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Victoria Kwakwa

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Mobilization of Funds for NEPAD Implementation

By

Dr. (Mrs.) Victoria Kwakwa[2]

1. Introduction

The New Partnership for Africa's Development (NEPAD) is a pledge by African leaders, based on a common vision and a firm shared conviction that they have a pressing duty to eradicate poverty and to place their countries both individually and collectively, on a path of sustainable growth and development and at the same time, to participate actively in the world economy and body politic. The program is anchored on the determination of Africans to extricate themselves and their continent from the malaise of underdevelopment and exclusion is globalizing world[3]. Broadly the goals of NEPAD include:

- Restoration of peace and security in Africa;
- Eradication of widespread poverty, several underdevelopment and acute income inequality between the rich and the poor;
- Promotion of accelerated growth and sustainable development,
- Halting the marginalization of Africa in the globalization process.

NEPAD is a welcome initiative and its goals are indeed laudable. Nevertheless it is clear that the initiative faces considerable challenges in raising the financial resources needed to achieve these goals. This paper explores issues related to the Mobilization of Funds for NEPAD implementation. The next section discusses the nature of the financing need; the third section explores domestic sources of funding, followed by a discussion of external funding sources in section four. Section five suggests some critical success for mobilizations of funds for NEPAD and

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[2]*Dr. Mrs.) Victoria Kwakwa, Country Economist, The World Bank, Abuja, and the paper was presented by Mr. Greg Nzekwu*

[3]*The New Partnership for Africa's Development October 2001*

the last section concludes.

II. NEPAD Financing Requirements

What are the resource implications of achieving NEPAD's goals?. This can only be estimated with reference to specific development targets in line with NEPAD goals. The Millennium Development Goal (MDG) having been agreed by the entire international community under the UN, appear particularly appropriate for this estimation. In particular, the specific and over-arching target of reducing by half the number of Africans living in extreme income poverty i.e. living on under USS1 a day by 2015 is particularly relevant and central to NEPAD's goals. In this regard, the NEPAD Steering Committee estimates first, that a minimum real growth rate of 7 percent annually is required on a sustained basis to achieve this objective in Africa. This in turn requires an investment rate of 33 percent of GDP annually. With estimated attainable savings rate of only 15 percent of GDP, and given the savings investment balance, this implies a saving gap of 18 percent of GDP annually. The Steering Committee estimates that about 8 percent of GDP can be raised through regular external flows, leaving some 10 percent of GDP- about USS54 billion still required in additional financing to close the savings gap. The UNECA and the World Bank (African Indicators 2001) estimated the resource gap to achieve the MDG income poverty reduction target in 1998 to be $ 64 billion or 12 percent of GDP at that time. The upshot of these estimates is that over $50 billion is needed annually to meet the objective of halving the number of Africans living in extreme poverty by 2015, which would move towards NEPAD goal of eradicating poverty.

III Domestic Sources of Funding for NEPAD Implementation.

There is a general tendency in African countries to focus on mobilizing funds from external sources in support of African development. In the past, the focus was on external development assistance through official sources, or through the public sector. But there is now also growing recognition of the importance of external unofficial or private inflows. Nevertheless, one of the important lessons of African's development experience over the last fifty odd years is that Africans need to and can indeed do more to harness domestic resources in support of development. Furthermore, to pull in international investment, African economies need to generate their own investment. Mr. Travor Manuel, Minister of Finance, Republic of South Africa made the following comments in a speech to the Commonwealth Business Council in September 2002:

"Despite the enormity of aid flows and once-off investments in natural resources, for many of our economies, these are necessary but simply insufficient to raise living standards and growth rates. Economic growth is impossible without an active, capable and well-governed state and private sector, just as poverty reduction is impossible without growth that benefits more than just the elite".

In the same speech, Mr. Manuel also recognized that while focusing on what Africa must do to pull in investment from abroad critically important, most African economies are small and mostly open economies subjected to shifts in investor sentiment in the rest of the world. These comments suggest that there must be a proper balance between focus on mobilizing funds from external sources on the one hand and from domestic sources on the other hand. I think we can go further to say that the chances of mobilizing external resources will be improved if African countries can put in place the needed steps to attract domestic investment. In addition, in conformity with the principle of ownership on which NEPAD was premised, is makes sense for the search for resources to fund NEPAD to begin at home and for Africans to begin to do what they need to do to raise more resources from domestic sources.

