higher for Africa (Figure 2.1). In terms of per capita GDP growth, sub-Saharan Africa fell behind all other regions from 1985 through 1995 but is in about the middle in the recent higher-growth period (Figure 2.2).

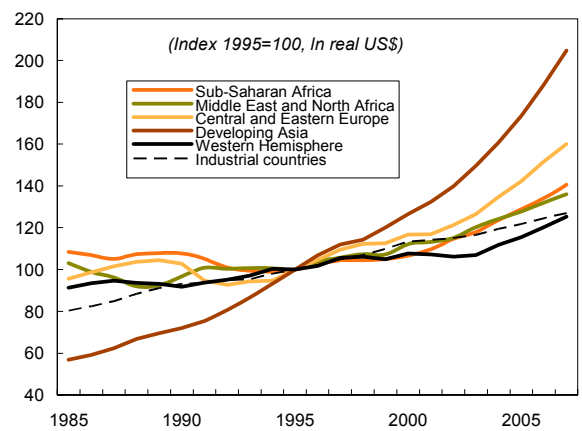
Perhaps most promising is the persistence of the recent accelerations. In every period, there have been some fast-growing countries in sub-Saharan Africa. However, in previous periods, the sub-

Figure 2.1. Sub-Saharan Africa: Diverging, but Not Necessarily Decoupled, from World Growth



Source: IMF, *World Economic Outlook*.

Figure 2.2. International Comparisons: GDP per Capita



Source: IMF, *World Economic Outlook*.

Saharan African countries that had enjoyed high growth for any particular five-year stretch tended to see very low growth in the subsequent five-year period. The fairly large set of fast growers as of 2000, however, saw solid growth in 2000–05. More strikingly—and in contrast to the experience in the late 1970s, when there was also a large group with high per capita growth—the following period (from 2005 on) has also seen sustained, indeed higher, growth. In Figure 2.3, each bubble represents countries that enjoyed per capita growth above 2¼ percent during the five-year period ending in the year shown in the bubble's label, with the size of the bubble representing the number of such countries. The vertical axis shows the growth rate in the five years preceding the label year, and the horizontal axis the growth rate for the same countries in the following five years. Fast growers since 1995 stand out as having very high average growth, and maintaining high growth in the subsequent period.

Another way to see whether something different—and more sustained—is happening is to observe the unprecedented number of countries enjoying significant and persistent increases in the rate of per capita income growth ("up-breaks") in the 1990s (Figure 2.4). "Significant" in this context means that the up-breaks are economically sizable (at least 2 percent of GDP) and also statistically important (larger than could be explained by the typical random variation in growth rates within countries). "Sustained" means the growth lasted at least five years. Meanwhile, down-breaks have become rare, so an unprecedented number of countries are enjoying unusually rapid growth.

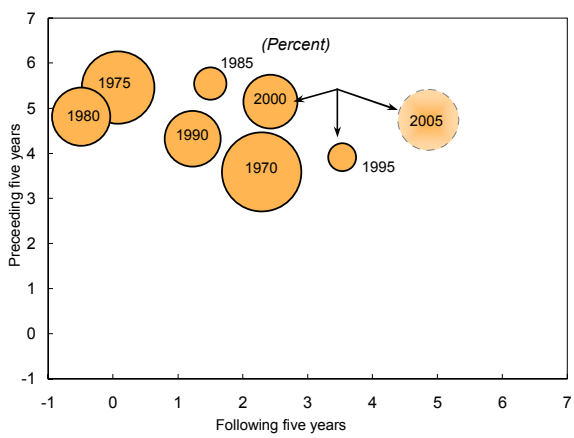
The increase in growth has been experienced by all subgroups of countries, despite the diversity of experiences (Figure 2.5). Growth levels have been highest and acceleration beyond the earlier period strongest in oil producers and resource-intensive countries, but growth and acceleration are also evident in non-oil and non-resource-intensive countries.

Sub-Saharan Africa's recent growth success raises a number of questions:

- What is driving the stronger performance in recent years?
- Is the per capita income growth also reducing poverty?
- What can policymakers do to sustain and accelerate growth?

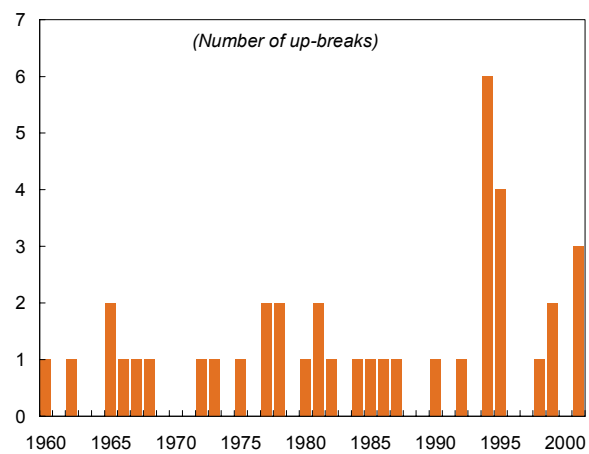
The rest of this chapter addresses these questions by drawing on recent successes in Africa and on findings in the extensive literature on growth.

Figure 2.3. Sub-Saharan Africa: GDP per Capita Growth, Five-Year Averages



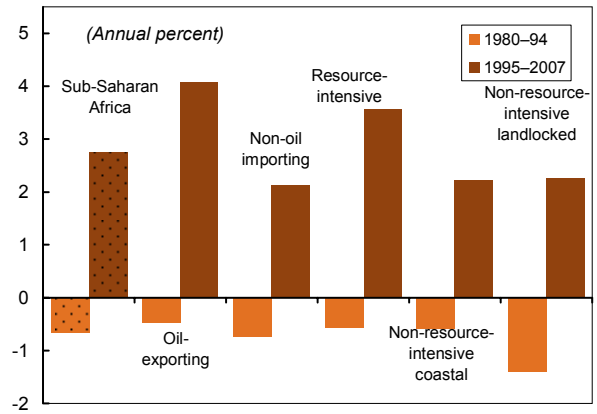
Note: Figure depicts countries with average annual per capita growth exceeding 2¼ percent in five-year periods from 1965 through 2004 (vertical axis), along with their average annual per capita growth in the subsequent five-year period (or four-year period, through the forecast growth for 2008, in the case of the 2005 bubble) (horizontal axis). Bubble size corresponds to the number of countries in each group. Equatorial Guinea is excluded from the bubbles from 1995 through 2005, as it had oil-related growth of 39.3 percent a year over 1995–99.

Figure 2.4. Frequency of Growth Up-Breaks in Sub-Saharan Africa



Source: Berg, Ostry, and Zettelmeyer (2008).

Figure 2.5. Sub-Saharan Africa: Real GDP per Capita Growth



Source: IMF, *World Economic Outlook*.

Learning from African Success Stories

The first step in learning from success is to identify the fast growers (Box 2.1, Table 2.1). Here, the cutoffs for growth in per capita income are essentially arbitrary: 2¼ percent and above for fast growers, and ½ percent or lower for a comparison group of slow growers. At 2¼ percent, income per person doubles in about 32 years. Fast and slow growers each account for about one-third of the 44 sub-Saharan African countries.

The next step is to review the experience of the fast growers, looking at how their economic characteristics evolved during and in some cases before their acceleration and at how they compare to the slow growers.[1] This section structures the discussion around some key economic features of countries around the world (see Box 2.2):

Table 2.1. Sub-Saharan Africa: Income Growth and Demographic Characteristics, 1995–2007

	Resource-Intensive[1]	Land-locked	Years of Acceleration[2]	Real per Capita GDP Growth	Real GDP Growth	PPP Real GDP per Capita (Constant 2000 dollars) 1995	PPP Real GDP per Capita (Constant 2000 dollars) 2007	GDP (Current US$, million) 2007	Population Growth	Population (Millions)
High-Growth				**5.2**	**8.2**	**1,890**	**3,785**	**37,382**	**2.6**	**26.3**
Angola	Y		1993	6.9	10.7	2,259	5,026	61,356	3.0	16.3
Botswana	Y	Y	1986, 1996	5.9	6.4	6,951	13,847	12,313	0.6	1.6
Burkina Faso		Y	1983, 1998	3.3	6.1	728	1,081	6,977	2.7	13.7
Cape Verde			1994, 2000	5.1	7.2	1,531	2,780	1,428	2.0	0.5
Chad	Y	Y	1981, 2001	3.9	6.9	883	1,401	7,095	3.1	9.5
Equatorial Guinea	Y		1995, 2001	26.6	36.1	792	13,412	10,485	5.4	1.2
Ethiopia		Y	1982, 1987	3.1	6.3	429	620	19,431	2.9	77.2
Ghana			1983	2.4	4.9	904	1,195	14,863	2.6	22.0
Mali		Y	…	2.5	4.9	646	874	6,745	2.4	13.1
Mauritius			1984	3.1	4.2	6,431	9,301	6,959	1.0	1.3
Mozambique			1985, 1990, 1995	6.7	8.4	338	731	7,559	2.1	20.3
Nigeria	Y		2000	4.0	6.4	1,100	1,766	166,778	2.8	143.9
Rwanda		Y	1994	2.5	10.0	609	816	3,320	5.4	9.4
São Tomé & Príncipe	Y		…	2.4	4.2	1,026	1,364	144	1.9	0.2
South Africa			1995	2.3	3.6	6,199	8,167	282,630	1.3	47.9
Tanzania			1994, 1999	3.4	5.6	724	1,079	16,184	2.3	39.0
Uganda		Y	1981, 1986	3.6	7.3	580	882	11,227	3.3	30.9
Medium-Growth[3]				**1.6**	**3.8**	**2,146**	**2,645**	**8,153**	**2.3**	**10.7**
p-values[4]				0.0	0.0	0.40	0.23	…	…	…
Low-Growth[3]				**-1.2**	**1.5**	**1,801**	**1,509**	**5,364**	**2.6**	**10.1**
p-values[4]				0.0	0.0	0.47	0.05	…	…	…
Sub-Saharan Africa Average				**2.1**	**4.8**	**1,941**	**2,724**	**18,559**	**2.5**	**16.6**

Sources: IMF, *World Economic Outlook*; and IMF, African Department database.

[1] Ndulu, O'Connell, and others (2007).

[2] Start date of accelerations since the 1980s.

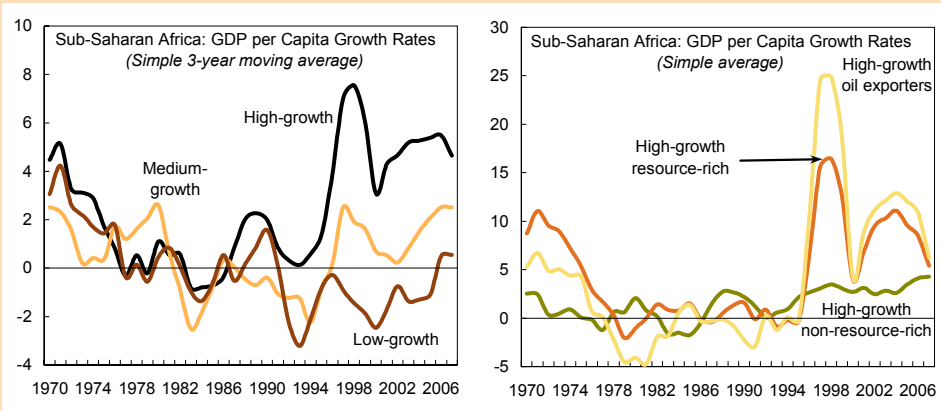
[3] Low-growth countries are listed in Box 2.1. Medium-growth countries are Benin, Cameroon, Gambia, Kenya, Lesotho, Madagascar, Malawi, Namibia, Niger, Senegal, Seychelles, Swaziland, and Zambia.

[4] The average growth for the group is statistically different from that for the high-growth group (based on a *p*-value from a *t*-test for the null hypothesis of no difference in means for the two groups). A low *p*-value means the null is rejected.

[1] The approach of this section was inspired partly by Gelb (2007).

