Could Asian Policies Propel African Growth?

Michael Roemer

Abstract

The unprecedented, rapid growth of economies in East and Southeast Asia since the 1960s has been both a ray of hope and a taunting mirage to other countries whose development has proceeded fitfully, or hardly at all, over the past 30 years. The contrast with Africa has been especially start. Yet there was nothing pre-ordained about this divergence. In the 1950s and 1960s, most observers thought Asia's economies were destined for prolonged poverty, while Africa's independence spurred great optimism. Moreover, the endowments of countries like Indonesia, Malaysia and Thailand in the 1960s were not too different from those of several African countries in the 1980s. The differences in performance can be traced to political leadership that was more attuned to development in Asia and to better economic policies, especially macroeconomic management, flexible factor markets and outward-looking, if still protectionist, industrial policies.

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COULD ASIAN POLICIES PROPEL AFRICAN GROWTH?

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The unprecedented, rapid growth of economies in East and Southeast Asia since the 1960s has been both a ray of hope and a taunting mirage to other countries whose development has proceeded fitfully, or hardly at all, over the past 30 years. The contrast with Africa has been especially stark, as Figure 1 shows. From 1973 to 1993, in all the rapidly growing economies of East and Southeast Asia--China, Hong Kong, Indonesia, Malaysia, Singapore, South Korea, Taiwan and Thailand--income per capita grew by 4 to 9% a year, doubling or even, as in Korea, quintupling incomes over those 20 years. Only the Philippines, of the Asian countries in the graph, failed to grow rapidly. In Africa, only Botswana grew at Asian rates (7% a year) and the second-fastest grower, Cameroon, saw incomes rise by only one percent a year. Eight of the 14 countries listed suffered declines in average incomes.[2]

FIGURE 1 HERE

There was nothing pre-ordained about this divergence. In the 1950s and early 1960s Asia appeared caught in a low-level equilibrium trap, with large and growing populations, unstable governments, and in many cases a weak natural resource base. Many observers thought Asia's economies were destined for prolonged poverty. In contrast, as Africa gained independence in the late 1950s and 1960s, it held great promise. Africa started with limited educational attainments and experience in governance, but with relatively generous land and resource endowments compared to its population. Destructive civil wars had mostly been avoided and national independence brought a wave of optimism that anything could be done. But Africa's promise has not realized. After a spurt of post-independence economic growth, external shocks, poor policy responses and ineffective development strategies brought economic stagnation to many countries, causing even front-runners such as Kenya and Cote d'Ivoire to lose momentum.

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[1] I want to thank David Lindauer, my co-editor of *Asia and Africa: Legacies and Opportunities* [1994] for reading and commenting on this paper, which is an update and revision of our Chapter 1 of that volume. I am also grateful to Melvin Spence and to Faith Paul for collecting and organizing the data.

[2] This paper follows the pattern of Lindauer and Roemer [1994] in selecting 9 countries of East and Southeast Asia and 14 countries of Africa to illustrate the similarities and contrasts between the two regions. The Asian countries are the most rapidly growing ones plus the Philippines. Other countries in East and Southeast Asia, including Myanmar, North Korea and Vietnam, experienced slower growth. The African countries included in this study broadly represent the spectrum of well- and poorly-endowed countries as well as anglophone and francophone countries. Data used in this paper are from World Bank [1995] and IMF [1995] unless otherwise noted.

What is there in the Asian experience that might be translated to Africa? The countries most often cited as models for others are Hong Kong, Singapore, South Korea and Taiwan, which are designated "East Asian" countries despite the location of Singapore in Southeast Asia. Less attention has been paid to three other countries of Southeast Asia--Indonesia, Malaysia, and Thailand--which have also grown rapidly since the late 1960s. These three countries have natural and human endowments, ethnic heterogeneity and forms of government that resemble those in Africa far better than did the countries of East Asia. Thus the experiences of Indonesia, Malaysia and Thailand may suggest development strategies that are more appropriate for Africa [Lindauer and Roemer, 1994: ch.1].

To consider whether Southeast Asian policies could be adapted to stimulate rapid growth in Africa, this paper considers the sources of growth in Asia; discusses issues of governance that establish the framework for economic strategies; assesses the factor endowments of Asia and Africa; and then explores three groups of economic policies that make Asian growth distinctive: macroeconomic management, factor market flexibility and industrial policy.

Sources of Growth in Asia and Africa

One source of Asian growth has been the sheer accumulation of factors of production. Young [1995] has argued that much of the growth of income per capita in the four East Asian “tigers” can be explained by factor accumulation, including physical and human capital and increasing workforce participation rates. His estimates of the contribution to income growth of increases in factor productivity (the unexplained residual) range from slightly negative (in Singapore) to 2.3% a year (in Hong Kong), accounting for zero to under 40% of the growth in per capita incomes from the mid-1960s to 1990. Young differs from a broad consensus among economists that a much larger fraction of Asian growth is due to increases in total factor productivity. In *The East Asian Miracle* [World Bank 1993], for example, cross-country regressions are presented in which factor accumulation, relative income and regional dummy variables explain half or less of variations in growth rates for some 80 countries, implying that the unexplained balance may be due to increases in factor productivity.

If sheer accumulation has been the cause of Asian growth, then African policies to induce higher saving and investment in equipment, infrastructure and education should be sufficient to accelerate growth. These would include budget balance or even surplus, reform of government expenditures, high interest rates for savers, possibly subsidized rates for borrowers, high taxes on consumption and forced saving schemes. These measures encompass a number of standard stabilization and structural adjustment policies but could exclude some, especially trade and market reforms, that many African governments have resisted. Krugman [1994] carries Young’s conclusions to an extreme, arguing that the so-called Asian “miracle” is little different from the massive accumulation that market Soviet growth in the 1950s and 1960s. There is convincing evidence, which we discuss below, that Krugman is wrong, but his *reductio ad absurdum* emphasizes the importance of sorting out the causes of the differences between Asian and African growth.

Our small sample of Asian and African countries can help to do this. Figure 2 plots the growth in per capita income from 1973 to 1993 against the average share of investment over the same period. The countries in the diagram fit into two groups. First, all the Asian countries, except the Philippines, plus Botswana had investment rates in excess of 25% of GNP and per capita growth rates exceeding 4% per year. All African countries and the Philippines had growth rates below 2% a year, but investment rates ranged from around 10 to 30%. This scatter diagram confirms the importance of capital accumulation in income growth. But it also shows that high investment rates alone do not guarantee rapid growth. Countries such as Kenya, Cameroon, Tanzania, Cote d'Ivoire and the Philippines had levels of investment comparable to those of many of East Asia's successful economies, but much lower, even negative, rates of growth over 20 years. Asian countries enjoyed much higher returns to their investments than did African countries. Something other than the accumulation of physical capital must have been at work.

FIGURE 2 HERE

The same point can be made about the accumulation of human capital, as shown in Figure 3. The Asian countries for which data are available increased their stock of human capital, measured as average years of schooling per adult, at rates of 2 to 5% a year from 1960 to 1985. But the African countries in our sample also cluster in the same range, with a few either lower or higher. This limited data set provides no support for the argument that rapid accumulation of human capital is correlated with high rates of income growth. A comparison of Asia and Africa suggests that increases in human capital may be necessary but are not sufficient for rapid economic growth.

FIGURE 3 HERE

The increase in one other factor of production bears a tighter relationship to economic growth: availability of foreign exchange. Figure 4 shows that growth in GNP per capita is closely correlated with growth in the dollar value of exports for the 22 countries in our sample, with none of the overlap noted for physical and human capital. The case for including foreign exchange as a factor of production lies in the incomplete and specialized structure of developing economies, which must import some intermediate goods, capital and technologically advanced inputs and hence require foreign exchange to pay for these imports. The Asian countries (and Botswana) were much more successful than African countries in expanding their export earnings over long periods and have been able to grow more rapidly as a result. Export growth serves economic growth in many ways other than financing imports. By seeking world markets for their goods, developing country producers are exposed to more intense competition, gain economies of scale, attract foreign investment and gain better access to improved technologies, all of which contribute to productivity gains. Thus the correlation between GNP and export growth, whatever it may mean for factor accumulation, suggests that openness to trade and the resulting factor productivity gains had much to do with Asia's higher growth rates.

FIGURE 4 HERE

Rapid Asian growth may have been less "miraculous" than many have claimed, owing more to factor accumulation and less to productivity gains. But any comparison between Asia and Africa cannot escape the conclusion that differences in growth were caused by more than the differences in rates of physical and human capital accumulation. Asia put its capital--physical and human--to much more productive use that did Africa. Easterly and Levine [1996] attribute 0.35% of the difference between African and Asian growth rates to differences in the endowments (not the growth) of schooling per adult and 0.68% to differences in the endowments of infrastructure (as proxied by telephones per capita), a total of about 1% a year.[3] But they attribute a growth difference of 1.5% a year to differences in macroeconomic policies. Sachs [1996] applies the results of a multi-country regression to show that if African countries had adopted Asian policies, their growth rates could have increased by 4.6% per year. Disparities in Asian and African economic performance lie in different approaches to governance, in stricter adherence to the dictates of factor endowments, and in more suitable macroeconomic, factor market, trade and industrial policies.