The NEPAD initiative recognizes the importance of both domestic and external sources for achieving the needed funding for NEPAD. This is evident in the NEPAD document as well as in the estimation of resource requirements put forward by the NEPAD Steering Committee. Some African Heads of States including President Thabo Mbeki have actually advocated that Africans rely more on themselves for funding NEPAD. Key sources of domestic funding include:

Domestic Savings

Savings performance (both public and private) in SUB-Saharan African (SSA) countries is far below that of other developing regions. As a region, SSA has extremely low and stagnant savings. Gabon and Angola which have experienced rates of about 38 percent and 28 percent respectively in the late 1990s are clearly outliers in a region where most have savings rate of under 15% and in some cases even negative rates of saving. Unlike in other developing regions where increased domestic savings have been driven by private savings, in the African case, private savings have not risen fast enough to offset negative trends in public savings. Stimulating domestic private savings will not be achieved overnight and will require substantial reforms including efforts to reform financial sector. In the shorter term perhaps, there is better chance (relatively) of promoting public savings through public expenditure reforms that promote efficiency and discipline in public resources use.

Forced savings schemes e.g. through contributory pension systems as is being proposed here in Nigeria could also be an important part of promoting savings and investible funds that could be tapped to fund NEPAD programs.

Export Earnings

Africa's share of world trade has fallen sharply over the last half a century. There are several factors behinds this. One is the continent's heavy reliance on mainly unprocessed and semi-processed low-value-added primary commodities. Coffee for example accounts for around 95 percent of Uganda's total export earnings and over 65 percent in Burundi, Ethiopia and Rwanda. And downward pressure on many primary commodity prices during the 1980s and much of the 1990s has hurt African export earnings. In Nigeria, proceeds of oil exports constitute about 95 percent of total export earnings. The major drawback for the economy is the extreme volatility in international oil prices and therefore in export receipts.

Much more needs to be down to build a diversified export revenue base that can allow sustained growth in export proceeds to support African development and NEPAD. Again this will not happen overnight and will require some structural transformation of African economies towards production of higher value manufactured exports. In the short term, African economies could take better advantage of arrangements such as African Growth Opportunity Act (AGOA), and other similar initiatives aimed at giving preference to African exports to the west.

These initiatives are not perfect and do not have African export earnings in perspective. Besides, they will be considerably impacted by policies in the developed countries regarding government subsidies and support to developed country producers (mainly farmers) in areas that compete with African exports e.g. agricultural exports. The average American farmer receives an estimated $12,000 annually in subsidies and other forms of government support while EU farmers receive about $16,000 annually. There has recently been considerable discussion of the adverse impacts on African exports earnings of developed country subsidies to cotton producers.

A Change in policy in the industrial countries on this issue could certainly have considerable positive impact on African economies and therefore generate considerable resources for NEPAD funding. But again, appreciable strengthening of this potential source of funding will take a while to achieve.

Financial / Capital Markets:

African financial and capital markets are shallow and often do not provide access to long term fund which are critical for the type of investment which would be needed for NEPAD initiatives. Stock exchanges do not exist in most countries, and the banking sector which tends to dominate the formal financial sector is often weak and reaches only a small proportion of the populations. In several countries including Nigeria, where there is evidence of considerable resource availability in banks, the financial intermediation function is still extremely weak and limited resources are provided to fund productive investments such as envisaged under

NEPAD. Most economies have low levels of monetization with large informal sectors largely cut off from formal financial markets. Bringing this large informal sector into the monelised economy will be critical and could provide an important source of funds for NEPAD.

For African Governments, domestic funding has the upside of avoiding 'conditionalities' sometimes linked to external resources, some of which they might find intrusive. However in the short run, Africa is capital scarce thus domestic sources are unlikely to contribute significantly to NEPAD.

Significant measures which will likely take a while to have impact, is needed. This is true for virtually every potential source of domestic funding that could be mobilized in support of NEPAD implementation. However, domestic funding needs to and can be built up over the medium and longer term if the right measures are put in place now. This will also be important in ensuring that over time, NEPAD is truly "African".

IV External Sources of Funding for NEPAD

Official Development ASSISTANCE (ODA)

NEPAD has received strong endorsement from external partners in the developed world. But donors are understandably reticent to write a blank cheque for the initiative. Donors particularly want to see some concrete results and some reforms in African countries that will ensure that assistance is utilized more effectively to support NEPAD's laudable goals.