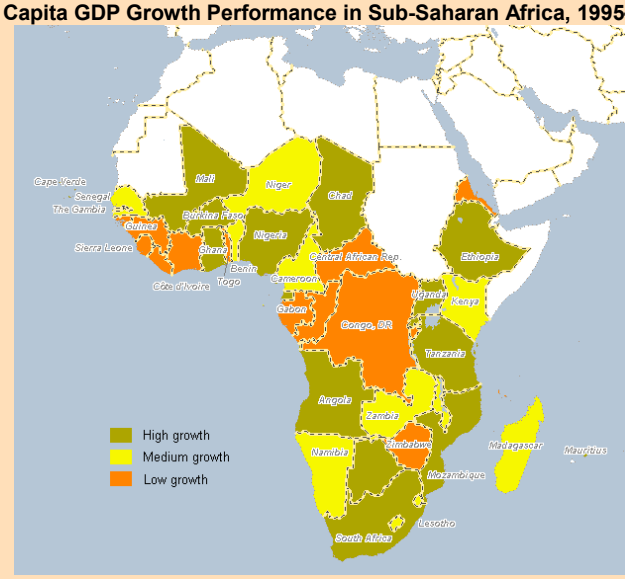
Box 2.1. Identifying High- and Low-Growth Countries

This section looks at the characteristics of recent African success stories and the experiences of the countries involved. This approach is not meant to establish causality or test theories, but to provide a better understanding of basic facts and patterns behind Africa's recent takeoff. For this purpose, countries classified as high growth had average annual real per capita GDP growth above 2¼ percent for 1995–2007.[1] The group consists of 17 countries: 4 oil exporters, 4 middle-income countries, and 9 low-income countries. Subgroups of particular interest are oil exporters, resource-rich countries, and other (Table 2.1 indicates which sub-Saharan African countries are high growth under the definition provided above).



Countries classified as low growth had average annual real per capita GDP growth of ½ percent or less in 1995–2007. The group consists of 14 countries: 2 oil exporters (Gabon and Republic of Congo) and 12 fragile countries (Burundi, the Central African Republic, Democratic Republic of Congo, the Comoros, Côte d'Ivoire, Eritrea, Guinea, Guinea-Bissau, Liberia, Sierra Leone, Togo, and Zimbabwe). Countries not otherwise classified are medium-growth countries.

Per Capita GDP Growth Performance in Sub-Saharan Africa, 1995–2007



Note: This box was prepared by Paulo Drummond.

[1]While it may seem somewhat arbitrary to pick a particular breakpoint for such a diverse continent, 1995 is the first year that for the region as a whole, after a hiatus of several years, per capita growth was positive. Also, up-breaks became far more frequent at around that time.

(i) *Initial endowments and geography*.

(ii) *Conflicts or extreme state failure*.

(iii) *The economic environment*, including terms of trade changes and growth in trading partners, FDI, and aid.

(iv) *The effects of macroeconomic policy* in such areas as inflation, fiscal policy and debt, exchange rate and trade, and foreign reserves.

(v) *Structural features subject to policy influence*, such as the quality of legal and economic institutions, governance, regulatory frameworks, education, social policy, physical infrastructure, and financial linkages.

Some caveats are in order. The aim of this analysis (following in the steps of the reports discussed in Box 2.2) is to explain patterns of recent successes and how they fit in with the broader literature, a primary goal being to learn from them how growth can be sustained. Clearly, the determinants of growth are also a function of the level of development. Relying on the broader literature, the following analysis does not attempt to identify cause and effect statistically. Nor is it a goal to use these cases to establish which growth theories are correct. In general, our hypothesis is that the most-interesting factors are those that are affected by policy. The analysis proceeds in terms of groups of factors influencing growth, but obviously policies and other factors interact in complicated ways, as is clear from some of the case studies presented in the chapter's boxes.

Box 2.2. Lessons from Recent Growth Studies

This chapter benefited greatly from five major recent studies that, together, review comprehensively the current state of knowledge about growth and its implications for Africa.

The ***Growth Report*** is the product of the **Commission on Growth and Development (2008)**, which consists of 19 leaders, mostly from developing countries, and 2 academics, Robert Solow and Michael Spence (chair). The report brings together the commissioners' views on what a successful growth strategy entails. The commission analyzes 13 economies that since 1950 have grown an average of at least 7 percent a year for 25 years or longer. Its emphasis was thus on sustained growth. Although most of the economies studied are in Asia, Botswana is included.

The African Economic Growth Project **(Ndulu, O'Connell, and others, 2007)**, referred to here as the **AEGP,** is a collaborative effort of the African Economic Research Consortium, Harvard University, and Oxford University to assess growth in postindependence sub-Saharan Africa. The final product, in two volumes, integrates African case studies with cross-country econometric evidence.

Ndulu, Chakraborti, and others (2007) is a World Bank "flagship report" that reviews the past half century of economic growth in Africa and distills that experience into a set of policy recommendations.

Arbache, Go, and Page (2008) reviews the recent acceleration of growth in Africa.

Finally, **Pattillo, Gupta, and Carey (2006)** reviews economic growth in sub-Saharan Africa through 2003, with a focus on the first part of the current growth acceleration.

These five studies help answer two broad questions relevant for sub-Saharan Africa:

Why has Africa grown so much more slowly than other regions? The AEGP reviews the cross-country evidence. Africa's colonial history and geography have left it with two features that have impaired growth: (i) an especially large proportion of population in landlocked resource-poor countries, and (ii) a large number of resource-rich countries, possibly subject to the "natural resource curse." However, performance is also

Box 2.2 *(concluded)*

strongly related to two sets of variables that are more subject to change, at least in the medium term: demography and policy. First, sub-Saharan Africa is the one continent still experiencing an explosion in population growth. While mortality rates—notwithstanding the impact of HIV/AIDS—have declined across the globe as a result of improvements in public health, fertility rates have remained broadly unchanged in sub-Saharan Africa (while declining elsewhere). This has resulted in an increasingly young African population with a high age-dependency ratio. Second, Africa's poor growth performance is strongly correlated with policy variables like inflation and government consumption. The AEGP finds that policy variables explain roughly half of the difference in performance.

What are the lessons for accelerating and sustaining growth? Increased sensitivity to the weaknesses of cross-country growth regressions—chiefly the difficulty in assigning causality from one variable to another—has led researchers in different directions in attempting to answer this question, including a greater focus on case studies. The studies discussed have thus supplemented cross-country statistical analysis with extensive country-specific analysis.

The first key lesson from these studies is that countries need to *avoid substantial policy errors*. At the same time, no single reform is likely to be sufficient to generate rapid growth in all countries. The lessons can be grouped into five categories. Countries need to

- *Engage the global economy at some level.* The global economy provides knowledge ("it is easier to learn something than it is to invent it"; Commission on Growth and Development, 2008, p. 22) and a large market for the goods that developing economies produce.
- *Avoid macroeconomic instability.* Complementary fiscal and monetary policy are needed to support macroeconomic stability, because persistently high and variable inflation impairs the ability of private sector actors to make appropriate investment decisions.
- *Adopt some form of market economy*. Countries can vary in the level of regulation, but they must recognize that market prices send important signals for resource allocation.
- *Conduct a responsible fiscal policy that does not borrow too much against the future*. Capable governments need to be farsighted in recognizing the "fundamental bargain between the present and future" (Commission on Growth and Development, 2008, p. 26). Likewise, governments need to avoid the temptation to redistribute wealth according to the ethnic or regional preferences of the ruling elite.
- *Avoid civil war.*

Surprisingly few sub-Saharan African economies have succeeded in avoiding all of these pitfalls since independence.

A second key lesson from these studies is that, besides avoiding major failures, *governments must have a critical proactive agenda*. Though the reports vary to some extent, there are common themes. As summarized in the *Growth Report*, for example, coherent growth strategies include a variety of policies that encourage the efficient allocation of capital and labor, such as providing adequate infrastructure and property rights, or securing an economic environment that leads to greater innovation. Policies that promote inclusion are also important, especially to ensure that reforms are sustainable. Putting such strategies in place requires a credible and committed government. All the reports provide a broad agenda and emphasize that the details must be country- and context-specific.

———————

Note: This box was prepared by Chad Steinberg.

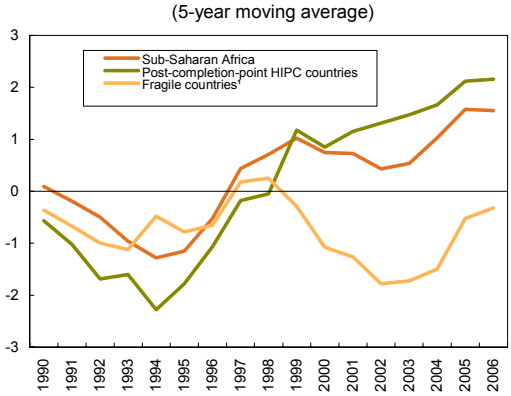
Much of the growth in current fast growers has been fueled by a significant increase in total factor productivity (TFP) (Box 2.3). This contrasts with the general experience in Africa up to 1995, which was characterized by low productivity growth in response to investment (Ndulu, Chakraborti, and others, 2007). Similarly, microeconomic evidence suggests historically low rates of return on investment in Africa (Ndulu, O'Connell, and others, 2007). Investment, both public and private, is clearly critical. Moreover, the sharp distinction between the contributions of TFP and factor accumulation is artificial, both because any measurement error in investment shows up as TFP and because productivity growth and investment are mutually related. Nevertheless, the importance of increases in TFP underscores the role of strong policies and reforms in growth accelerations in many sub-Saharan African countries.

Box 2.3. Productivity in Sub-Saharan Africa: Changes since the Mid-1990s

Growth-accounting analysis using data for 1985–2006 shows that

- Until the mid-1990s, growth in all country groups in the region was driven primarily by factor accumulation.
- For about the past 10 years, while factor accumulation has continued to be important to growth, even more important have been improvements in productivity (especially in high-growth countries and countries that have passed their completion point under the Heavily Indebted Poor Countries initiative).
- Both real GDP and TFP growth decelerated continuously over the period in fragile countries.

Sub-Saharan Africa: Productivity Growth, 1990–2006
(5-year moving average)



Source: IMF, staff calculations.
[1] Excluding post-completion-point HIPC countries (The Gambia, São Tomé and Príncipe, and Sierra Leone).

Sources of Growth in Sub-Saharan Africa: 1985–2006

	1985–89	1990–94	1995–99	2000–06
Sub-Saharan Africa				
Real GDP growth	3.5	1.7	4.4	4.2
Factor accumulation	3.2	3.0	3.3	3.0
TFP growth	0.3	–1.3	1.1	1.2
High-growth countries				
Real GDP growth	5.1	2.7	7.3	5.1
Factor accumulation	4.0	3.9	4.8	3.3
TFP growth	1.1	–1.2	2.5	1.8
Low-growth countries				
Real GDP growth	3.7	2.8	2.3	1.1
Factor accumulation	2.5	2.9	2.7	2.2
TFP growth	1.2	–0.1	–0.4	–1.1
Post-completion-point HIPC countries				
Real GDP growth	2.6	0.6	4.3	5.2
Factor accumulation	3.2	2.9	3.1	3.4
TFP growth	–0.6	–2.3	1.2	1.8
Fragile countries [1]				
Real GDP growth	2.3	1.7	1.7	0.8
Factor accumulation	2.4	2.2	2.0	1.6
TFP growth	–0.1	–0.5	–0.3	–0.8

Source: IMF, *World Economic Outlook;* and IMF, staff calculations.
[1] Excluding post-completion-point HIPC countries (The Gambia, São Tomé and Príncipe, and Sierra Leone).

Note: This box was prepared by Dhaneshwar Ghura, Bernardin Akitoby, and Priscilla Muthoora.

Initial income, endowments, and geography

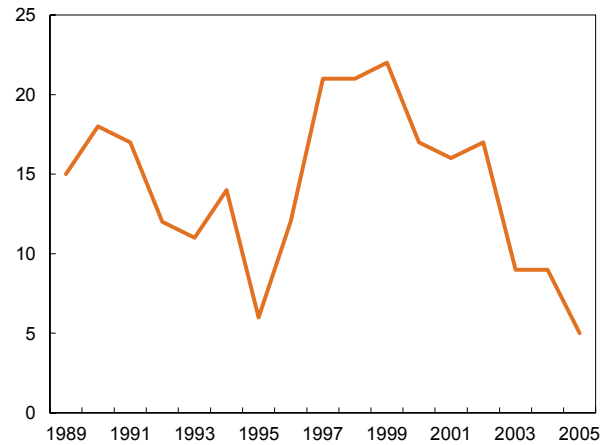
The current fast growers started from different income levels. They were not systematically poorer, as would be consistent with a catch-up phenomenon. But neither were they richer, as might be expected if escape from poverty traps were the main issue facing poor countries in the region.[2]

While geography and resource endowments have historically been important in determining growth patterns in Africa, in the past decade they have not been decisive in determining which countries were fast growers.[3] Of the 17 high-growth countries in sub-Saharan Africa (see Table 2.1), 6 are resource-rich, 6 are resource-scarce and coastal, and 5 are resource-scarce and landlocked (Burkina Faso, Ethiopia, Mali, Rwanda, and Uganda). And low growers are equally split among the resource-rich, resource-poor-coastal and resource-poor-landlocked groups. Thus, recent experience among fast growers in Africa would seem to suggest that growth opportunities based on geography and endowments alone cannot explain the accelerations and are not necessary conditions for fast growth. The fast-growing landlocked resource-poor countries in Africa managed to offset their location and resource disadvantages. However, this may be partly explained by improvements in neighboring countries: high-growth resource-rich and resource-poor coastal economies are increasingly pulling their landlocked neighbors along.[4]

Conflicts and extreme state failure

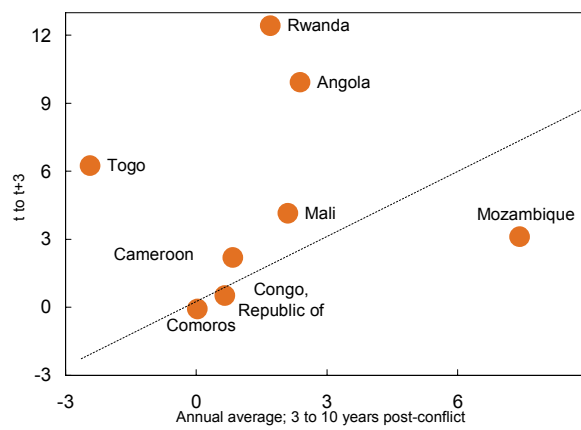
Over the past decade armed conflicts and state failure in the region have dwindled (Figure 2.6). And indeed, growth began in four of the current successes (Angola, Mali, Mozambique, and Rwanda) only when conflict ended (Figure 2.7).[5] (See Box 2.4 on Mozambique's growth after stabilization.) These four countries tended to see especially high growth in the first few years after the conflict ended, but as the growth was sustained, it became comparable to that in the nonconflict fast growers. However, four other countries where conflicts ended in the past 15 years were not able to sustain high growth (Figure 2.7), as several of these countries remained fragile states in the post-conflict period.