Governance and Economic Strategy[4]

Perhaps the central question in comparing the economic performance of Africa and Asia is why, over the past three decades, Asian governments have been more development-oriented? Political stability has certainly played a role. Park's 18-year reign in Korea, the Kuomintang's hold on Taiwan, Britain's colonial regime in Hong Kong, Lee's long dominance of Singapore, Suharto's 29-year rule in Indonesia and UMNO's long-tenured prime ministers in Malaysia all coincided with rapid developments in those countries. Thailand is a special case: although prime ministers changed frequently until the recent political reforms, the popularly revered monarchy has been able to protect and entrench the high-ranking officials who make economic policy.

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[3] Although Easterly and Levine use initial endowments of schooling and telephones, they employ three decade averages for each country. Factor accumulation enters by enhancing the initial conditions for the second and third decades.

[4] This section and the next section are substantially drawn from Lindauer and Roemer [1994].

Though political stability may be necessary for sustained rapid growth, it is obviously not sufficient. The Philippines, despite long-lived regimes, has not developed rapidly. Africa also has had stable governments for a decade and often much longer in Cote d'Ivoire, The Gambia, Kenya, Malawi, Senegal, Tanzania, Zaire, Zambia and Zimbabwe, none of which has maintained rapid development into the 1990s.

For a regime to become developmentally effective, economic development must weigh so heavily in the government's priorities that it is willing to risk political capital to achieve growth. Several Asian governments saw rapid development as essential to the survival of their regimes, as in Indonesia and Malaysia, or even to their countries, as in Korea, Taiwan, and Singapore. The choice of long-run development over short-run political and personal gain manifests itself in different ways. Rent-seeking is a common feature of both Southeast Asian and African countries. Yet leaders in Southeast Asia, with the notable exception of Marcos in the Philippines, have understood that growing rents require growing economies; when rent-seeking threatened sound economies, the rents were curbed. Leith and Lofchie [1993] observe that, in Ghana before the reforms of the 1980s and in other African countries, leaders have extracted rents without heed to sustaining growth in the economy that produces them. The result has been economic decline, much as if a renewable but limited natural resource had been overexploited.

The accommodation of entrepreneurially able ethnic minorities is another choice for development over politics. Ethnic Chinese have played major, even dominant roles in commerce and industry in Indonesia, Malaysia and Thailand, where governments have secured the political and economic rights of their Chinese minorities despite strong, sometimes violent, popular pressure for their suppression. In Africa, the position of former colonial European residents, of Lebanese in West Africa and of ethnic Indians in East Africa has been far more precarious, discouraging their investment. Even indigenous Africans have been disadvantaged if they belonged to an ethnic group that opposes the government or is unpopular with a more powerful group. Few African governments have pushed forcefully for accommodation among different racial or ethnic groups as an essential ingredient for sustained development either explicitly, as in Malaysia, or implicitly, as in Indonesia and Thailand.

The insulation of economic policymaking from politics is another important manifestation of Asia's development priorities. In Korea, Taiwan and Singapore, where economic prosperity and national survival were linked inextricably, good economic policy was considered good politics. In Southeast Asia, however, where rent-seeking was inherent in the clientelistic style of governance,[5] regimes made self-denying choices to establish planning commissions, finance ministries and central banks as bastions of economic technocrats entrusted to manage the economy. These officials have enjoyed long tenure in their jobs. One Indonesian

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[5] *Clientelism* is a reciprocal relationship in which politicians and officials with political or bureaucratic power create rents through controls over the economy and grant access to, or property rights over, those rents to private firms and individuals. The latter are, or then become, supporters and financiers of the politicians and officials.

finance minister spent 15 years on the job before he became coordinating economics minister for 5 more years. In Thailand, protected by the monarchy, the most senior, widely respected economist outlasted several governments. Malaysia's technocratic policymakers were less influential, but Malay political leaders acknowledged that rapid economic growth underlay their political and social goals. Though Africa has had a number of excellent economic policymakers, few of them were as influential over so long a period as their counterparts in Asia.

Governments in Asia have been able to choose economic development and reform without sacrificing regime stability and African regimes could do the same. The governments of Korea, Taiwan and to a lesser extent Singapore, threatened by foreign enemies and anxious to spur growth, chose to intervene to push their economies faster than unaided markets would, although in the same general directions. Determined political leaders and well-educated officials, often with military-like discipline, combined to elevate public goals above private gain as officials interacted with businessmen to generate export-led growth.

These characteristics were not so strong in Southeast Asia. Disciplined intervention to promote public goals was almost certain to be thwarted by the clientelism and rent-seeking that were entrenched features of governance. Consequently the governments of Indonesia, Malaysia and Thailand have left development more to the market than did Korea and Taiwan. They have actively managed their macroeconomies to establish stable and productive climates for investment; have invested heavily in infrastructure and agriculture; and acted to insulate exports from the distortions of protection and rent-seeking by making inputs available to exporters at world prices, free of quantitative controls. Other interventions have occurred, especially public investment in large-scale industry, but for the most part these industries have not played a central role in export-led growth in the three Southeast Asian countries. Export growth in Southeast Asia has come from multinational firms (especially in natural resources and electronics); from medium-sized firms producing labor-intensive goods, many owned by East Asian investors; and from agriculture. Market incentives, not government intervention, played the major role in guiding export growth.

The application to Africa of Asia's experience with government seems clear. African regimes, like those in Southeast Asia, have limited capacity to intervene decisively in private decisionmaking to accelerate development, as Korea once did. In both regions, clientelism and rent-seeking are characteristic of most regimes. In Africa, these have weakened, whether permanently or temporarily, only where economies have been largely destroyed, as in Ghana and Uganda. In contrast to Southeast Asia, Africa's low government salaries, declining standards of performance and weak official leadership have eroded morale in the civil service and forced many of the most competent officers to seek jobs elsewhere, often overseas. Until these conditions can be overcome, African developers should choose strategies that are no more interventionist than those in Southeast Asia, where civil service capabilities have been improving. For many countries in Africa, a mix even closer to open market economies, as described below, is likely to be more effective until governments themselves are transformed.

The Dictates of Factor Endowments

Each one of the rapidly growing economies of East and Southeast Asia followed the dictates of comparative advantage. Hong Kong, Korea and Singapore, poor in natural resources and capital but well endowed with unskilled labor, based their early development strategies on labor-intensive manufactures. Relative to its population, Taiwan had a better endowment of land than the other tigers and used it intensively in the early stages of growth, while also emphasizing labor-intensive manufactures and eventually more skill-intensive exports.

The export mix was not left entirely to existing endowments and market forces. Korea, Singapore and Taiwan did intervene to promote new exports. The most dramatic of these, Korea's heavy and chemical industry drive of the 1970s, probably pushed beyond the market and beyond Korea's comparative advantage at the time. But as economies develop, they accumulate physical and human capital that gradually shift comparative advantage towards the kinds of goods in which Korea invested in the 1970s. These and similar interventions in East Asia may have accelerated a process that was occurring in any case, but they did not take great leaps beyond the countries evolving capabilities.

All the Southeast Asian countries are endowed with highly productive agricultural land and other natural resources, which determined their export base during the early stages of rapid growth. These countries, not merely accepting their endowments, invested to maintain their cost advantage in traditional exports such as oil, natural gas, metals, timber, rice, palm oil and rubber, and also diversified within primary products into exports of coffee, tea, cocoa and fruit. In Indonesia and Thailand the primary export share of gross domestic product increased from 1970 to 1990, while in Malaysia it was maintained at nearly 40% of GDP, even as manufacturing and modern service industries flourished [Tomich, Roemer and Vincent, 1974].

Thus the three Southeast Asian countries moved into manufacturing, for import replacement and for export, from a solid base of primary export earnings. This strategy helped these economies to avoid the chronic shortages of foreign exchange that crippled African manufacturing in the 1980s. Nor did the Southeast Asian countries succumb to the opposite problem, Dutch disease, which handicaps export industry and agriculture through exchange rate appreciation brought on by rising export earnings. Indonesia, for example, devalued its exchange rate despite booming oil revenues in order to protect agriculture, while investing its oil rents productively in agriculture (especially irrigation for smallholder rice production), education, public health and infrastructure. Employing such policies, Indonesia and Malaysia converted their primary export wealth into sustainable development in other sectors. Nigeria, in contrast, allowed its exchange rate to appreciate, destroying export agriculture, and invested too much of its oil rents in projects with poor long-run returns.

In Southeast Asia, governments also invested--in research, irrigation, fertilizer subsidies, infrastructure, education, and health--to raise productivity in food agriculture, consistent with their comparative advantage and essential to their development strategy. Rising output of rice and other foods, especially in Indonesia and Thailand, freed workers for employment in industry, contributed to the relatively low real wages of urban workers and minimized the need to use foreign exchange for imports of staple foods [Goldman, 1994]. Agricultural productivity gains also played a central role in the dramatic reduction of rural poverty in Indonesia and Malaysia.[6] In Africa, neglect of agriculture is reflected in the decline of food production per capita since 1975 and the persistence of both rural and urban poverty.