There have been some promises. The EU has pledged an annual funding package of $ 3.7 billion annually over and above existing commitments to the region. T the G8 summit in Kananaskis, Canada in 2002, Canada pledged an immediate allocation of about C$500 million. The UK announced before the Summit that its aid to Africa would increase to $1.4 billion by 2006. Germany, France and Italy were also open to the idea of a major EU commitment. However, US, Russia and Japan felt they could not pledge more than they have already pledged to the region, partly because of domestic economic difficulties. The African Action Plan issued by the G8 repeated external donor ODA commitment during the Monterrey

Conference on Development Finance to collective provide $12 billion more in annual aid by 2006, with 50 percent ($6 billion) of this going to Africa.

So far, little ODA money had flowed to support NEPAD activities, mainly because funds were conditional, a fact that was reinforced by the G8 Summit in Evian, France in June 2003.

External donors want to see some proof that economic and security situation on the continent is stabilizing and that aid can be more effective than in the past supporting development in African. It is also important to note the general decline in ODA to the developing world, reflecting donor concerns about aid effectiveness. ODA flows to SSA declined 32 percent between 1995 to 2000 with only a slight increase in 2001. it is also likely that the great share of ODA in the next few years will go to humanitarian relief and reconstruction in Afghanistan and Iraq.

Debt Relief / Forgiveness

Apart from traditional debt relief/rescheduling arrangements under the Paris Club, the only new initiative in this regard is the highly indebted Poor Country (HICP) initiative led by the Worlds Bank and the IMF. This initiative is applied on the basis of a determination of "debt sustainability". This means only countries that are judged as poor and with debt levels that are unsustainable are eligible for debt relief under this initiative. Countries like Nigeria who are poor but meet the applied definition of debt sustainability cannot participate in the initiative. As at September 2003, it had been agreed that about 27 of the 38 countries that potentially qualify for HIPC will eventually benefit from reduction in debt stock by about $^{2/3}$ in NPV terms. Eight of these countries had reached a point where debt relief is ready to be disbursed. But the HIPC initiative is seen as too limited in scope and too slow in delivering concrete results since external debt service payments could still be a significant portion of resources outflow. African countries would like further and deeper debt relief beyond what is provided by the Paris Club and HIPC and in the long term would like to link debt relief to costed poverty reduction outcomes, to really create the extent of fiscal space needed to fund NEPAD. In the interim, African countries would like to fix ceilings on debt service payments as a proportion of fiscal revenues.

Foreign Direct investment

Global FDI peaked at $199.66 billion in1999 but by 2002 had declined to $143 billion, reflecting conditions in investing countries. SSA gets between 3-5 percent of FDI flows to all developing countries, peaking at 8 percent in 2001. FDI flows are extremely selective in terms of acceptable recipient countries since they are driven by returns on investment rather than by development need. The real issue in attracting higher levels of FDI into Africa is whether African countries can provide rates of return that are competitive relative to returns elsewhere. The fact that Africa attracts such small shares of overall FDI suggests that returns to investment in Africa real or perceived may not be competitive enough to make such investment attractive. While it is likely that returns on investments in SSA can potentially yield just as high if not even higher returns than elsewhere, action is needed to improve the investment climate, to address issues of security of life and property and to address the often cost of complimentary production infrastructural services. Such small shares of overall FDI suggests that returns to investment in Africa - real or perceived may not be competitive enough to make such investment attractive.

While it is likely that returns on investments in SSA can potentially yield just as high if not even higher returns than elsewhere, action is needed to improve the investment climate, to address issues of security of life and property and to address the often cost of complimentary production infrastructural services.

Workers' Remittances

Workers' remittances are an increasingly important source of capital for developing countries, including countries in SSA. In 2002, workers' remittances to developing countries rose 67 percent over its 2001 level. The growth is one of the driving forces behind NEPAD's African's Diaspora initiative which aims to engage Africans living abroad in the development of the continent. Given the string desire for the most Africans abroad to return to their countries at some point or at a minimum contribute to their countries' development, and the fact that several have done extremely well outside, this is certainly an important source of capital to tap and one that could be available relatively quickly/easily.

Capital Repatriation

It is well known that there are considerable "African" i.e. resources originating in Africa- resources abroad (both legal and illegal) and owned by Africans that could boost investment funds for NEPAD. For resources that were sent legally out of the country, the challenge is convincing owners that their monies if returned to Africa could yield decent returns to make repatriation a worthwhile venture. For monies that were illegally sent outside the country, one challenge is getting some cooperation of foreign banks to help repatriate these funds. Another option that is increasingly discussed in some circles here in Nigeria is for all such monies to be brought in without fear of persecution of owners if and only if they will put into productive investments that will promote NEPAD goals.