Figure 2.6. Number of Conflicts in Sub-Saharan Africa, 1989–2005



Source: Uppsala University, Uppsala Conflict Data Program.

Figure 2.7. Sub-Saharan Africa: GDP per Capita Growth Post-Conflict



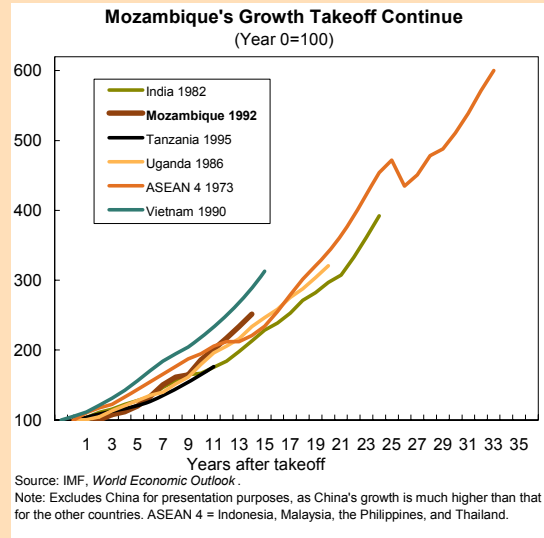
Source: IMF, *World Economic Outlook*.
Note: *t* is the year the conflict ended.

[2] On the role of poverty traps, see Sachs and others (2004), Kraay and Radaatz (2007), and World Bank and IMF (2005).
[3] This contrasts with the results of Ndulu, O'Connell, and others (2007), among others, in explaining overall growth in sub-Saharan Africa since independence.
[4] Collier (2007) among others emphasizes that growth in landlocked resource-poor countries depends especially strongly on the performance of the neighbors.
[5] See Collier (1999).

Box 2.4. Mozambique: Sustaining Growth after Stabilization

Since a peace agreement was signed in 1992, per capita GDP in Mozambique has grown almost without interruption, averaging 7.3 percent annually for the last 15 years. This prosperity has brought growth in virtually all sectors including agriculture, and a significant decline in the poverty headcount index (from 69 percent in 1997 to 54 percent in 2003).

Post-conflict growth has been founded on robust contributions from all principal growth drivers, as has been common where growth has been sustained in Southeast Asia (table; see also Jones, 2008). Solid human capital improvements have accompanied significant capital deepening (mostly from private investments) and TFP growth, which has been driven largely by better capacity utilization. Notably, the share associated with technological innovation and other changes is far superior to the African average.



Source: IMF, *World Economic Outlook* .
Note: Excludes China for presentation purposes, as China's growth is much higher than that for the other countries. ASEAN 4 = Indonesia, Malaysia, the Philippines, and Thailand.

Comparative Growth Accounting Evidence

		Output Growth Rates (Percent)				
			Growth Contributors			
				Capital		
		Growth	TFP	Physical	Human	Labor
1990–2000	Africa	2.3	–0.5	–0.1	0.4	2.5
1990–2000	East Asia	5.7	0.5	2.3	0.5	2.4
1990–2000	Latin America	3.3	0.4	0.2	0.3	2.4
1990–2000	South Asia	5.3	1.2	1.2	0.4	2.5
1992–1998	Mozambique	5.2	1.7	1.8	0.4	1.3
1999–2004	Mozambique	7.4	1.1	3.8	0.9	1.5

Sources: Bosworth and Collins (2003) for regions; and Jones (2008) for Mozambique.

Political stability, structural reforms, and prudent macroeconomic policies have helped sustain growth. From a highly regulated initial policy environment, steadfast implementation of first-generation reforms to liberalize trade, privatize public enterprises, and remove price and exchange rate controls have boosted foreign direct investment, particularly from South Africa, in sectors other than agriculture. Prudent economic policies and improvements in public financial management secured donor support for investment in education early on. Private investments and aid inflows have continued through second-generation reforms to consolidate macroeconomic stability, reduce the cost of doing business, and enhance governance. The result has been a structural shift toward more productive nonagricultural sectors, a decline in the agricultural labor force, widespread productivity gains and sustained growth.

Note: This box was prepared by Victor Lledó. See Clément and Peiris (2008) for a comprehensive discussion of Mozambique's growth experience, strategy, and lessons.

The low-growth group largely consists of conflict and post-conflict countries. Ndulu, O'Connell, and others (2007) identifies "state failure" as a policy syndrome that strongly lowers growth in sub-Saharan Africa countries when it is observed. It can also have regional implications for neighboring countries. Recent experience suggests that this syndrome is largely responsible for the worst growth performances in sub-Saharan Africa.

The external economic environment

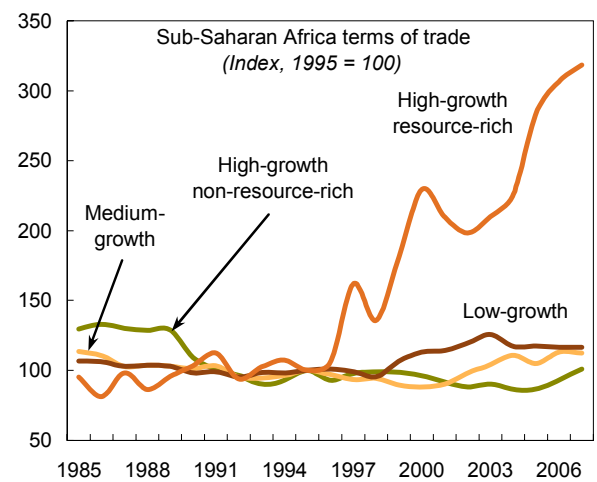
Pessimists about the sustainability of the current growth boom in sub-Saharan Africa may point out that the terms of trade have been exceptionally strong in recent years. The last period of high growth in sub-Saharan Africa, in the 1960s and early 1970s, also coincided with a terms of trade boom; unfortunately the boom ended in the 1980s and early 1990s with a terms of trade bust.[6] From the perspective of sustaining growth, the most-daunting results are that positive terms of trade shocks may have positive short-term effects on output but adverse ones in the longer term (Collier and Goderis, 2007). Similarly, positive terms of trade shocks are more strongly correlated with shorter-lived expansions than with sustained growth. This suggests that terms-of-trade-induced booms may be less likely to last (Hausmann, Pritchett, and Rodrik, 2004).

Fast growers have had a variety of experiences with their terms of trade: some countries, especially resource-rich countries, have benefited from trading gains; others have grown rapidly despite stable or declining terms of trade (Figure 2.8). At the same time, the terms of trade experiences of low-growth countries have also varied, with some growing slowly despite very large gains, while in others low growth has been associated with terms of trade losses. In sum, while terms of trade have been part of the growth acceleration in many countries, in others additional factors have had more of an effect on growth.

FDI may help sustain high growth but is not a prerequisite for the initiation of it. This can be seen from the fact that FDI inflows have risen substantially in resource-rich fast growers, but in general this has followed rather than coming before or with the takeoff (Figure 2.9). Still, the bulk of the cross-country evidence suggests that FDI (implemented with technological know-how) can be an important element in sustaining growth over longer periods.

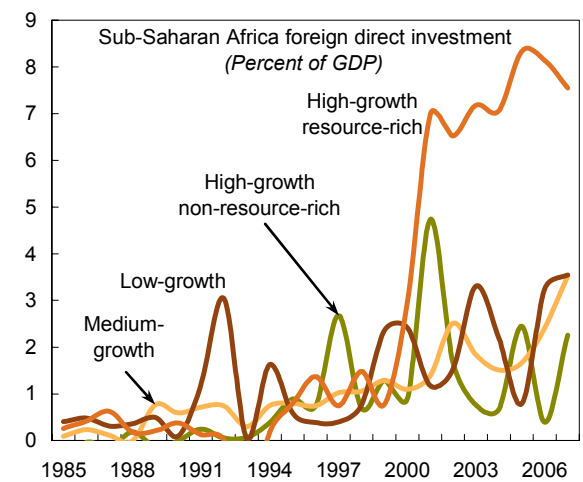
Aid to the region has grown sharply during the past decade. After collapsing when the cold war ended, aid to Africa has picked up since 2000, a period that roughly corresponds to the strongest period of growth in sub-Saharan Africa (Figure 2.10). The upturn in aid to sub-Saharan Africa is strongest for the high- and medium-growth groups, and decreases for the rest.

Figure 2.8. Terms of Trade Shocks



Source: IMF, *World Economic Outlook*.

Figure 2.9. Foreign Direct Investment

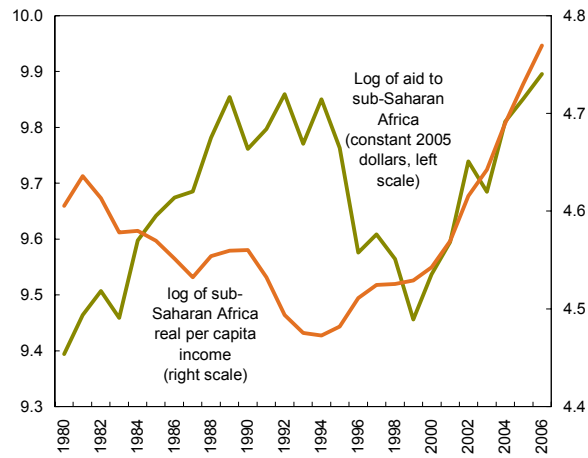


Source: IMF, *World Economic Outlook*.

[6] In general, the empirical importance of terms of trade shocks for Africa is disputed. Deaton (1999) finds them critical, whereas Ndulu, O'Connell, and others (2007) argue that their importance is "notoriously" hard to demonstrate.

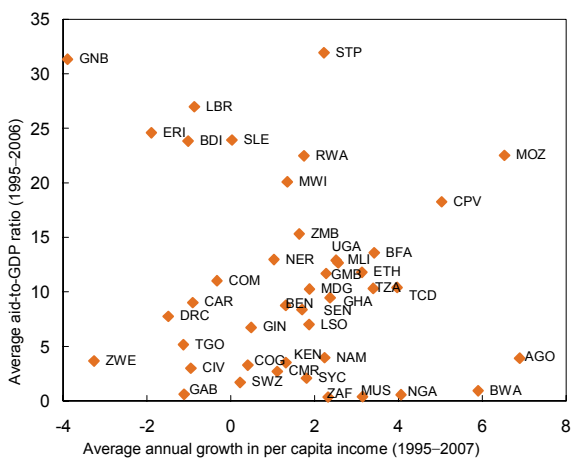
Increases in aid have been broadly associated with the current acceleration, but again there has been a diversity of experiences (Figure 2.11). The high-growth group includes recipients of both high and low amounts of aid. Within the high-aid group are a number of strong regional performers, including Mozambique, Cape Verde, and Burkina Faso; the low-aid recipients have tended to be resource-rich countries like Nigeria, Botswana, and Angola that have not faced a resource constraint. There is no clear evidence from the recent accelerations that aid prevents sustained growth. On the contrary, it can be a helpful mechanism for relieving resource constraints.

Figure 2.10. Aid to Sub-Saharan Africa



Sources: Roodman (2006); and IMF, staff calculations.