During the 1980s, as agricultural productivity rose and world prices fell for many commodities, Indonesia and Thailand took advantage of their low-cost labor by moving with almost explosive force into labor-intensive export manufacturing, especially in textiles, clothing, and electronics. Malaysia had anticipated this development a good decade earlier and by the end of the 1980s was moving into more capital- and skill-intensive exports, notably in electronics. Though investments were made in chemicals, autos, aircraft and other industries not justified by existing comparative advantage, the principal thrust of policy was to encourage industries in which the Southeast Asian economies could compete in world markets. In Africa, inward-looking policies lost sight of comparative advantage and created a high-cost industrial sector with little export potential [Roemer, 1994].

Industrialization was immeasurably helped by the ability of Asian countries to utilize, not only their natural resources, but all the human resources available to them. For Korea, with its homogeneous population, this was no problem. The Kuomintang government of Taiwan encouraged small-scale industry, guided by market forces, at least partly because that strategy would tap the productive energies of the native Taiwanese without threatening the political control of the mainland Chinese who moved to Taiwan with the communist take-over of China in 1949. We have already spoken of the accommodation of ethnic Chinese businessmen in Southeast Asia. Indonesia's Sukarno, though no development leader, did knit many ethnic groups into a nation, largely ending ethnic strife as a deterrent to development. Africa has not been as successful in drawing on the talents and energies of all its ethnic groups, one of the choices of politics over development discussed in the previous section.

Southeast Asia in particular has supplemented its own resources with capital from abroad, including direct foreign investment. This has added not only capital, but entrepreneurial and technological capacity. African countries with limited entrepreneurial capacity, or which cannot easily accommodate ethnic minorities, may wish to utilize foreign investment as a substitute for some period. To attract foreign investors, African countries will have to follow the Southeast Asian countries in managing rather open economies, with export-oriented incentives and a minimum of controls.

African developers, like those in Asia, will have to follow the path of comparative advantage based on existing factor endowments, making full use of all their resources. Africa's

[6] In Malaysia, the headcount incidence of poverty dropped from 18% in 1970 to 2% in 1990, while in Indonesia the decline over the same period was from 60 to 15%, most likely one of the most dramatic declines in absolute poverty in history [Johansen, 1993: 42].

comparative advantage continues to lie in its natural resources and unskilled labor, which means in smallholder agriculture for food and export in most countries; in mineral exports for Algeria, Botswana, Cameroon, The Congo, Namibia, Nigeria, South Africa, Zambia and Zaire; and in tourism. Investment opportunities still exist in these often maligned industries. In light of the Southeast Asian experience, investments in primary industries ought to be pursued.

Labor-intensive manufacturing for export is presumably the next realm for many countries in Africa, especially those facing population pressure on their land. None of the Asian countries skipped over this step and, despite attempted technological leaps into chemicals, autos and aircraft, Southeast Asia's comparative advantage is still based primarily on labor-intensive manufactures. Neither factor endowments nor governmental capabilities suggest that leapfrogging into technologically advanced industries could work in Africa.

It is often alleged that Africa lags so far behind Asia in human capital accumulation that, even with large investments in education, they cannot catch up sufficiently to emulate Asian industrialization. In 1985, Asian endowments of human capital ran from 4.5 years of schooling per adult (Indonesia) to 8.5 years (Korea), while African endowments ranged from as little as one year (Mali) to 5.5 years (Zambia).[7] However, if one views Africa’s problem as generating growth from a primary or unskilled-labor base, as the Asian countries did in the 1960s and 1970s, then the relevant comparison is not African and Asia today, but Africa today and Asia in the 1960s. Figure 5 compares Asian educational endowments in 1960 with African endowments in 1985. It shows that there is little to distinguish the two groups of countries; African and Asian countries are interspersed throughout the graph. Not only does Africa start with levels of human capital comparable to those of the high-growth Asian countries at the start of their development spurts, but, as shown in Figure 3, Africa is also accumulating human capital as rapidly on average as the Asian countries have done.

FIGURE 5 HERE

Macroeconomic Management

The experience of developing countries everywhere suggests that macroeconomic stability is a necessary, but not sufficient, condition for rapid economic growth. Stanley Fischer [1993] has provided convincing evidence for this proposition through pooled cross-country and time-series regressions covering 80 countries over [20] years. Fischer’s regressions employ three dependent variables: growth of real GDP, growth of the capital stock and growth of factor productivity (the residual in a sources-of-growth accounting). He finds that three indicators of macroeconomic policy--low parallel market exchange rate premiums over the official rate, low budget deficits as

[7] From unpublished World Bank data.

a share of GNP and low rates of inflation--are positively and significantly associated with the dependent variables. Moreover, causality tends to run from the policy variables to the growth variables, rather than the other way around.

Figures 6 through 9 show that, for the three variables identified by Fischer, there is a stark contrast between Asian and African economic performance. Because policies change over relatively short periods of time, it is difficult to give accurate indicators of policy stances over the 20-year period used in the earlier charts. But more accurate policy indicators that cover two or three years cannot tell us much about long-term growth. As a compromise, the data in Figures 6 to 9 cover an eight-year period, from 1985 to 1993. During that period, the four East Asian and three Southeast Asian countries all maintained consistently sound macroeconomic policies. Among a few African countries, however, there have been major shifts in policy stance, particularly in Ghana, Uganda and Zambia, although these shifts do not mute the contrast between Africa and Asia.

Figure 6, comparing growth rates with parallel market exchange rate premiums, gives typical results. The Asian countries except China all had very low exchange rate premiums, suggesting that official rates, all of which were managed, kept very close to market-determined levels. African premiums, however, ranged from zero (a ratio of 1 in the chart) to almost 3 (for Zambia). Most of the countries experiencing rapid growth, at least 4% a year, also had low premiums; the exceptions were China and Botswana, with premiums was of 35 and 37%, respectively. Conversely, with those two exceptions, countries with high premiums had much lower growth rates over the eight-year period, mostly 2% or less; Uganda, recovering from civil war, experienced 2.4% growth. Thus, for this limited sample, a low exchange rate premium appears to be a helpful condition for rapid growth. But it is not sufficient: several countries, mostly francophone states, had low premiums and low or negative growth rates. The reason was that the greatly overvalued CFA franc, although penalizing exports and stifling economic growth, was backed by the French franc, so that traders took little risk in holding CFA francs and thus did not require a premium to do so. The devaluation of the CFA franc in January 1994, which doubled its rate against the dollar, was one of the most important policy reforms in Africa over the past decade.

FIGURE 6 HERE

A more controversial aspect of Asian exchange rate policy has been currency convertibility. Only Korea and Taiwan of the Asian countries in our sample did not allow convertibility. The Southeast Asian countries opened their capital accounts and have managed convertible currencies for two of decades or more. In Africa, the franc zone had convertibility but no flexibility to adjust the rate, so exports suffered. Outside the franc zone, African countries had strict currency controls. Convertibility in Asia has had two advantages. First, it has imposed a credible discipline on macroeconomic policy: with no exchange controls, the only safeguards against a catastrophic loss of reserves is sound macroeconomic policies. Second, convertibility contributes to an attractive investment climate, both because it is a credible guarantor of sound macro policy and because investors, domestic and foreign, know they can repatriate capital without hindrance. Indonesia, Malaysia and Thailand have all attracted substantial flows of foreign direct investment.

Convertibility cannot, however, be called a necessary condition for rapid growth, as Table 1 shows. Korea and Taiwan have maintained some foreign exchange controls throughout their periods of rapid growth and have only recently begun to dismantle them. What they and the other Asian countries shared was flexible management of their exchange rates. In contrast, the franc zone countries, which did maintain convertibility, maintained a fixed rate until 1994 and suffered stagnation or decline in average incomes. On the basis of these comparisons, it is flexibility rather than convertibility that matters. However, if attracting foreign investment is important to a country's development, as it was in Southeast Asia, then an end to controls over both the current and capital account appears to be an important ingredient of development strategy. Recent reforms in The Gambia, Ghana, Kenya, Zambia, and other countries have moved towards both exchange convertibility and rate flexibility.