This is of course an extremely controversial issue that will need further thought and discussion since Africa countries also want to avoid giving a signal that they will tolerate or will punish corruption and theft of public funds. On the other hand, in cases where these resources are significant and are almost impossible to get the cooperation of foreign banks or governments for its repatriation, it could be argued that the society as a whole would benefit if the money is brought in and used productively even if the owner of the capital is not taken to task.

V. Some Critical Success Factors in Mobilization of Funds for NEPAD Implementation

Whether one looks at domestic or external sources of funding, it is clear that NEPAD faces a Herculean task mobilizing the level of resources needed to achieve its goals. But there are a few factors that will be important determinants of success in this regard.

Good Governance, Accountability and Transparency in Government

This is fundamental, first, for the credibility of NEPAD as a whole. Africans as well as the international community need to be convinced that this not just another initiative similar to past initiatives but one that is different and has a strong chance of success. This can only be the case if African Governments who own this initiative show readiness and willingness to address some of the fundamentals constraint to Africa's development. A first and over-reaching issue is that of good governance and accountability of government. If African governments begin to credibly address issues of corruption and lack of accountability in government, it will send a strong signal that things are changing and this will build their credibility and therefore, the credibility of NEPAD.

Such actions will also help raise public savings as public resources are managed more efficiently or at a minimum ensure that public resources are starched further and are used more effectively to achieve investment and growth objectives. It will raise domestic private savings through promotion of macroeconomic stability which will foster private sector confidence and savings. It will give external official donors the comfort that their ODA will be used better to achieve NEPAD goals and improve the perceptions of potential external private investors. This is a fundamental issue that African Government have control over and need to address urgently to achieve success in mobilizing the resources they need in support of NEPAD.

Improved Security of Life and Property, Regulatory Framework and Markets

Improved security of life and property, and improved regulatory framework and markets will reduce perceptions of Africa as a risky place to do business and enhance returns to investment, both of which will promote private external capital flows as well as repatriation of African capital abroad.

Strengthened Financial Intermediation

Considerably more resources can be tapped from domestic markets if African governments undertake reforms to strengthen the functioning of financial markets and the financial intermediations function. This is important for promoting private savings and for achieving greater monetization of African economies especially in the rural areas.

Enhanced African Country Access to Developing Country Markets

It is increasingly recognized that action on the part of developed countries to increase access by African countries to develop country markets can go a long way towards boosting developing country export earnings and therefore raise resources for funding NEPAD implementation. This is an important and direct area of action for developed countries who want to support the NEPAD initiative.

Stronger Action in Both Africa and Developed Countries to Combat Financial Crime and Money Laundering

Actions by African countries to curtail the theft of public funds, financial crimes and money laundering is critical for stemming the leakage of financial resources from Africa to the developed world. On their part, developed country authorities also need to be much more vigilant in identifying and preventing their countries and institutions from being used as conduits / bases for stolen or other forms of ill-gotten wealth from African countries. Furthermore, they could act more aggressively to track and repatriate funds currently in their hands. Some estimates suggest that if African looted funds were returned, NEPAD might need additional G8 funding to meet its goals.

These factors include actions that African governments can take on their own and in a few cases, actions that need to be taken by developed countries. African countries need to focus on what they can do and what is in their power to deliver- on the levers that they control. This is not to say that external parties should not do anything but reflect the fact that a lot can be achieved is African Countries take on the reforms and actions that is within their power to implement.

Conclusion

NEPAD offers a unique opportunity for a fresh start in Africa and for African countries to finally begin to move forward individually and collectively in achieving their development objectives. If successful, it could herald the end of protracted stagnation and economic decline and set in motion real economic and social take-off of the content. But success of NEPAD will require considerable levels of financing for the various investment programs. This in turn cannot be achieved without more fundamental reforms to the way African economics are managed. African governments need to create the conditions for renewed hope in "the African Project".

They need to begin reforms that rebuild trust in government, make it easier for private operators both domestic and foreign to do business in Africa and secure decent and competitive levels of profit to their investments. They need to show that they can use their own resources better to act as a catalyst for inflows of foreign official assistance including debt relief. Developed countries also need to take actions on their part to facilitate the process.

In summary, without these fundamental reforms, with an investment and economic environment that continues to be severally distorted, tolerant of public sector inefficiency and resources misuse, unfriendly to private sector initiative, it is unlikely that NEPAD will go very far. It would become another failed initiative that leaves the majority of Africans just as poor, if not pooper than when the initiative was launched. African governments need to do all in their power to prevent such an outcome.