Figure 2.11. Aid and Growth in Sub-Saharan Africa



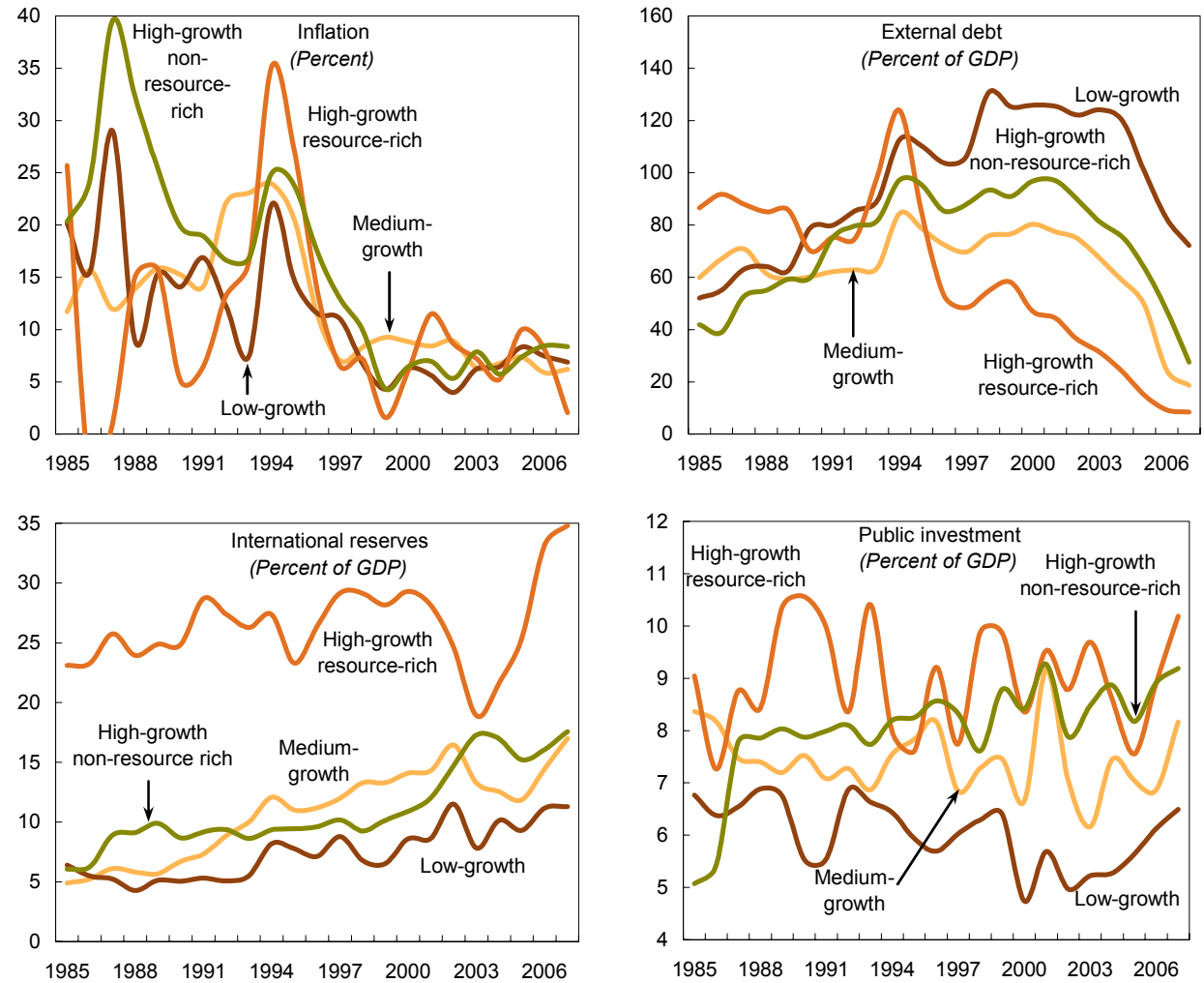
Sources: Roodman (2006); and IMF, staff calculations.
Note: Country names are abbreviated according to the ISO Alpha-3 standard codes.

Macroeconomic policies

Improved macroeconomic policies are characteristic of the current sustained growers (Figure 2.12):

- *Inflation has decreased significantly from very high levels in recent years*, in both the fast growers and other groups, partly as a result of improved macroeconomic policies. The decline in inflation roughly coincides with the start of the high-growth period. That high-growth countries have kept inflation fairly low is consistent with the broader literature, which finds that countries with lower inflation are generally more likely to sustain high-growth episodes (Berg, Ostry, and Zettelmeyer, 2008). On the other hand, the failure of low inflation to trigger growth in countries in the other groups is consistent with the established notion that low inflation alone is not a sufficient condition for higher growth.
- *A firm fiscal policy reveals itself in several dimensions in the fast growers.* Debt has decreased in all groups since about 2001, reflecting both Heavily Indebted Poor Countries (HIPC) Initiative and Multilateral Debt Relief Initiative (MDRI) debt relief and restrained deficits (after grants). Strong public investment within an overall envelope of fiscal responsibility has helped fast growers develop much-needed infrastructure. Box 2.5 uses the case of Tanzania to illustrate growth supported by economic stabilization.
- *Vulnerabilities have been reduced*, notably through substantial accumulation of foreign reserves and lower debt levels. This illustrates a more general point: although sub-Saharan African countries remain susceptible to terms of trade shocks, better fundamentals have improved their ability to weather the storm (the current shock notwithstanding).

Figure 2.12. Macroeconomic Indicators



Source: IMF, African Department database.
Note: Inflation figures exclude Angola, the Democratic Republic of Congo, and Zimbabwe, which experienced hyperinflation in the period.

Fast growers in Africa tend to have more flexible exchange rate regimes: 5 of the 17 fast-growing countries have a hard peg. This may be because exchange rate flexibility helps them avoid overvaluation and adjust to shocks. The literature on this issue is mixed, finding little clear relationship between the exchange rate regime and growth in developing countries generally (Rogoff and others, 2004) and in Africa specifically (Masson and Pattillo, 2005).

Related to—but distinct from—the exchange rate regime itself is the degree of overvaluation of the real exchange rate. High-growth non-resource-rich countries have observed a weakening real exchange rate throughout the high-growth period (see Figure 2.13), such that they have been undervalued relative to countries in the other groups—and valued in a way roughly comparable to the average developing country—since 2000 or so.[7] Resource-rich countries, not surprisingly, have seen a real appreciation in recent years, reflecting strong terms of trade and natural resource discoveries.

[7] This is broadly consistent with the evidence in Rodrik (2007) to the effect that exchange rate undervaluation—measured as in Figure 2.13—is related to faster growth.

Box 2.5. Tanzania's Growth Experience

Tanzania's economic growth has accelerated significantly in recent years. Real GDP growth picked up in the mid-1990s, as stabilization was cemented and structural reforms started to show effects. It continued to accelerate into the new century, averaging about 7 percent a year for 2001–07—more than double the average of the 1980s and 1990s. As a result, per capita income has almost doubled since 1995 and poverty has declined. Key reforms included opening up the economy to trade and investment, promoting the development of an efficient private financial sector, and placing public finances on a sound financial footing. When reforms reached a critical mass, they stimulated a virtuous circle of higher private investment, economic growth, and development partner support. But although higher aid flows and FDI have both contributed to a significant increase in capital accumulation, the recent growth acceleration is largely due to sustained improvements in TFP resulting from the success of the reforms.

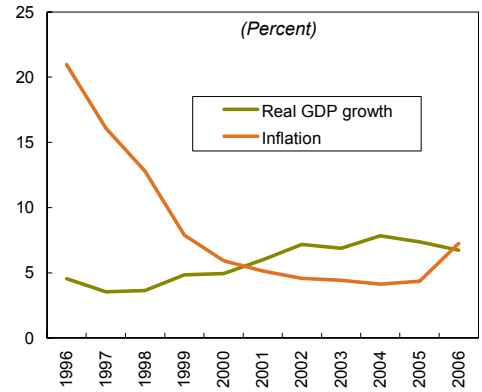
The IMF supported these reforms through concessional lending, debt relief, technical assistance, and policy advice, but country ownership made them durable. Tanzania's is a truly homegrown development strategy produced by a participatory process, involving civil society, and documented in the country's second-generation Poverty Reduction Strategy Paper, the MKUKUTA, which adopts an outcome-based approach focusing on growth and reduction of poverty, enhanced quality of life and social well-being, and good governance and accountability.

Tanzania: Contributions to Real GDP Growth
(percent)

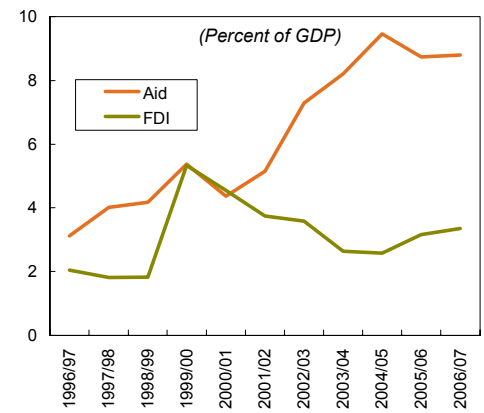
	1986–90	1991–95	1996–2000	2001–06	2007
Real GDP growth	5.3	1.8	4.3	7.0	7.3
Labor force	2.2	2.5	1.7	1.7	1.8
Capital	0.9	1.3	0.3	1.6	2.3
Total factor productivity	2.2	–2.0	2.3	3.7	3.2

Source: IMF staff calculations.

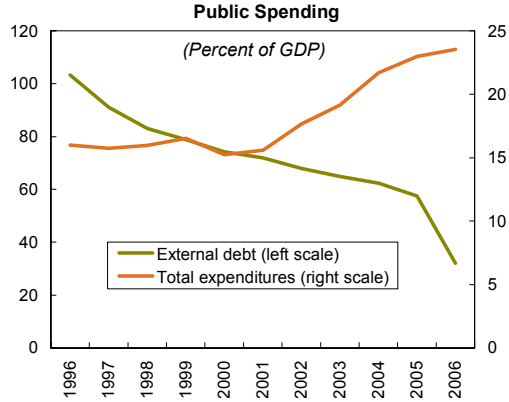
Macroeconomic Stability: GDP and Inflation



Capital Inflows: Aid and FDI



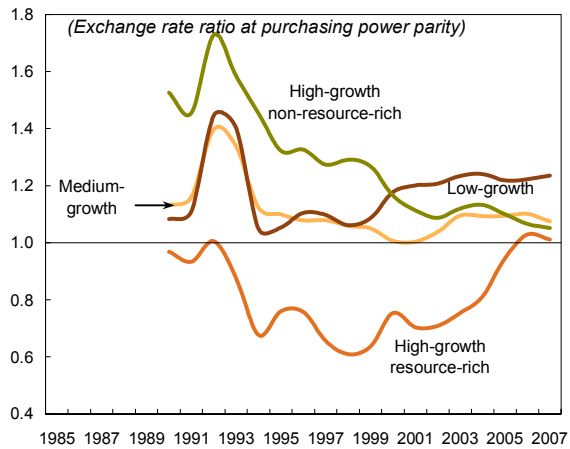
Fiscal Effectiveness: Debt Reduction and Public Spending



Sources: Tanzanian authorities; IMF, *World Economic Outlook;* and IMF, staff estimates.

Note: This box was prepared by Yuri Sobolev and is based on the forthcoming IMF study *Tanzania—The Story of an African Transition.*

Figure 2.13. Measuring Overvaluation: Exchange Rate Overvaluation

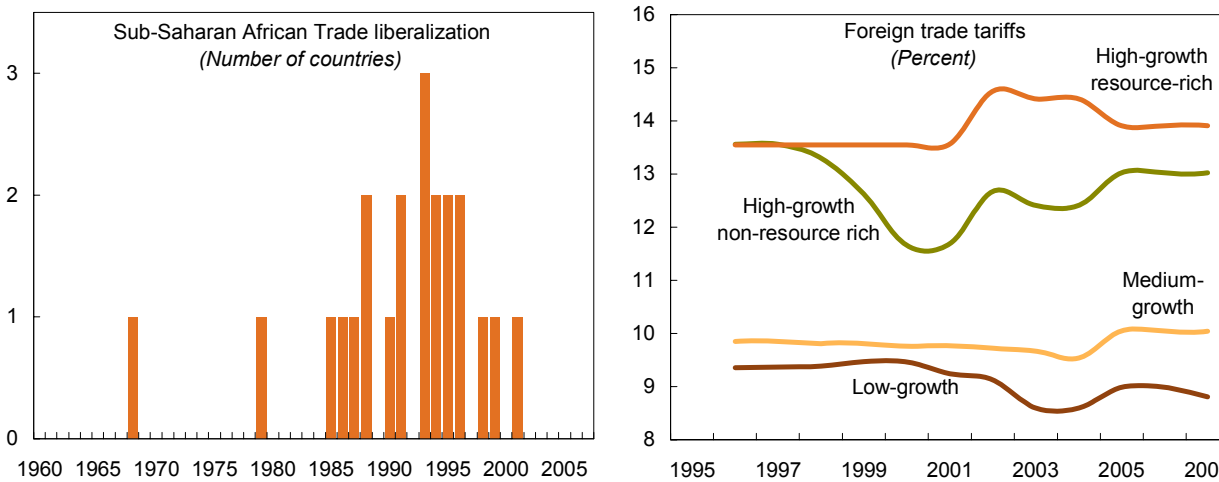


Sources: IMF, *World Economic Outlook*; and IMF, staff calculations.
Note: Ratio between the nominal exchange rate and the purchasing power parity exchange rate

With respect to trade policy, the most salient feature is the general and widespread liberalization of trade regimes that took place in the 1990s, coinciding with the overall growth takeoff (see Figure 2.14).[8] This liberalization did not accelerate growth in the slow growers, underscoring the fact that no single reform is likely to be sufficient to generate rapid growth in all countries if other conditions, such as adequate infrastructure, are not in place. The takeoff was also associated with some reduction in foreign trade tariffs in non-resource-rich countries.