Table 1: Currency Convertibility and Exchange Rate Flexibility

	Convertibility	**Foreign Exchange Controls**
Exchange Rate Flexibility	Hong Kong Indonesia Malaysia Singapore Thailand	Korea Taiwan
	The Gambia (post-85)	Kenya
Fixed Exchange Rate	Franc zone countries	Most other African countries

The relationship between government budget balances and growth is similar to but a little murkier than that between the parallel market exchange rate premium and growth. Figure 7 plots per capita GNP growth rates against budget surpluses expressed as a percentage of GNP. The fast-growing Asian countries had budget balances ranging from a 4% deficit (Taiwan) to a 0.7% surplus (Thailand). The two highest deficits, for Taiwan and Malaysia, must be seen in the context of the very high private saving rates experienced by those countries throughout the 1980s. In the late 1980s, Taiwan had to correct for an overzealous pursuit of tight macroeconomic policies that led to massive accumulations of foreign reserves [Roemer and Chou, 1996]. In both cases, deficits were financed entirely by borrowing from private savers and could be justified as stabilizing influences. The only African country with rapid growth, Botswana, ran budget surpluses of almost 17% during the period. Again, low-growth African countries had a range of balances from -9% of GNP (Zambia) to 8% (Cote d'Ivoire), and none of the African countries with deficits had saving rates approaching those of the Asian countries. In the absence of high saving rates, low deficits or surpluses appear to be necessary for rapid growth.

FIGURE 7 HERE

Conservative fiscal management helps growth in two ways. First, it helps make government a contributor to national saving and investment rather than a borrower that consumes private saving and crowds out private investment. Second, it reduces the need and temptation to use seignorage--borrowing from the monetary authority--as a means to finance government deficits. Increasing dependence on seignorage is a path to higher inflation which, as Fischer [1993] has shown, stifles rapid economic growth. Figure 8 shows that the governments of rapidly-growing Asian countries avoided borrowing from the central bank--indeed, in Indonesia it is illegal--and for the most part reduced their outstanding debt from 1985 to 1993. Ghana and most of the francophone states also avoided seignorage. But other African countries (and the Philippines) did use seignorage to finance deficits in amounts ranging to 5% of GNP.

FIGURE 8 HERE

Of all macroeconomic indicators, the rate of inflation appears to provide the strongest message for economic growth. Fischer [1993: 497] found that the inflation rate was the only macroeconomic indicator that had significant coefficients with all three specifications of the dependent variable (income growth, capital stock growth and productivity growth) and was significant even when all other independent variables (budget balance, parallel market exchange rate premium, terms of trade and variance of inflation) were included in the regressions. Figure 9 gives a picture for the Asian and African countries in our sample. Of the countries with income growth exceeding 4% a year from 1985 to 1993, including Botswana, none had inflation rates over 12% a year.[8] African countries in the sample had inflation rates ranging from negative to almost 300% (Zaire, not shown on the graph), but none except Botswana had growth rates over 2.5% a year. The low-inflation African countries were all in the franc zone, where conservative monetary and fiscal policies, leading to low inflation, were employed to defend the overvalued CFA franc for many years, to the detriment of economic growth.

FIGURE 9 HERE

For economies out of external or internal balance, stabilization is bitter medicine and may for a time, like chloroquine taken for malaria, cause worse symptoms than the disease. But it is hard to avoid the conclusion that stabilization is essential as a precondition for renewed economic growth.

[8] A 30-country sample that includes Latin American and South Asian countries shows a similar pattern with only one country, Chile, growing faster than 2% per capita per year with inflation over 10% from 1980 to 1992 [Gillis, *et al.*, 1996: 114]. Chile’s numbers were a growth rate just under 4% and annual inflation of 20%.

Flexible Factor Markets

All rapidly-growing Asian economies have maintained substantial flexibility in the operation of both labor and capital markets. Governments in both East and Southeast Asia ensured that employment and wages have been determined by market forces, not by government intervention or by collective bargaining. Labor market flexibility has been important in permitting the rapid reallocation of workers as macroeconomic and trade policies encouraged the emergence of new, mostly export, industries from textiles, clothing and footwear to steel, automobiles and electronics. Asian countries have also invested in education in order to improve the skills of the work force. As macroeconomic and trade policies encouraged industrial growth, the combination of a mobile labor force and upgraded skills led to rapidly increasing real wages in both industry and agriculture in these Asian economies.

African countries have a history of government regulation and labor-mangement-government agreements over employment and wages in the formal sector [Lindauer and Velenchik, 1994]. Years of stagnation or decline have made many of these institutions ineffective and forced down both employment and real wages. And the large informal sector has always provided considerable employment and wage flexibility. The Asian experience suggests that, as African governments put new development strategies in place, they should not revive the tripartite labor market agreements of the past, but maintain as much market-based flexibility as possible. This issued has been explicitly joined in South Africa, where the ANC-allied union, COSATU, has won substantial control over the wage and employment agreements, not only of its own workers, but of workers in firms and sectors not covered by the union. COSATU leaders, recognizing the cost disadvantage this imposes on South African industries in an increasingly open world and regional trading system, are even seeking to influence other countries, especially those in southern Africa, to adopt a similar system. Countries adopting this or similar approaches will not be able to emulate the Asian model and will be unable to stimulate rapid growth or job creation.

In contrast to labor markets, many national financial markets in Asia were dominated by government institutions and repressed by government controls over entry, interest rates and credit allocations [Cole and Duesenberry, 1994]. Korea was among the most interventionist countries in Asia, using directed, subsidized credit as a tool to encourage investment in new exports, especially by the *chaebol*. Taiwan had a similar approach and Indonesia's banking system has been dominated by state-owned banks that offered subsidized credit to large firms and clients of the regime. Only Hong Kong and Singapore adhered to neoclassical principles, developing open financial markets that have become international financial centers.

Despite pervasive government intervention, financial markets remained flexible in all seven Asian countries, though for different reasons. Korea and Taiwan each had a flourishing parallel or curb market that handled sufficient credit for the needs of small and medium firms, which were among the most dynamic exporters in the early stages of Korean growth and remain so in Taiwan. Although nominal interest rates, at 30% or more, were much higher on curb market loans than on bank loans, many labor-intensive firms were able to pay these rates and still earn profits in export markets. Indonesia, Malaysia and Thailand did not develop informal credit markets capable of financing industrialization. But, because these countries maintained convertible currencies, many investors, especially ethnic Chinese businessmen, had access to financial markets in Singapore and Hong Kong. This enabled firms to overcome the most stifling effects of financial interventions. During the 1980s, the Southeast Asian countries inaugurated financial reforms that started to release domestic financial markets from repressive interventions. Not only were Asian financial markets flexible, but even countries that controlled interest rates kept real rates positive, as Figure 10 shows.

FIGURE 10 HERE

African financial markets have also been repressed by credit and interest rate controls. Governments, however, have not been able to direct credit into productive channels as in Korea and Taiwan. Informal credit markets remain fragmented and operate on a small scale, serving households, farmers, traders and microenterprises, but not modern manufacturers. Foreign exchange controls have barred all but the largest firms from world financial markets. Moreover, in most African countries, interest rates were repressed so much that real rates turned negative. Again, only the francophone countries maintained positive real rates as part of their defense of the overvalued CFA franc. Financial reforms were not a prerequisite for outward-looking growth in Asia. In Africa, however, financial reforms may be necessary to overcome the disadvantages of small, fragmented informal markets and the long absence of African firms from world credit markets.

Trade and Industrial Strategy

We have already described how industrialization in Asia followed the contours of comparative advantage determined substantially by existing and evolving factor endowments. Despite this, Korea, Taiwan, Indonesia, Malaysia and Thailand all employed protectionist trade regimes. In the neoclassical paradigm of development, an outward-looking economy is characterized by internal prices for tradable goods that reflect world prices. Price distortions from this ideal are caused by import controls, tariffs, internal taxes, subsidies, credit allocations, public monopolies, and other government interventions. Figure 11 gives a rough indication of the deviations of prices from world levels in several Asian countries during the 1970s and compares these to similar measures for several other countries.[9] The three fast-growing Asian countries in the list--Malaysia, Thailand and Korea--have price distortions in the middle of the range. Economies such as Brazil, Kenya and Mexico, which were not notably open during the 1970s, have lower price deviations than the three Asian countries. Malawi's prices were about as distorted as those

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[9] Figure 11 measures the coefficient of variation, which is the standard deviation of the difference between domestic prices and purchasing power parity (U.S.) prices divided by the mean of PPP prices. A coefficient of 1.0 means that 32% of the sample of prices (the share of the distribution outside one standard deviation) differs from the PPP price by at least 100%. These estimates are from Perkins [1991: 22].

for the Asian economies and Zambia's were much more so. However, the Asian countries that protected local producers each took steps to insulate exporters from the disincentives of protectionist regimes, providing manufacturers with simulated free trade environments that offered easy access to inputs essentially at world prices.

FIGURE 11 HERE

In Korea the large-scale, heavy, import-substituting industries were promoted on the understanding that they would soon become competitive exporters, as several did. Korea employed an arsenal of weapons to encourage exports, especially by the conglomerates, including subsidized credit from government banks, licenses for and duty drawbacks on imported inputs, protection in the domestic market to cross-subsidize export development, relaxed enforcement of income taxes and moral suasion. Officials, meeting with the *chaebol*, established and enforced ambitious export targets on which continued subsidies depended. Targets and their enforcement were directly sanctioned by President Park.

Korea's pro-export interventions, which have been described as "market-conforming," speeded industrial development beyond the rate dictated by comparative advantage and market forces, though in the same general direction. But these measures required an extraordinary performance by Korea's bureaucracy. President Park laid down and enforced export goals as a national imperative. Officials were sufficiently disciplined to manage these complex interventions. Firms that did not meet targets suffered the consequences, giving Korea's interventionist policies a credibility that few other governments have been able to achieve.

Southeast Asian countries tried nothing so ambitious. Malaysia used export processing zones extensively, especially but not only for electronics exporters. Indonesia established an agency to grant exporters both access to imports despite protective licensing restrictions and drawbacks of (or exemption from) duties on inputs. Thailand relied more on macroeconomic incentives to support exports, but also granted duty exemptions to foreign investors who planned to export. In all three countries, the economic stresses of the 1980s impelled governments to institute gradualist but determined reform programs that have begun to reduce protection, turning all industries outward to face international competition. These well-established reforms have given investors clear signals about the direction and dependability of future policies.

In Africa, trade policies have been exclusively inward-looking and government intervention has been pervasive in industry. The political culture of clientelism and rent-seeking and the declining effectiveness of bureaucracies have hindered industrialization. After two decades of industrialization, there is little evidence of internationally competitive manufacturing. One exception is Mauritius, which adopted outward-looking policies akin to those in Asia. For Sub-Saharan Africa as a whole, intervention has been tried and failed.

Export zones in Africa have foundered because officials try to control or extract rents from them. Tariff and other tax rebate schemes have failed to stimulate exports because payments are so slow and uncertain that firms do not count on them. A few determined governments may make such programs work and they could be helpful. But for the majority of countries, a mix closer to the open, market-based economy, with very limited protection for infant industries, may be more effective in moving towards the next, manufacturing-based phase of comparative advantage.

Conclusion: Can Asian Policies Work in Africa?

This review of Asia's high-growth strategies suggests that, to accelerate their growth, African countries should pursue the following policies:

- Empower competent technocratic policymakers to manage macroeconomic and development policies with strong political support.

- Create a climate in which all ethnic groups, especially entrepreneurially talented minorities, can participate in development with low risk.

- Design strategies that build on existing comparative advantage in agriculture and labor-intensive industry while investing in education that will create a more skilled workforce for a gradual transition to new industrial and service exports.

- Adhere strictly to sound macroeconomic policies including a realistic and flexible exchange rate, small budget deficits or preferably small surpluses and appropriately tight monetary policies; currency convertibility is a credible guarantor of these policies.

- Keep labor markets flexible, so that market forces determine wages and employers are free to hire and dismiss with a minimum of government regulation.

- Reform financial markets, permitting market forces to determine credit allocations and interest rates and, along with currency convertibility, creating a welcoming climate for foreign investors.

- Undertake trade reforms that will open economies increasingly to world markets; while the vestiges of protection remain in place, create mechanisms by which export producers can obtain inputs at world prices, free of duties and free from import controls.

It is often argued that, even with such development reforms, African countries cannot emulate Asian growth rates. What grounds do we have for optimism? First, world markets can accommodate rapid African export growth. True, conditions do not seem so promising for African countries as they did for Asia in the 1960s and 1970s. Growth rates are slower in the northern countries and Asian exporters will be formidable competitors. However, Africa's share of world trade is tiny, so that a major expansion of its exports could easily be absorbed if only African economies become competitive. Moreover, the very growth of Asian economies itself establishes new markets for African goods that were not available to Asia 30 years ago.

Second, Africa has not really tried sound development strategies. Its policies have been unstable, inward-looking and generally counterproductive. Asian and other rapidly-growing countries have shown that better policies can deliver faster growth. Ghana, Uganda and other reforming countries in Africa have also proved the worth of growth-oriented policies, even if the results have not been as dramatic as those in Asia nor as African reformers had hoped. Econometric studies by Sachs [1996] and by Easterly and Levine [1996] suggest that these policies might be capable of adding 1.5 to 4% a year to long-term growth rates in Africa.

Third, the dominant pessimism about African development is not new. A similar cloud of doom hung over Asia in the 1950s and 1960s. Korea and Taiwan were considered hopeless cases before their economic reforms were implemented, scholars wrote of the imploding Indonesian economy, racial strife threatened stability in Malaysia, upheavals threatened stability in China and the Vietnam war made the entire region seem politically risky. In this perspective, Africa's current troubles do not seem insurmountable. Countries such as South Africa, Uganda and Mozambique have shown themselves capable of overcoming dire conditions and have at least begun the process of renewed development. With sound and steady economic development policies, what has been accomplished by several countries in Asia could be accomplished by several countries in Africa as well.

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Figure 1: Growth of GNP Per Capita
Percent per annum