Fast growers have generally had rapid growth of exports and imports, but experiences diverge for resource-intensive and non-resource-intensive countries (Figure 2.15). The region's non-resource-intensive countries have, in general, seen only limited increases in diversification and growth of manufactured exports. Only in a handful of fast growers (Botswana, Cape Verde, Mauritius, Namibia, and South Africa) is the share of manufacturing exports in total exports in the double digits (note that the data are unusually spotty here).

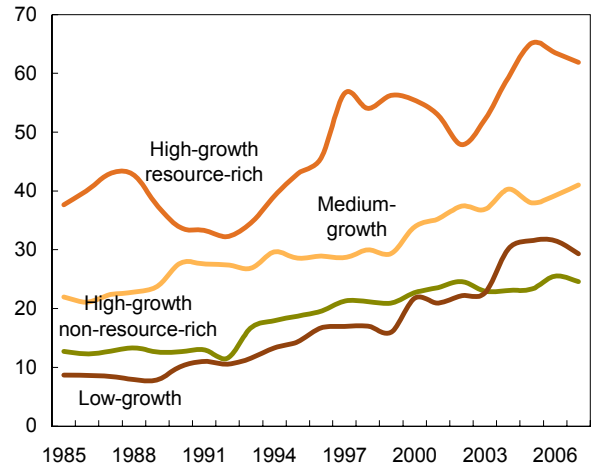
Figure 2.14. Openness and Trade Policy



Sources: Wacziarg and Welch (2008); and UNCTAD.
Note: Six of the region's high growers liberalized trade during the 1990s.

[8] The tariff level is still relatively high in sub-Saharan Africa on average. On recent trade performance in Africa, see Carey, Gupta, and Jacoby (2007). Data on trade liberalization are based on the updated data set of trade policy indicators and liberalization dates in Wacziarg and Welch (2008).

Figure 2.15. Exports of Goods and Services as a Percentage of GDP



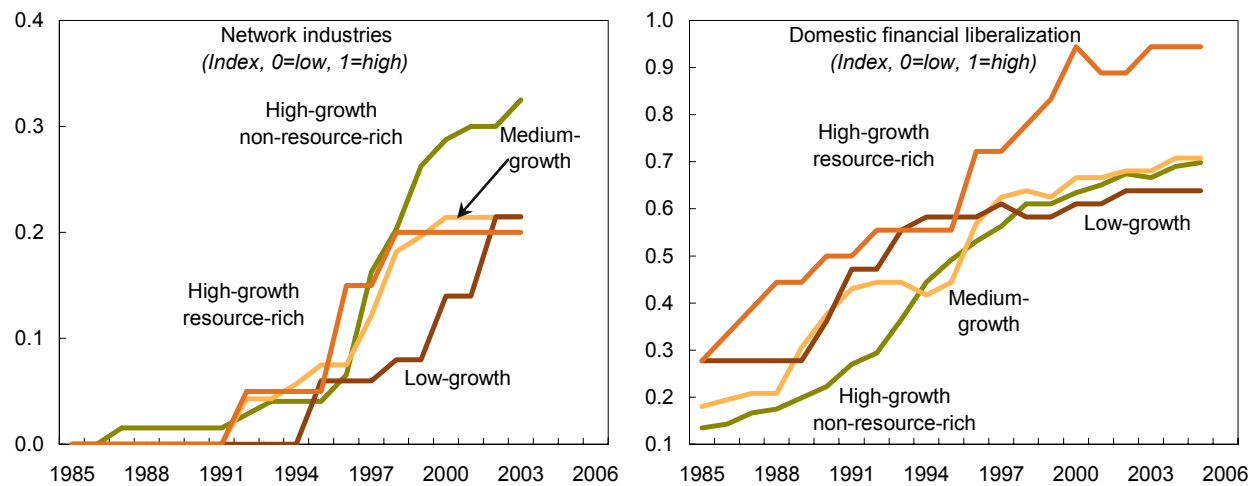
Source: IMF, *World Economic Outlook*; and IMF, staff calculations.

This relatively slow pace of growth of manufactured exports and, more generally, diversification of exports away from primary commodities contrasts with the experience of most sustained fast growers in other regions, as emphasized in Johnson, Ostry, and Subramanian (2007). The microeconomic evidence is that, at least as much as in other regions, exporting firms in sub-Saharan Africa enjoy greater productivity growth (Mengistae and Pattillo, 2004). Thus, it is a source of concern that African countries have not in general followed the path of other fast-growing developing countries in both raising productivity in agriculture and restructuring the economy toward services and more-diversified exports (Ndulu, Chakraborti, and others, 2007). Box 2.6 illustrates some of these points using the case of Uganda, one of Africa's sustained fast growers.

Structural and institutional reforms

The fast growers, like most African countries, emerged from the period of structural adjustment in the 1980s and early 1990s with a near-absence of what Ndulu, O'Connell, and others (2007) refer to as the regulatory syndrome of pervasive and deep state controls that often characterized sub-Saharan African economies in earlier periods. The progress achieved in the structural adjustment period is illustrated by liberalization of telecommunication and electricity industries and domestic financial liberalization (Figure 2.16). That this progress did not lead to a growth acceleration in all countries again demonstrates that there is no simple recipe for success. However, the evidence is broadly consistent with the notion that such basic reforms are close to being a necessary condition.

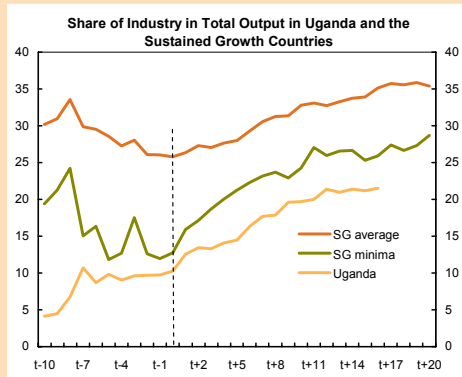
Figure 2.16. Sub-Saharan Africa: Network Industries and Domestic Financial Liberalization

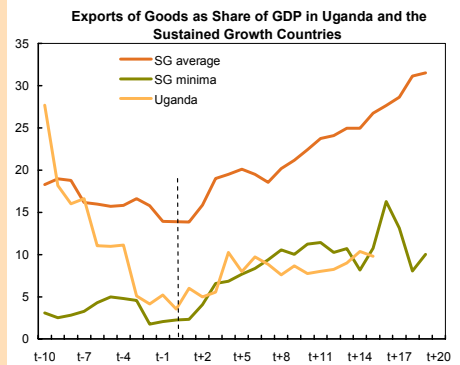


Source: IMF (2008).

Box 2.6. Growth and Structural Transformation in Uganda

It is useful to think about three overlapping development challenges for African countries: *getting growth started, sustaining growth,* and *effecting economic transformation*. Uganda has done well on the first two counts: the economy is now in its 20th year of uninterrupted expansion. But there is concern among policymakers that despite macroeconomic stability and reasonably well-functioning markets, the country's economy has not significantly transitioned from subsistence agriculture to higher-productivity activities. One way to ascertain whether this is the case is to compare the evolution of correlates of economic transformation (industrialization, financial deepening, etc.) in Uganda with their evolution in the small group of sustained-growth (SG) countries that have registered high rates of economic growth and engendered significant transformation over the last few decades. A forthcoming IMF study does just that.





Source: Uganda Bureau of Statistics and staff estimates.

The study finds that there has been significant economic transformation in this group of countries over the last 20 years, but from a lower base and at a slower pace in Uganda. Thus, for example, though industrialization in Uganda (top figure) has increased markedly, it is only some 15 years into the country's growth episode that this aggregate approaches the level observed in the SG countries at the start of their growth episodes.[1]

Another finding is the generally weak performance of Uganda's tradables sector relative to those of the SG countries. Direct measures of competitiveness do not point to significant problems (at least currently). But outcome variables—the ultimate test—show the trade and current account deficits to be much wider now than at the start of Uganda's growth episode. In part, this reflects the poor performance of the exports sector over the years (bottom figure), although that has improved recently.

Uganda's achievements over the last 20 or so years, considering weak fundamentals and significant shocks, are quite remarkable. If industrialization there has not been as substantial as in the SG countries, there is no single cause for this. There are hardware-type constraints on economic transformation, including limited human capital and weak infrastructure, but there are also software-type problems in terms of the quality of institutions, governance, regulation, and so on, which could all be better. Given limited capacity to address all these shortcomings, future government interventions should be carefully focused. The forthcoming working paper on which this box is based (see Note) identifies three such first-order interventions: improving infrastructure services, developing a focused growth strategy, and enhancing export competitiveness.

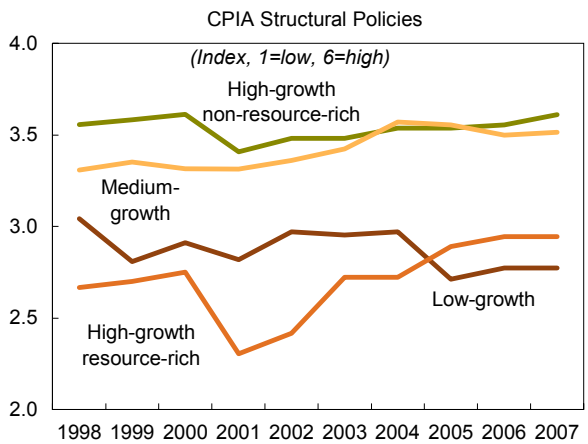
Note: Prepared by Abebe Aemro Selassie, drawing on a forthcoming IMF Working Paper "Beyond Macroeconomic Stability: The Quest for Industrialization in Uganda."

[1]The sustained growth countries are those identified in Johnson, Ostry, and Subramanian (2007): Chile, China, the Dominican Republic, Egypt, Indonesia, Republic of Korea, Malaysia, Singapore, Taiwan Province of China, Thailand, Tunisia, and Vietnam.

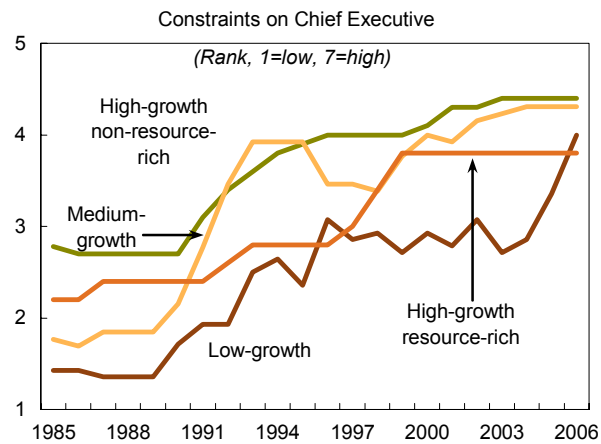
The fast growers—at least the non-resource-rich—by some measures have had relatively good structural policies in place at least since the late 1990s. This factor is difficult to quantify. However, the World Bank's Country Policy and Institutional Assessment (CPIA) attempts to measure the quality of policies and institutions along four dimensions: (i) economic management, (ii) structural policies, (iii) policies for social inclusion and equity, and (iv) public sector management and institutions. On all these measures, the fast growers have done better. The notable exception is resource-rich countries: even fast-growing resource-rich countries measure relatively poorly on all four dimensions. A similar picture emerges from a measure, from the Polity IV database, of the constraint on the executive, which assesses the de facto operational independence of a country's chief executive (Figure 2.17 illustrates for CPIA structural policies and constraints on the executive).[9]

However, on many broader measures of perceptions of institutional quality, sub-Saharan African fast growers did not look particularly good when their takeoffs began. This is consistent with Johnson, Ostry, and Subramanian (2007), which emphasizes that sustained fast growers in Asia and elsewhere started with institutions comparable to those of many African countries today. In some cases there has been improvement during the high-growth period, particularly in terms of democratic accountability (Figure 2.18). However, by other measures of institutional quality related to economic performance such as quality of the bureaucracy or property rights (the latter not shown in the figure), there has been no clear general pattern of improvement. The wealth of evidence from the literature suggests that strong institutions and governance lead to higher incomes and growth, although causality runs in both directions. It suggests also that fast growth may provide opportunities to improve institutions and governance, and that doing so may help sustain high growth. However, such improvements are clearly not automatic with faster growth.