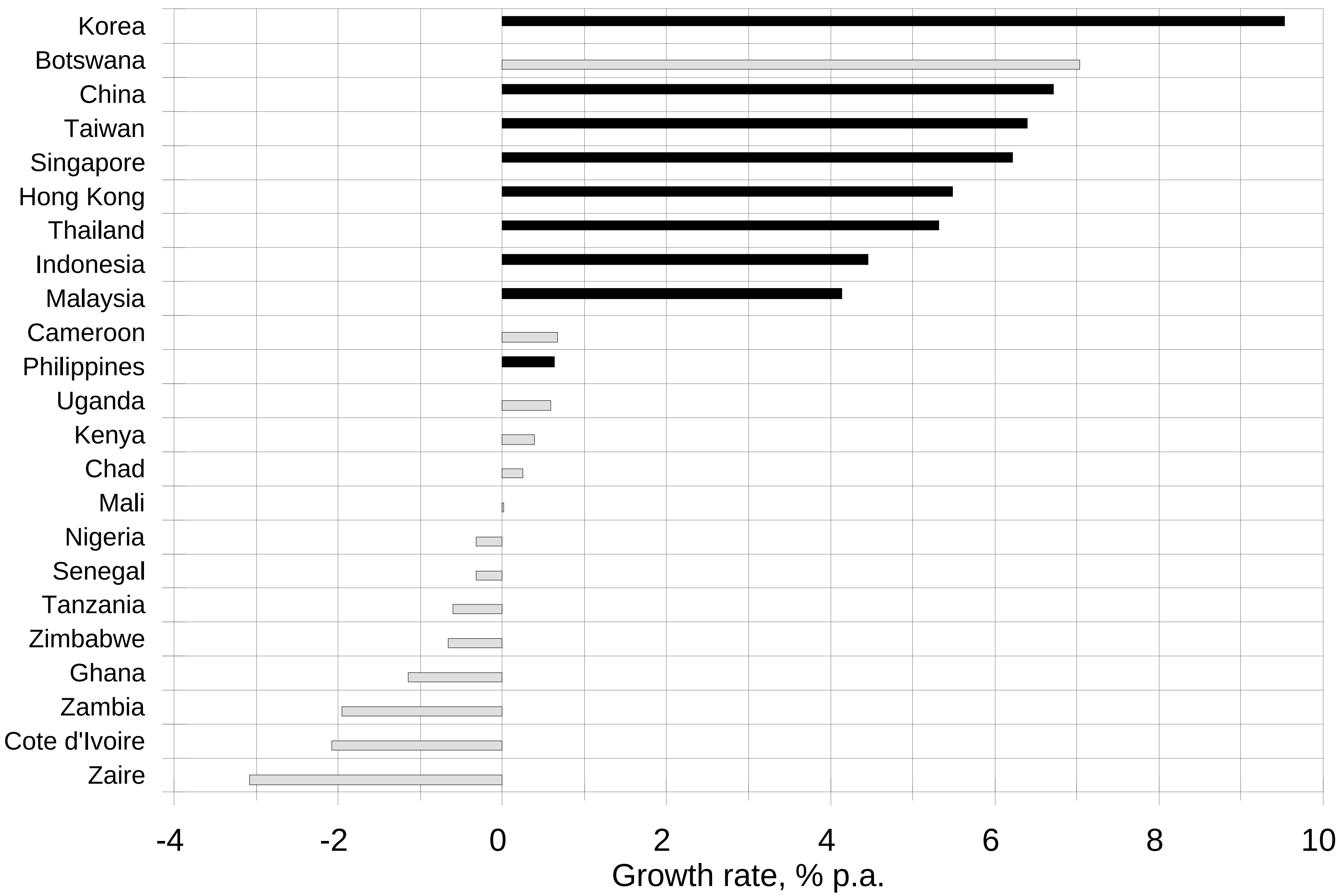

Figure 2: Growth vs. Investment Rates
Average, 1973 to 1993, Percent of GNP

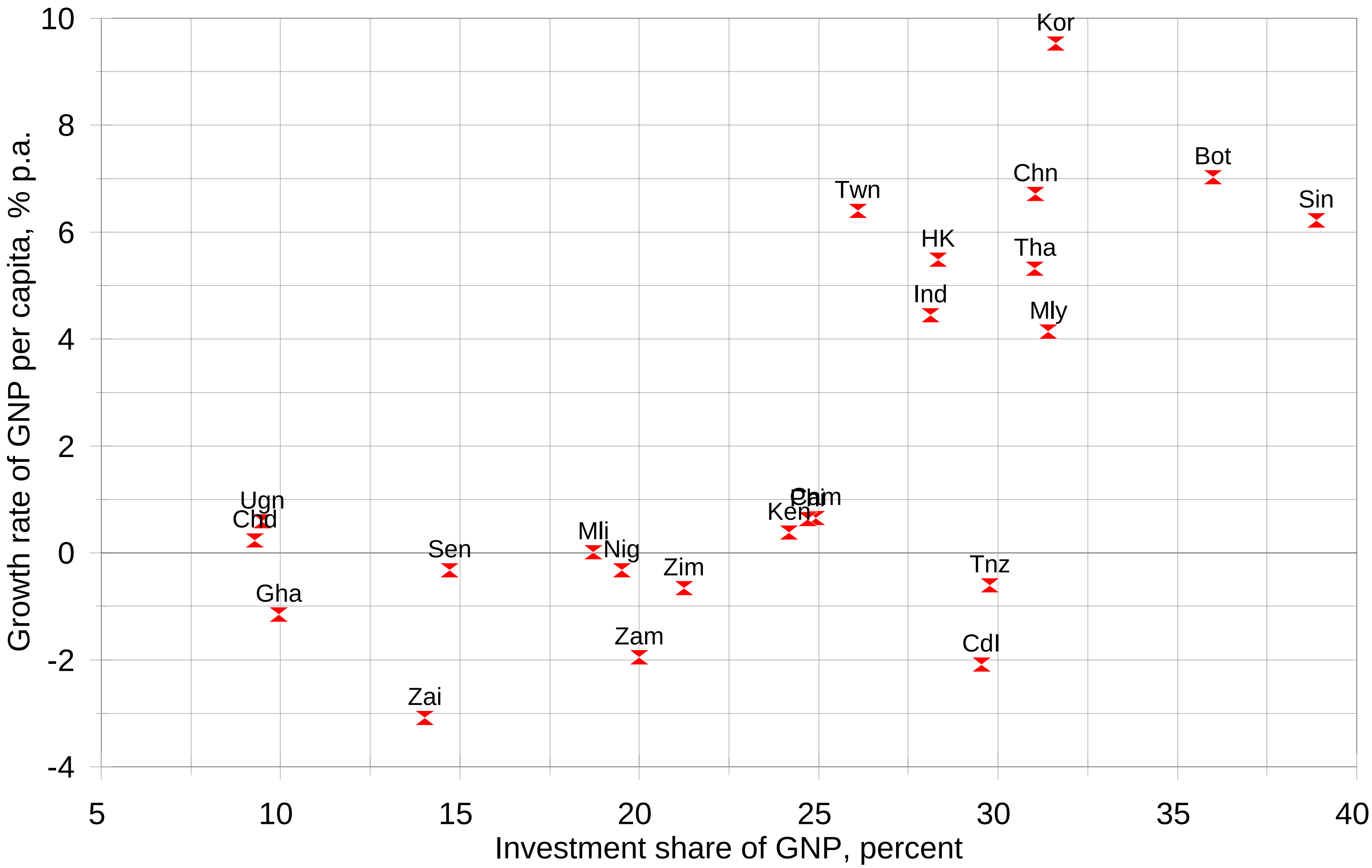

Figure 3: GNP vs. Human Cap. Growth

Yrs of School/Adult, 1960-1985, % p.a.

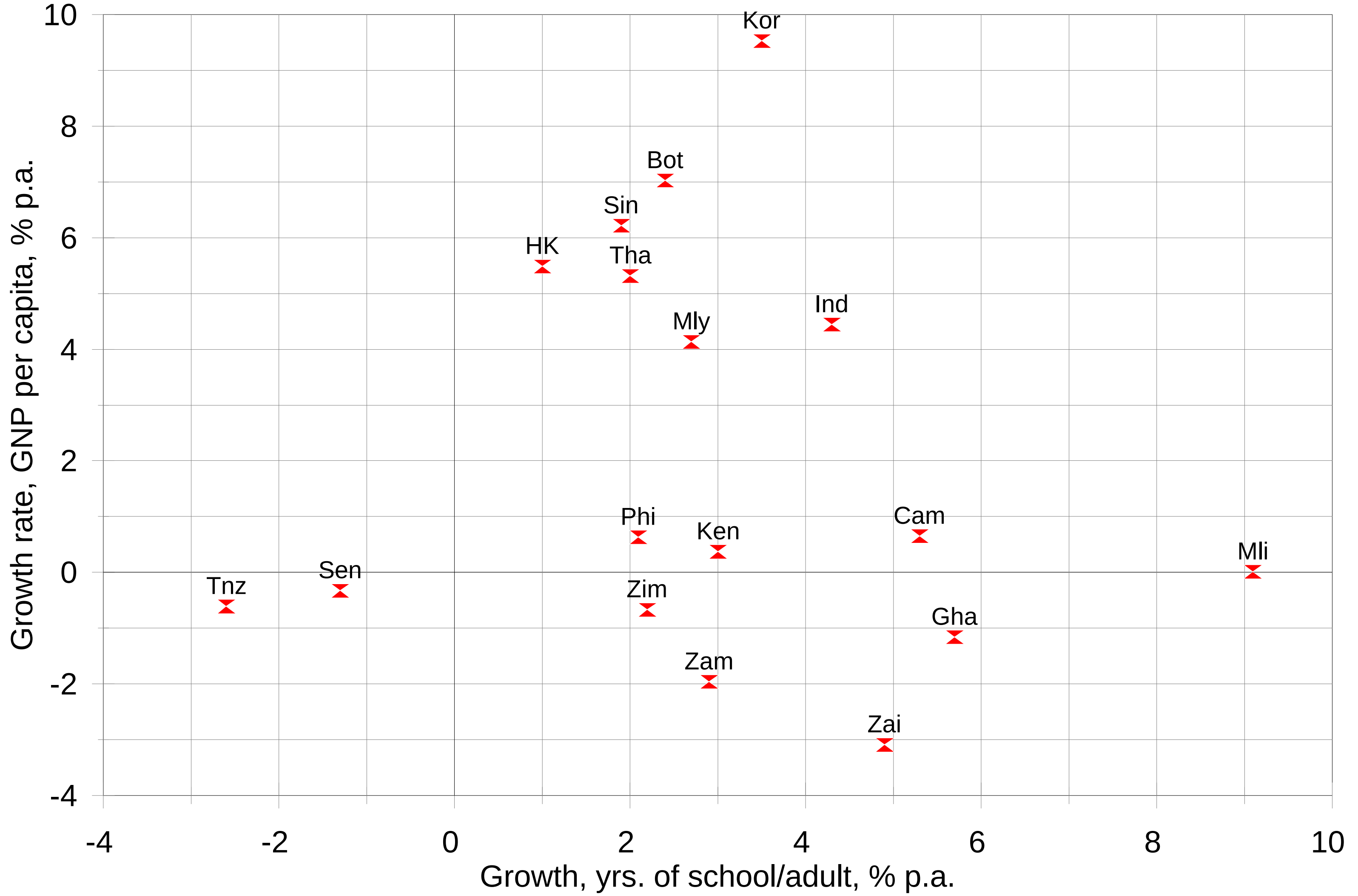

Figure 4: GNP vs. Export Growth
Dollar Exports, 1973 to 1993, % p.a.