Figure 2.17. CPIA Structural Policies and Constraints on Chief Executive



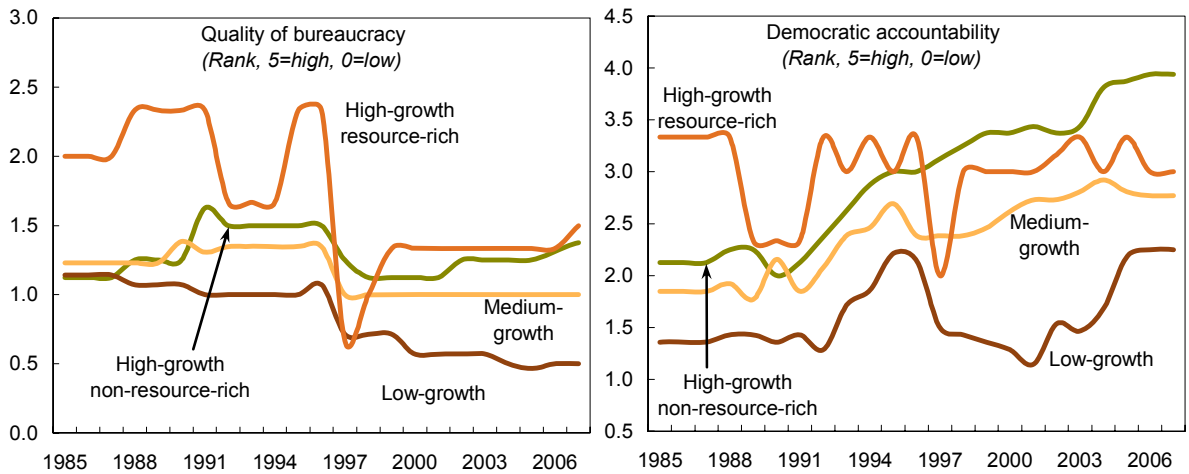
Source: World Bank IDA Resource Allocation Index.



Source: Center for Systemic Peace, Polity IV data set.

[9] This measure is widely used in cross-country and panel growth regressions, such as those in Acemoglu, Johnson, and Robinson (2001).

Figure 2.18. Institutions/Governance

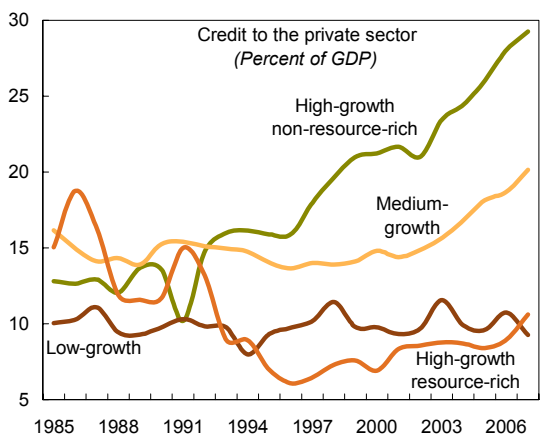


Source: *International Country Risk Guide*.

The high-growth countries in sub-Saharan Africa have mobilized savings and allocated capital better than countries in the other groups (Figure 2.19). Financial market access and financial sector reforms have had significant impact on per capita income growth in several of these countries (IMF, 2008).

With financial sector development and the other reforms discussed above, fast-growing economies have generally better total and private investment rates than medium- or low-growth countries (Figure 2.20). The ratio of private investment to GDP for sub-Saharan Africa on average has been rising in recent years; for fast growers, it is approaching that of other developing countries. Generally, however, sub-Saharan African countries have relatively low savings—partly because financial services are still weak—so a critical question is whether the resource constraint is holding back investment. In several high-growth countries (Burkina Faso, Mozambique, Tanzania, Uganda), foreign savings are relatively high, suggesting a relaxation of that constraint, allowing investment rates to pick up.

Figure 2.19. Financial Linkages



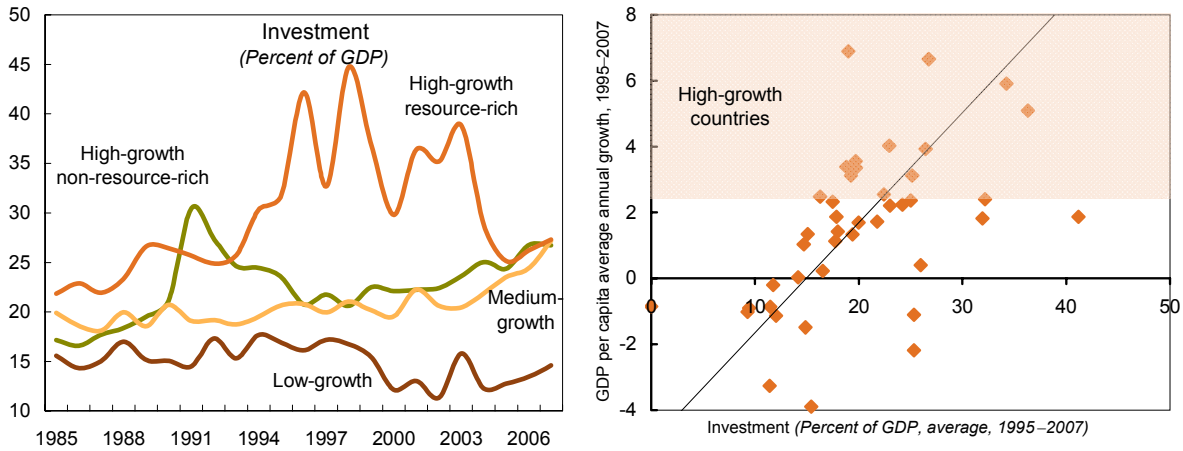
Source: IMF, *International Financial Statistics*; and IMF, staff calculations.

Putting it together

The growth takeoff in sub-Saharan Africa since 1995 has been associated with several factors, and no simple story emerges. However, the evidence suggests four broad conclusions:

- Several conditions sometimes considered critical to achieving sustained growth, such as direct access to the sea or high levels of economic institutions, have not been required in recent years for a country in sub-Saharan Africa to begin a period of sustained growth.

Figure 2.20. Total Investment and Growth
Sub-Saharan Africa: Average per Capita Growth Rates in Investment



Source: IMF, *World Economic Outlook*; and IMF, staff calculations.

- There are, however, a number of conditions that are apparently necessary for sustained takeoff: absence of conflict; a stable macroeconomy, as reflected in low inflation and sustainable debt; and a functioning market economy. Reflecting these basic conditions, fast growth in the region has generally followed a period of structural adjustment that reduced state controls and liberalized trade and domestic financial markets.

- A clear set of sufficient conditions for rapid growth does not emerge. The fast growers have on the whole done better in the areas of building reserves, sustaining high levels of public investment, and avoiding overvaluation of the real exchange rate, and on some measures of broad policy reform, notably the World Bank's CPIA (the latter two hold true mainly for non-resource-rich fast growers). However, these patterns are not stark. In general, growth seems to have responded to the specific circumstances in each country in terms of the external environment it faced and the policy choices it made.

- In many countries, fast growth has been associated with a more favorable external economic environment, including improvements in terms of trade, rising aid inflows, and rapid growth of exports. But several countries have grown fast despite stable or declining terms of trade or low levels of aid. The cases highlighted here, and in the literature, suggest the need for a flexible and country-specific strategy and a proactive state working to spur growth and ensure that its benefits are spread widely.

Growth, Income Inequality, and Poverty In Sub-Saharan Africa

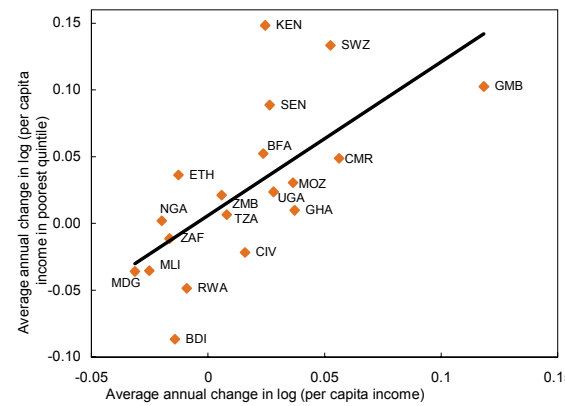
In 2004 sub-Saharan Africa had the worst incidence of extreme poverty in the world, as growth in China and India has dramatically reduced poverty elsewhere. Sub-Saharan Africa had been ahead of East and South Asia, in regard to poverty, in 1980; it has now fallen behind. However, it appears that sub-Saharan Africa's within-country income inequality has declined over the past two decades (IMF, 2003), in contrast to that in most other regions of the world. This would suggest that poor growth, not a worsening of the income distribution, is behind sub-Saharan Africa's difficulties in reducing poverty.

The recent growth in Sub-Saharan Africa, however, has helped reduce poverty in the region. The best way to examine the impact of growth on poverty would be to look at what happens to real incomes and poverty during the intervals between comprehensive household surveys. Unfortunately, such surveys are too rare for it to be possible to look at fast growers as a group or to compare them to other groups. Instead, Figure 2.21 plots the average annual growth of income received by the poorest 20 percent of the population (on the vertical axis) against the average annual growth in *average* per capita incomes (on the horizontal axis), for all available pairs of household surveys in a given country that span 1995.[10] In a country with a more even income distribution, the poor will receive more of the total income, including the increment resulting from the recent growth. But as the figure shows, incomes of the poor tend to rise equiproportionately with average incomes.

The economic upturn in sub-Saharan Africa has thus reduced the fraction of the population that lives below a fixed poverty line. Figure 2.22 suggests that per capita growth of 1 percent of GDP in the region is associated with a 0.5 percentage point fall in the US$1 a day poverty rate.[11]

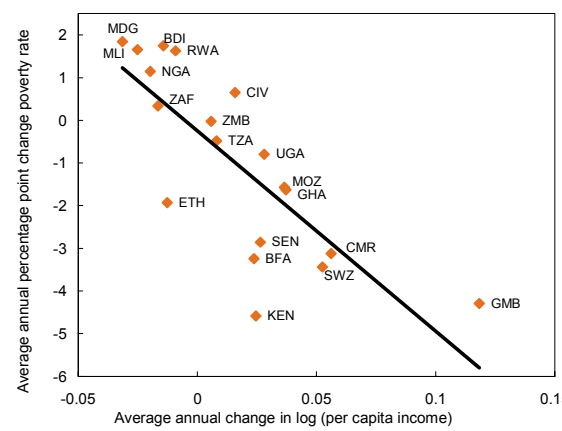
Over longer periods, the role of growth in poverty reduction tends to become clearer. Poverty reduction is like a marathon, rather than a sprint: it takes sustained effort over many years to achieve large and lasting gains. And it is only over these longer periods that the cumulative effect of average per capita income growth makes itself most clearly felt. Figure 2.23 shows that for periods of less than five years, much of the variation in the income of the poor is correlated with changes in the distribution of income, not changes in average income. Distributional changes can have large effects on poverty (as has been evident during the current food price shock). But over longer periods, the distributional changes tend to average out, and the effect of average growth on the income of the poor more clearly dominates.

Figure 2.21. Growth Rates



Source: Chen and Ravallion (2007); and IMF, staff calculations.
Note: Country names are abbreviated according to the ISO Alpha-3 standard codes.

Figure 2.22. Poverty Reduction

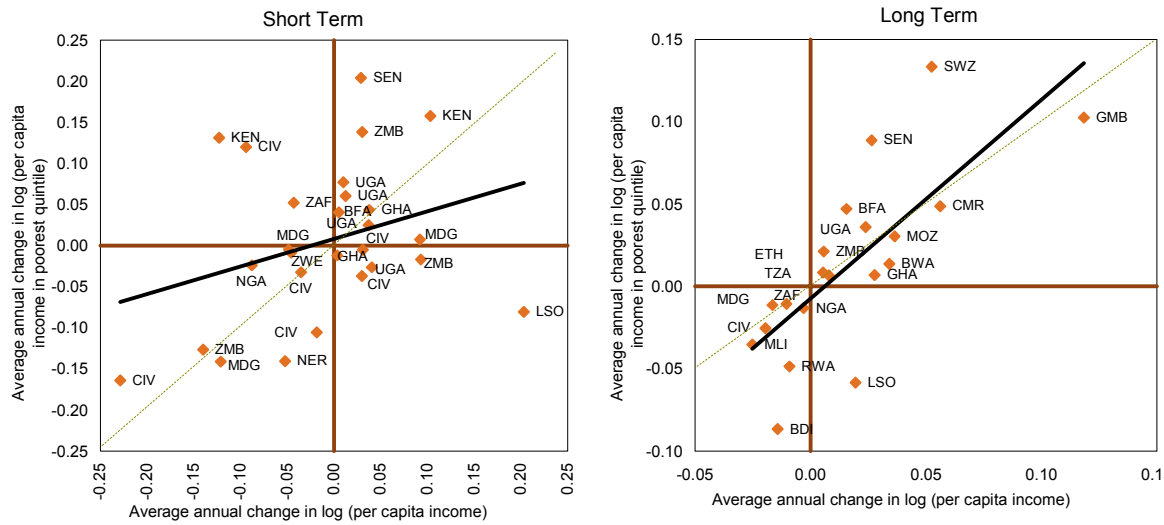


Sources: Chen and Ravallion (2007); and IMF, staff calculations.
Note: Country names are abbreviated according to the ISO Alpha-3 standard codes.