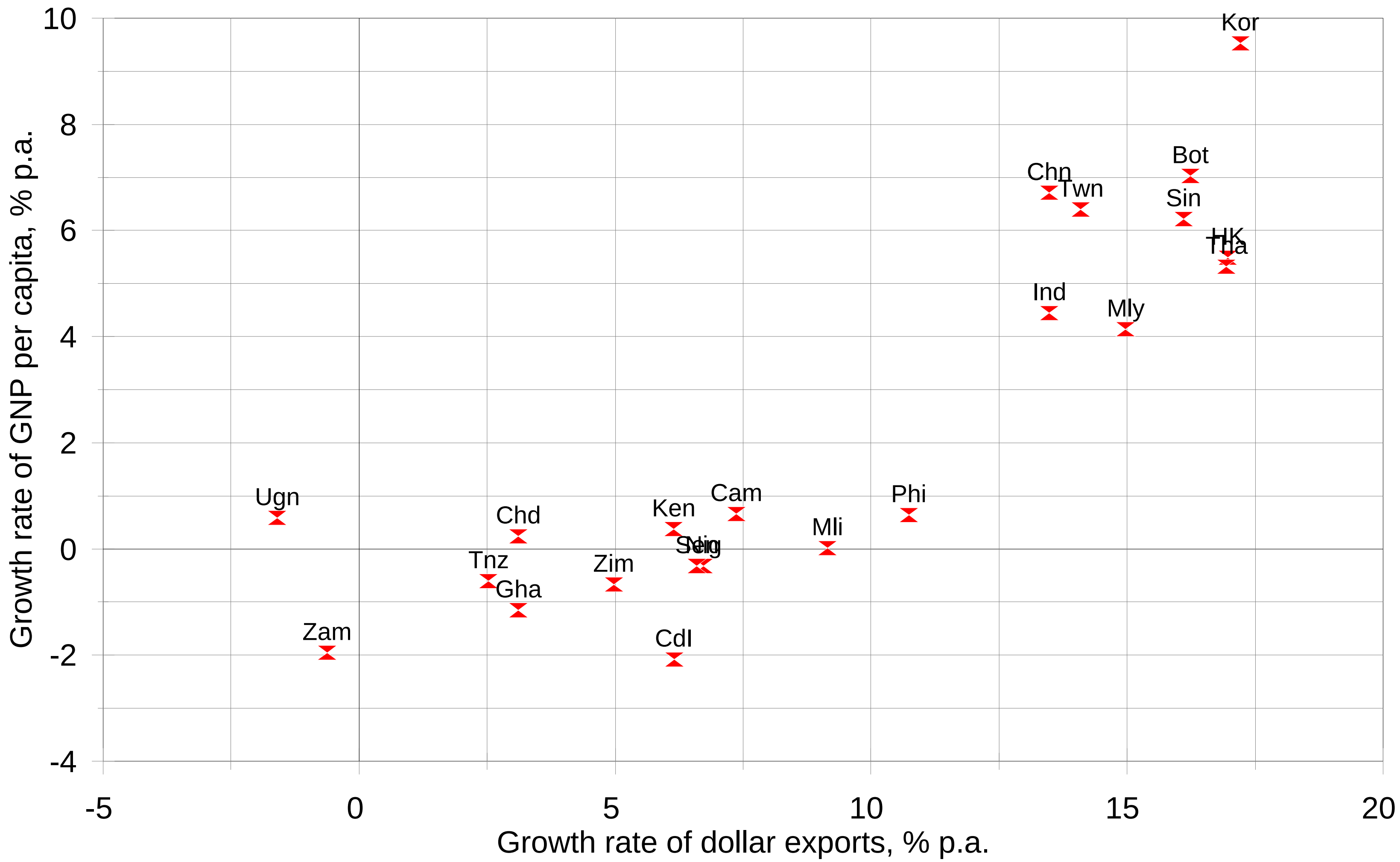

Figure 5: Average Years of Education
Asia: 1960; Africa: 1985

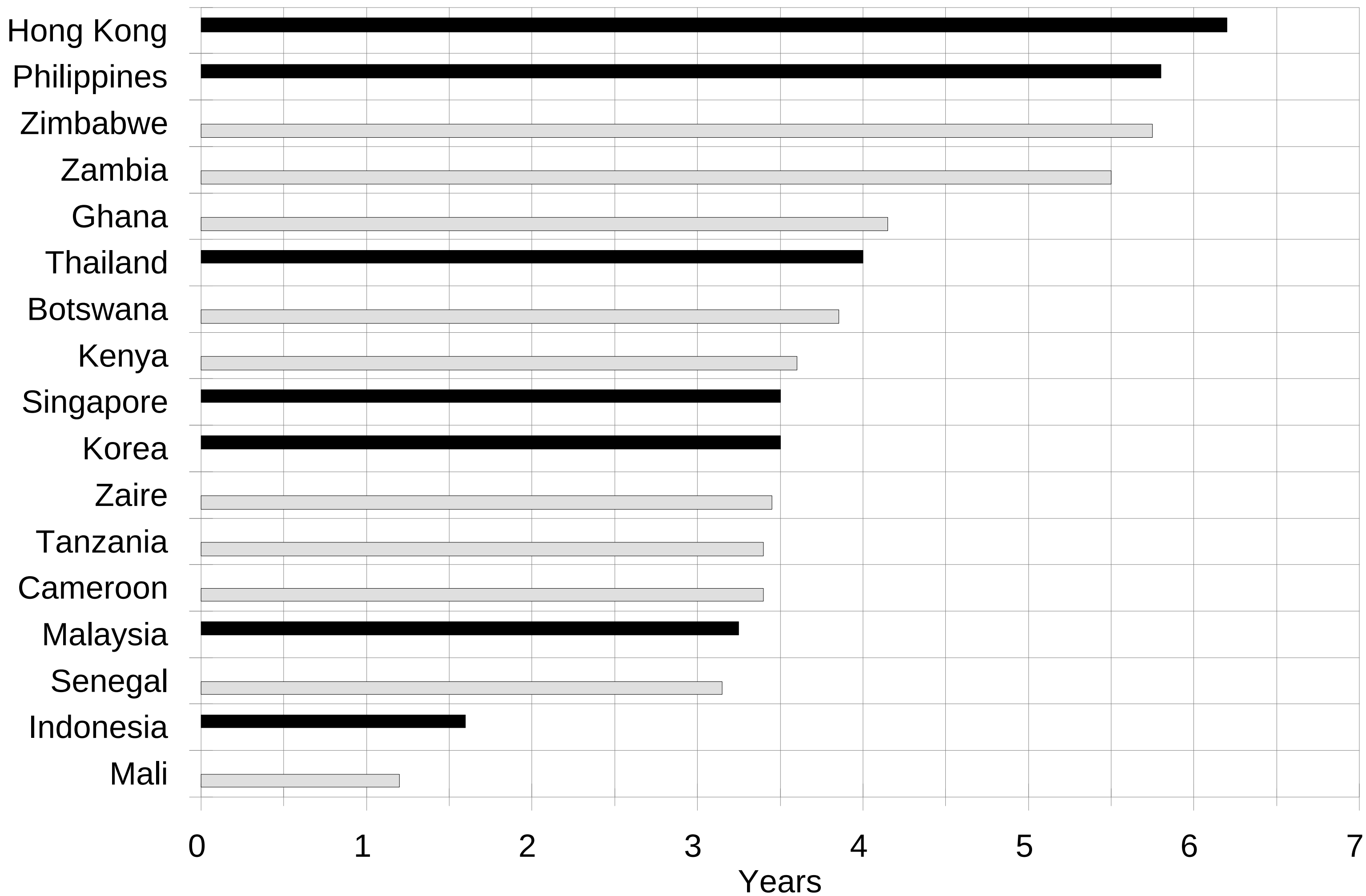

Figure 6: Growth vs. Exchg. Rate Prem
1985 to 1993

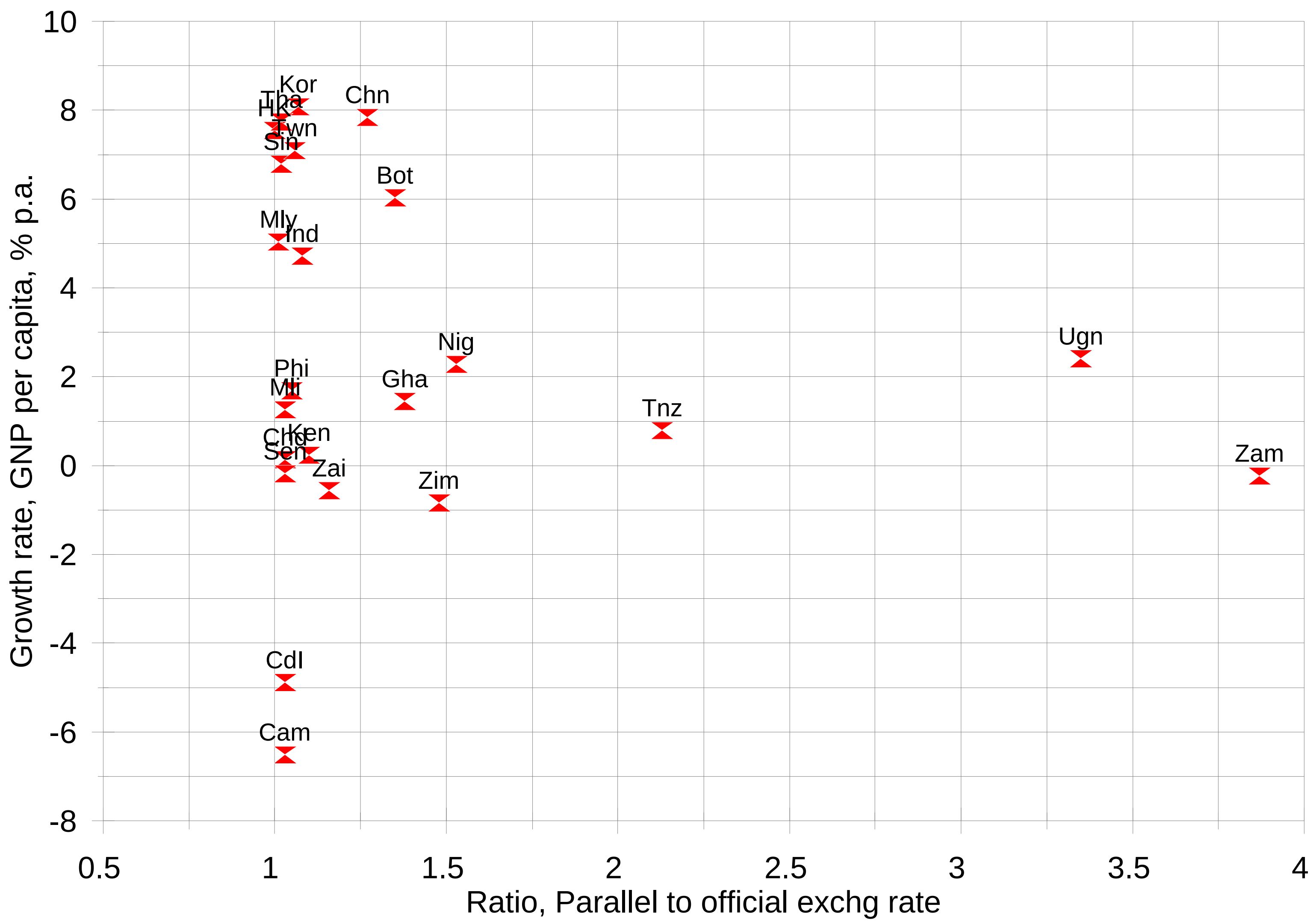

Figure 7: Growth vs. Budget Surplus