[10] The sample is limited to sub-Saharan African countries with both an observation before 1995 and one after. Furthermore, the sample is limited to two observations per country, with the survey year closest to 1990 chosen for the starting point, and the latest survey for the end point. The pattern is similar for broader samples, as documented in Dollar and Kraay (2002). It is also similar if the sample is restricted to the 16 high-growth cases, though there are very few observations.

[11] Compared with estimated elasticities for other regions reported by the World Bank and IMF (2007), the rate is somewhat low. Even when the poor benefit equiproportionately from growth in average incomes, the effect of a given average growth rate on poverty reduction will depend on how far the poor are from the mean and on the evenness of the income distribution. For example, a more uneven distribution may imply a smaller response of poverty to growth (on this see Ravallion, 1997).

Figure 2.23. Growth and Inequality



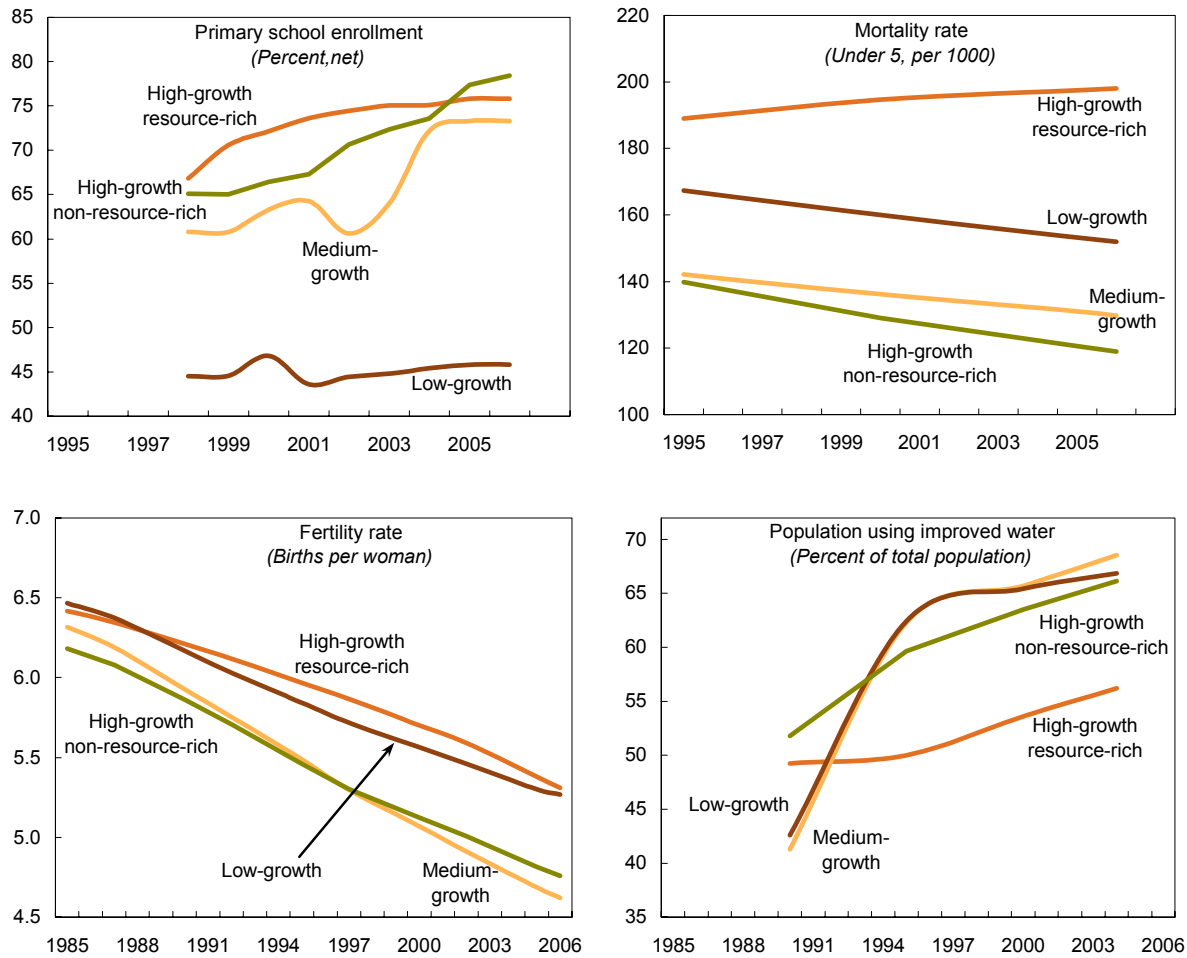
Sources: Chen and Ravallion (2007); and IMF, staff calculations.
Note: Country names are abbreviated according to the ISO Alpha-3 standard codes.

Fast-growing countries in the region, particularly those that are non-resource-rich, have seen major improvements in many of the other MDG target areas besides poverty (see Figure 2.24), though results are in many cases disappointing—particularly for resource-rich countries—and on current trajectories most countries, even the fast growers, will fail to achieve most MDGs by the 2015 target date (Commission on Growth and Development, 2008). Improvements in areas other than poverty addressed by the MDGs are important to promote the pace and sustainability of the current growth takeoff, for two reasons. First, these improvements increase human capital and thus in turn growth potential. Second, by improving social cohesion, and perhaps lowering the degree of inequality, they may help sustain the policies necessary politically to reform.[12]

In sum, two conclusions emerge from the evidence on whether growth has helped the poor in sub-Saharan Africa. First, the poor are on average significantly better off as a result of the recent period of growth, and usually enjoy at least the same rate of growth in their incomes as higher income groups. Second, this growth is beginning to yield benefits, as the fraction of the population living below the poverty level declines and social conditions improve, especially in fast growers. Of course, that growth is usually propoor does not mean it always is. It is important that policies, such as those related to spending on health and education, work to broaden the benefits of growth. For many resource-rich countries, this challenge is clearly greater.

[12] In general, the empirical evidence on the impact of inequality on growth is mixed.

Figure 2.24. Social Indicators



Source: World Bank, World Development Indicators.

Strategies and Policies to Sustain High Growth

Many sub-Saharan African countries have overcome decades of poor performance, poverty traps, unforgiving geography, and weak institutional endowments to achieve high and sustained real per capita income growth over the past 10–15 years. Sub-Saharan Africa's growth takeoff since 1995 has meant that, for the first time since the 1970s, income levels in the region have begun to converge with those in developed countries and have kept up with those in most other developing regions. Critically, this growth has both helped the poor and helped countries make progress towards even the other MDGs not related to poverty.

Although generally much higher than before, growth rates in most of the region's countries are still too low, especially to achieve the poverty reduction MDG (World Bank and IMF, 2008). Moreover, per capita growth of 2¼ percent, the threshold used here to define fast growers, would leave today's poorest countries still well below middle-income status 30 years from now. However, it would represent a huge improvement over the past, and if sustained, it would result in tremendous reductions in poverty within a generation.

Can this level of growth be sustained? Africa's postindependence history is a cautionary tale. High levels of growth in the 1960s and 1970s did not last in most countries. There are some grounds for optimism today, however: the current takeoff already looks more persistent, as

well as higher, than other post-independence growth episodes for which data are available.

The nature of the takeoff offers further grounds for hope. First, it is not dependent solely on natural resource booms or terms of trade increases: many of the fast growers have benefited from neither. Second, in most countries it is anchored in fundamental policy improvements made in the 1990s that have been continued. Sustaining these reforms will be critical to sustaining the growth takeoff itself.

The most fundamental of these policy reforms has simply been avoidance of the major policy failures that have been so critical in causing past growth booms to be aborted. The most important is the avoidance of "state failure." Many of the takeoff countries are post-conflict, and almost all of the slow-grower group are either in conflict or have only recently emerged—too recently to have achieved fast-grower status yet.

A second major achievement of most of the fast growers has been the establishment and maintenance of macroeconomic stability. Inflation has come down and has stayed low. Fiscal policy, abetted in many cases by higher aid and debt relief and in others by large resource revenues, has served to reduce debt levels while enabling levels of social and public investment spending to be increased. These policies and the associated substantial reserve accumulation have reduced vulnerability to shocks.

The fast growers generally emerged from the early 1990s without pervasive state controls, but beyond that the diversity of their starting points shows, encouragingly, that the minimum levels of institutions required to achieve rapid growth are quite low. Some of the longer-term trends are cause for optimism. The demographic transition to lower fertility rates and lower dependency ratios seems to have begun, albeit gradually, suggesting that this important if slow-moving factor may be starting to contribute to higher growth. Moreover, the spread of democracy might suggest that more accountable and hence responsive governments are becoming more common—though as Ndulu, Chakraborti, and others (2007) explain, the growth implications of this are not entirely straightforward.

Despite this good news, sustaining and broadening the current takeoff presents a series of policy challenges. This section examined factors that have helped produce sustained growth. It would be useful if this resulted in a recipe for all sub-Saharan African countries. However, the analysis here supports the conclusion of many other recent analyses that the necessary factors vary case by case. The evidence reviewed here and in the comprehensive studies summarized in Box 2.2, however, does point to a general conclusion: countries need to engage the global economy, maintain macroeconomic stability, and use prices to allocate resources.

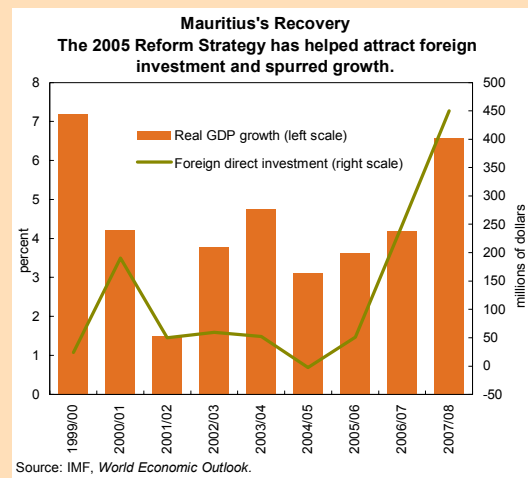
A major challenge with reform and growth strategies is not defining the ultimate objectives, but achieving them:

- *Reform strategies must be country and context specific.* What works well in one country may not be as effective transplanted to another unless it is adapted to local circumstances (North, 1990; Hausmann, Rodrik, and Velasco, 2005). Economies have achieved high income levels using a wide range of reform approaches, different degrees of state involvement in the economy, and diverse institutional structures.
- *The sequencing is important* (IMF, 2008). It appears, for instance, that liberalizing trade before the capital account may achieve better growth outcomes than the reverse, or even than pursuing both simultaneously.
- *Growth constraints and challenges change.* Reform strategies thus have to adapt over time (see Box 2.7 on Mauritius's growth for an example).

Box 2.7. The Mauritian Growth Miracles

The First Miracle. When Mauritius became independent, observers wondered about the prospects for a multiethnic society that was far from world markets, possessed few natural resources, and had an economy based on a single crop (sugar), a small domestic market, and a rapidly growing population. Mauritius showed how it could be done during the "first growth miracle" of the mid-1970s to mid-1990s, when per capita income rose from US$200 at independence to US$3,700 in 1997. The rise was founded on trade preferences for the traditional sugar sector and a new textile sector, and development of high-end tourism. Functioning democratic institutions promoted the social cohesion that is crucial in a multiethnic state. While other countries delayed reforms when subjected to shocks like terms of trade declines, Mauritius successfully overcame these shocks through institutions that promoted national consensus, regardless of the political philosophy of the government in power.

The Reform Challenge and the Second Miracle. Starting in about 2000, Mauritius began to suffer as trade preferences were phased out. The end of the Multifiber Agreement for textiles in December 2004, reductions in the European Union's sugar protocol prices by 36 percent over 2006–10, and more recently the surge in petroleum and food prices have produced a cumulative terms of trade shock of nearly 25 percent. Economic growth declined from 5 percent in the 1990s to 3 percent in the early 2000s.



Source: IMF, *World Economic Outlook*.

In response to this triple shock, the country's government in 2005 launched wide-ranging reforms that are bearing fruit. Designed through consultation, they attest to the ability of the Mauritian institutions to carry out tough reforms. Trade was liberalized (the eventual goal is a "duty-free island"), some price controls were lifted, and business regulations were simplified, earning Mauritius in 2008 the title of the best place to do business in Africa. Meanwhile, far-reaching tax reforms, notably featuring a 15 percent flat tax, and fiscal consolidation in the form of a new public debt law were initiated, with a goal of reducing public debt from 81 percent of GDP in 2002/03 to about 50 percent in the medium term. Appointing the Monetary Policy Committee in 2007 was a major step toward improved monetary policy. In response, growth has recovered to above 6 percent, and FDI is flowing into Mauritius at an unprecedented rate.

The Mauritian sugar and textiles industries have had to adapt to new realities. The sugar industry is consolidating and restructuring, with land converted to tourism and other agricultural uses. Producers are also expanding into such activities as generating power from sugar cane residue (bagasse), producing ethanol, and moving up the supply chain into refined sugar. After years of restructuring and decline, the textile sector began to prosper again in 2007/08 by concentrating on just-in-time supply of high-quality textiles, enabling Mauritian companies to differentiate themselves from low-cost producers.

New industries are also appearing. Mauritius has seen rapid growth in the offshore financial sector, founded on global business license firms: entities registered in Mauritius that funnel investments into other countries, primarily India. A real estate development initiative, known as "Integrated Resort Schemes," makes foreigners buying high-end real estate eligible for residency: it has drawn large amounts of FDI. Mauritius has also sought to position itself as a platform for investment from China and India into Eastern Africa, attracting additional large FDI flows.

Box 2.7. *(concluded)*

Looking ahead, the challenge for the authorities will be to sustain noninflationary growth. The economy is facing rising labor and infrastructural bottlenecks. The government is broadening structural reforms to spur economic efficiency and create fiscal space in public infrastructure and education. The authorities' ambitions are to see Mauritius transition to a regional banking and services hub. For these ambitions to be realized, the bold reform process started in 2005 will need to be pursued and deepened, with special attention to managing demand pressures and removing the constraints on higher growth.

Note: This box was prepared by Paul Mathieu and Patrick Imam.

A key policy challenge is improving the weak institutional environment in Africa. The broader experience on the role of institutions in growth, and the case studies examined here, show that the results in terms of institutional reforms and improvements are less clear-cut or widespread than may be desirable. In particular, there is sometimes a disconnect between specific policy reforms and the broad—often perception-based—indicators that are correlated with growth. Moreover, the agenda is too broad to be readily summarized. However, as described, for example, in Ndulu, Chakraborti, and others (2007), one basic element is a state that can deliver services more efficiently and accountably and with less corruption.

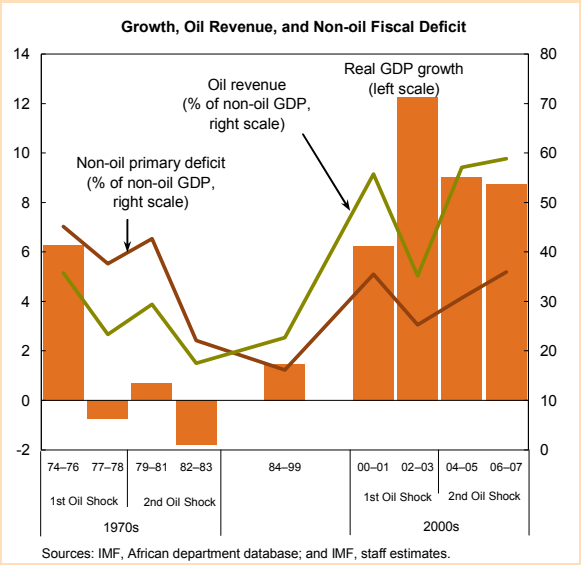
With debt relief, better policy frameworks, and a more-interested foreign capital market, many countries are now able to borrow internationally, at market rates, to finance public investment. When other sources of fiscal space (higher revenues, aid, more efficient allocation of spending) have also been used, and when sound public financial management, public investment programming, and debt management are in place, this ability to borrow internationally can be a boon. But clearly the risks are large: if the projects financed by the borrowing do not turn out to be as productive as hoped or the growth climate turns adverse for other reasons, a subsequent downturn could be deepened and prolonged by a debt crisis.

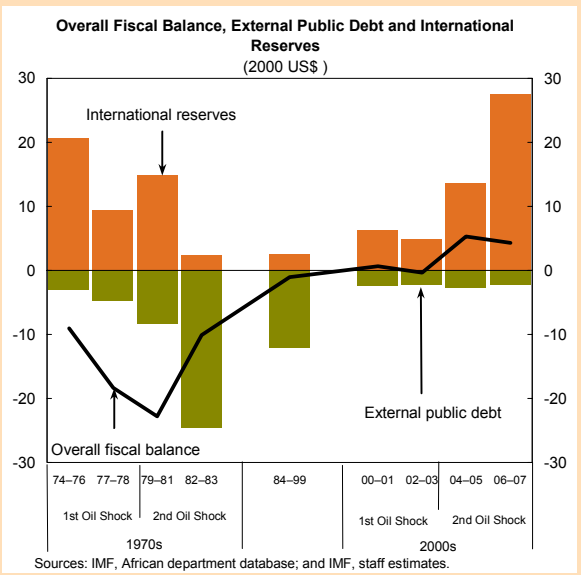
Resource-rich countries face a related challenge: to make the most of the boom. Unless they translate higher levels of resources into forceful policies and solid institutions—including improvement in public financial management and revenue transparency—underlying fiscal positions, and good investments in human and physical capital, the growth will end when the resource boom ends. It is reassuring that oil exporters today are saving more of their windfall gains (Box 2.8). However, some of the evidence discussed in this chapter, notably that from the CPIA on structural policies and on converting income gains into progress on the MDGs, suggests that much work remains to be done.

Another challenge relates to the role of structural transformation and manufactured exports. As emphasized in Box 2.2, fast-growing countries worldwide have been able to exploit globalization successfully, including by rapidly expanding exports. In the current success stories, these have played a fairly limited role, even in non-resource-intensive countries. However, the Commission on Growth and Development (2008) identifies export-led growth, in many cases of manufactured goods, as critical to growth success. Similarly, Johnson, Ostry, and Subramanian (2007) identify a dozen countries where income and institutional quality were similar to those in sub-Saharan Africa today that sustained high rates of growth (e.g., Indonesia and Thailand in the 1960s, or

Box 2.8. Sub-Saharan African Oil Producers during Past and Present Oil Booms

Sub-Saharan African oil-producing countries (SSA OPCs)[1]— although rather diverse in size, economic organization, and political history—show similar patterns of economic developments. The 1970s oil booms were characterized by boom-bust cycles: initially high growth, boosted by expansionary fiscal policies, was followed by contractions when oil revenue declined and public spending was sharply cut back. Accumulated macroeconomic imbalances (high external debt and low reserves) and Dutch disease effects resulted in a prolonged stagnation during the subsequent low-oil-price years.





In the present oil boom since 2000, growth has been strong and macroeconomic developments more favorable, driven by three factors. First, in the late 1990s steps were taken to tackle major macroeconomic imbalances: the CFA franc zone and Nigeria devalued, and external debt started to decline. Second, the increase in oil prices and revenues has been more gradual, supporting the implementation of less volatile fiscal policies. Third, and most importantly, macroeconomic policies reduced the impact of high oil revenues. While fiscal policies remained procyclical, the overall fiscal balance moved into surplus in all SSA OPCs. Fiscal institutions like Nigeria's oil-price-based fiscal rule and government deposits at central banks moderated the domestic demand impact of high oil revenues. In addition, resources were used to consolidate the fiscal and external positions. In all SSA OPCs external debt (also assisted by debt relief) was sharply reduced and international reserves increased significantly. These policy developments improved the macroeconomic indicators and—accompanied by structural reform programs—set the stage for increased confidence in the SSA OPC economies and the current high non-oil growth.

---

[1] The SSA OPCs covered in this box are Angola (since 2000, owing to data weaknesses in years prior to that), Cameroon (since 1979), the Republic of Congo, Equatorial Guinea (since 2000), Gabon, and Nigeria. The annual SSA OPC average is weighted by dollarized GDP. Although the figures included in this box are dominated by Nigeria, the pattern of developments in all SSA OPCs is broadly similar.

Note: This box was prepared by Christiane Roehler, building on earlier work by Valeria Fichera.

Vietnam and China in the 1980s). Their analysis highlights that rapid growth in manufactured exports was characteristic of almost all of these rapid growers (Chile being the only exception). They argue that manufactured-export-led growth lends itself particularly to institutional improvements during a boom, because improvements are necessary to sustain such growth. They contrast this type of growth with that associated with strong terms of trade gains, which they suggest are empirically less clearly associated with institutional improvements. The recent experience of fast-growing African countries is broadly consistent with this cautionary story.

Partly in light of these observations, a number of countries in Africa have increasingly turned their attention to an agenda of promoting private sector and export-led growth. Again, the agenda is extensive. Ndulu, Chakraborti, and others (2007) and Arbache, Go and Page (2008), among others, emphasize that the agenda of the state needs to move beyond avoiding major policy errors such as wars and macroeconomic instability—though the evidence discussed above suggests that this is indeed vital—to providing critical public goods.[13] These include improving infrastructure (roads, ports, electricity), which has been relatively neglected in the past 20 years or so, lowering the regulatory costs of doing business and providing stable property rights, and promoting an efficient and extensive financial sector. Better intraregional linkages are necessary, especially with respect to transportation and energy. Some of the recent success of landlocked resource-poor states may be due to the success of neighboring resource-rich coastal countries. This positive synergy needs to be built upon.

The Commission on Growth and Development's *Growth Report* (2008) notes possible emerging tensions between this export-oriented agenda and the current role of aid. Large increases in aid have helped bridge the resource gap, but as the *Report* notes, fears that aid may also undermine exports are "difficult to prove, but difficult to dismiss" (p. 77). Aid has been critical to providing better health and education and other social services. One of the purposes of aid is to free up domestic resources to produce for home consumption or investment rather than to close a foreign exchange gap, and some real appreciation may be an appropriate part of the process. But it may also damage nontraditional exports—at least in the short term, until the longer-term benefits of a healthier and better-educated population emerge. Bourguignon and Sundberg (2006) analyze this potential trade-off and underscore that aid-financed spending that is likely to be productive in the near term—for example, spending on infrastructure investment—can allow aid to support the traded-goods sector. In this context, it is important that the sectoral allocation of aid reflect country priorities and not just those of donors. Between 1993 and 2004, the share of aid to social sectors in the region rose from 27 percent to 43 percent, while the share going to productive sectors and program aid altogether fell from 36 to 23 percent (Ndulu, Chakraborti, and others 2007).

A final major challenge is the shifting global environment. As Chapter 1 discusses, growth in partner countries is declining, world financial markets are less hospitable, imported food and fuel inflation is challenging macroeconomic stability, and commodity prices are fluctuating wildly. Despite short-term correlations between African and world growth, there has been a medium-term divergence, but the continent is not expected to be sheltered from lower world growth.

Recent terms of trade shocks associated with rising food and fuel prices present difficult short-term policy challenges that, if mishandled, could derail the broader reform effort. As emphasized in Chapter 1, efforts to protect the

[13] Ndulu, Charkaborti, and others (2007) report that macroeconomic instability remains a concern of 43 percent of firms responding to a survey in Tanzania, 45 percent in Uganda, and 51 percent in Kenya, but only 30 percent in China.

most vulnerable are critical, but the policy reaction should not undermine debt sustainability, macroeconomic stability, or the broader structural reform effort. In the longer term, countries would benefit from eliminating restrictions on agricultural production, investing in infrastructure, enhancing agricultural support services, and avoiding measures such as export bans and price controls that undermine production incentives (see Box 1.5). Fortunately, the better macroeconomic policies of the recent past have enabled African economies to better withstand the current shock. On the other hand, the importance to national economies of growth in neighboring countries suggests that, just as favorable outcomes in some key major coastal and resource-rich countries like South Africa and Nigeria in recent years may be helping their neighbors, turnarounds in major countries could have important negative spillovers as well.

The need to adjust to these shocks underscores the importance of assuring that the benefits to reform remain broad-based. Recent work on the determinants of sustainable growth suggests that more equal income distribution helps to sustain growth (Berg, Ostry, and Zettlemeyer, 2008), perhaps because more equitable and cohesive societies build better institutions (Easterly, Ritzen, and Woolcock, 2006) or because they are better at managing external shocks (Rodrik, 1999). The relatively poor performance of many resource-rich countries in translating income gains into MDG achievement is thus doubly alarming.