Average, 1985 to 1993, Percent of GNP

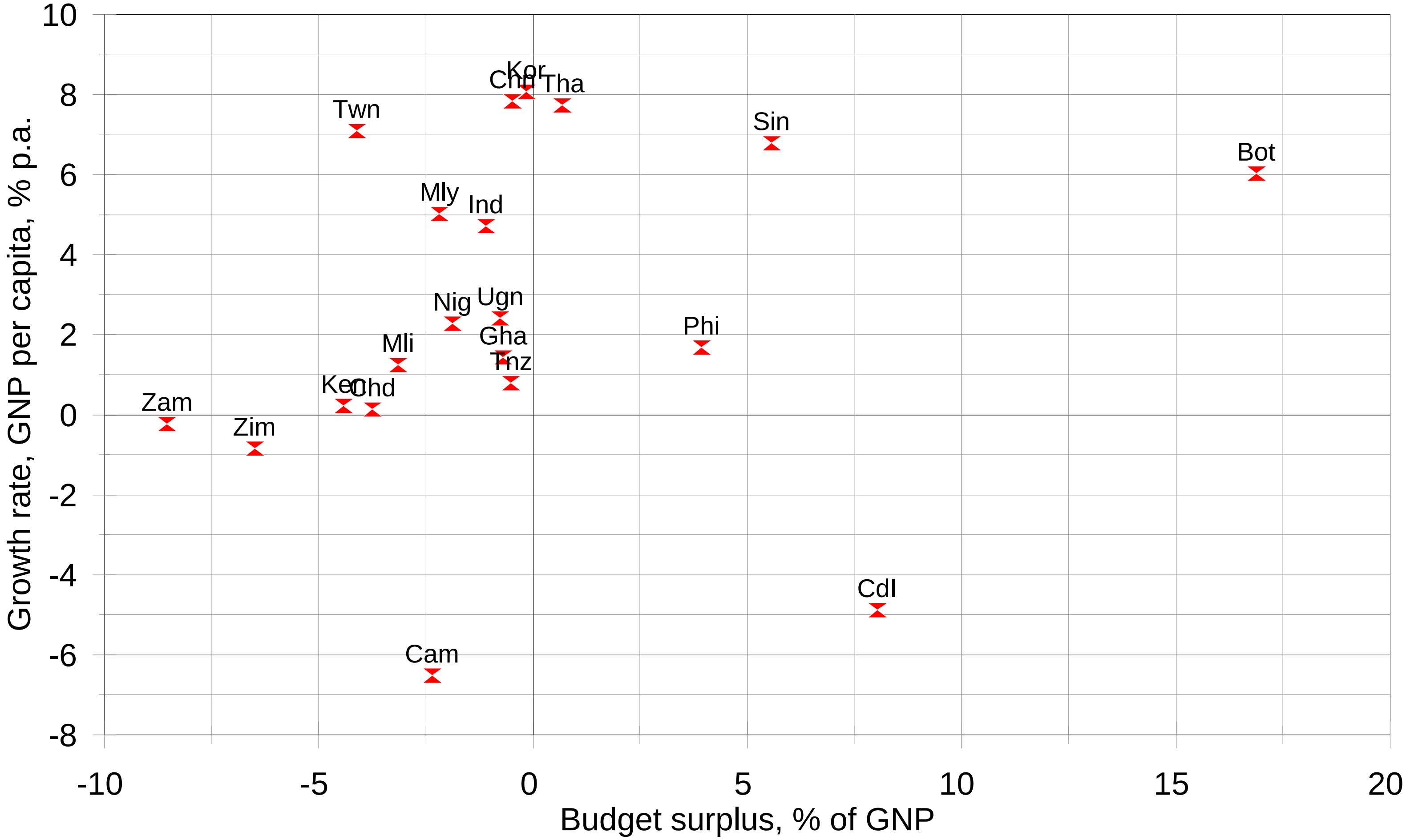

Fig. 8: Deficit Financed by Cen. Bank

Average, 1985 to 1993, Percent of GNP

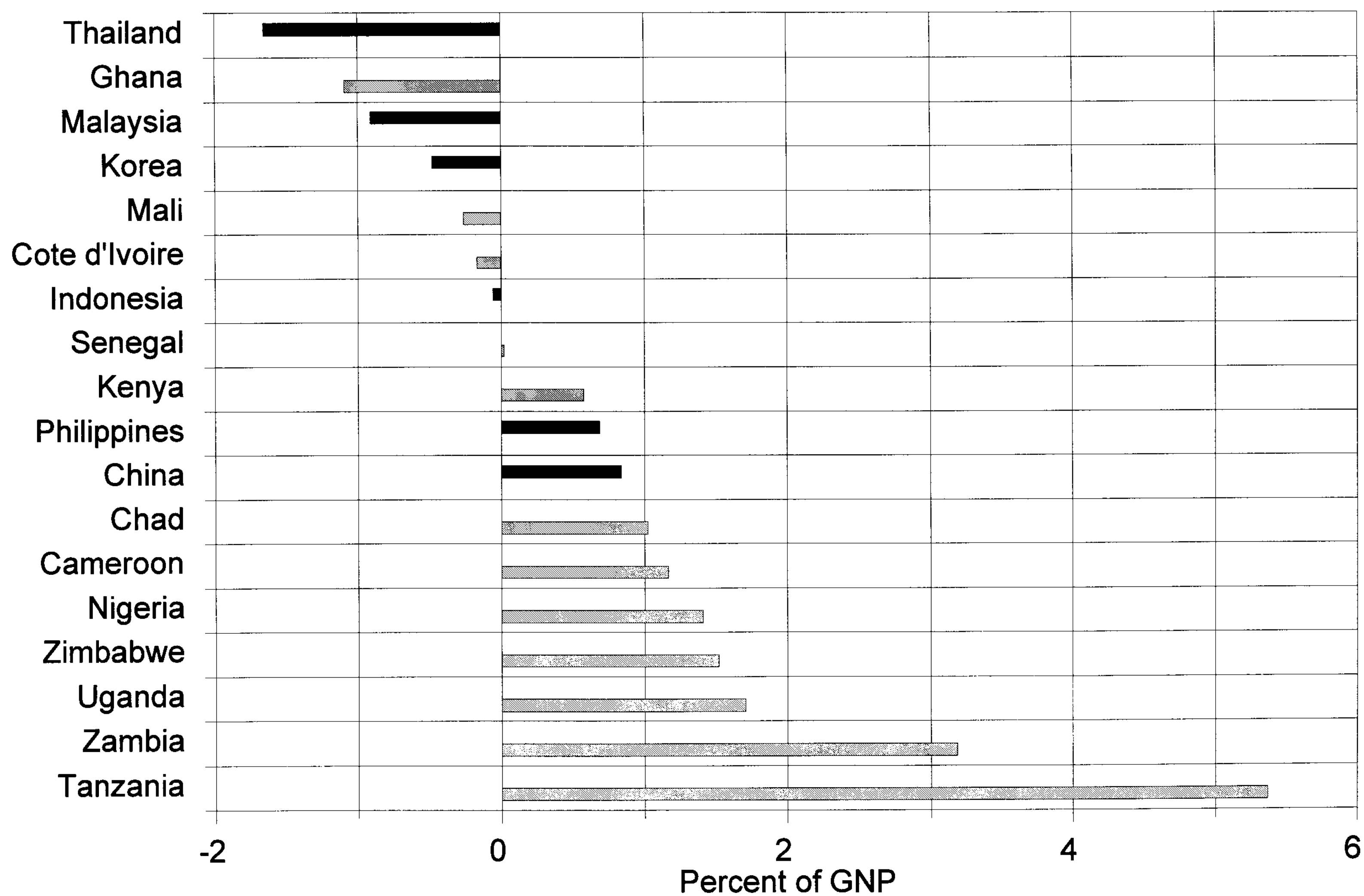

Figure 9: Growth vs. Inflation
1985 to 1993

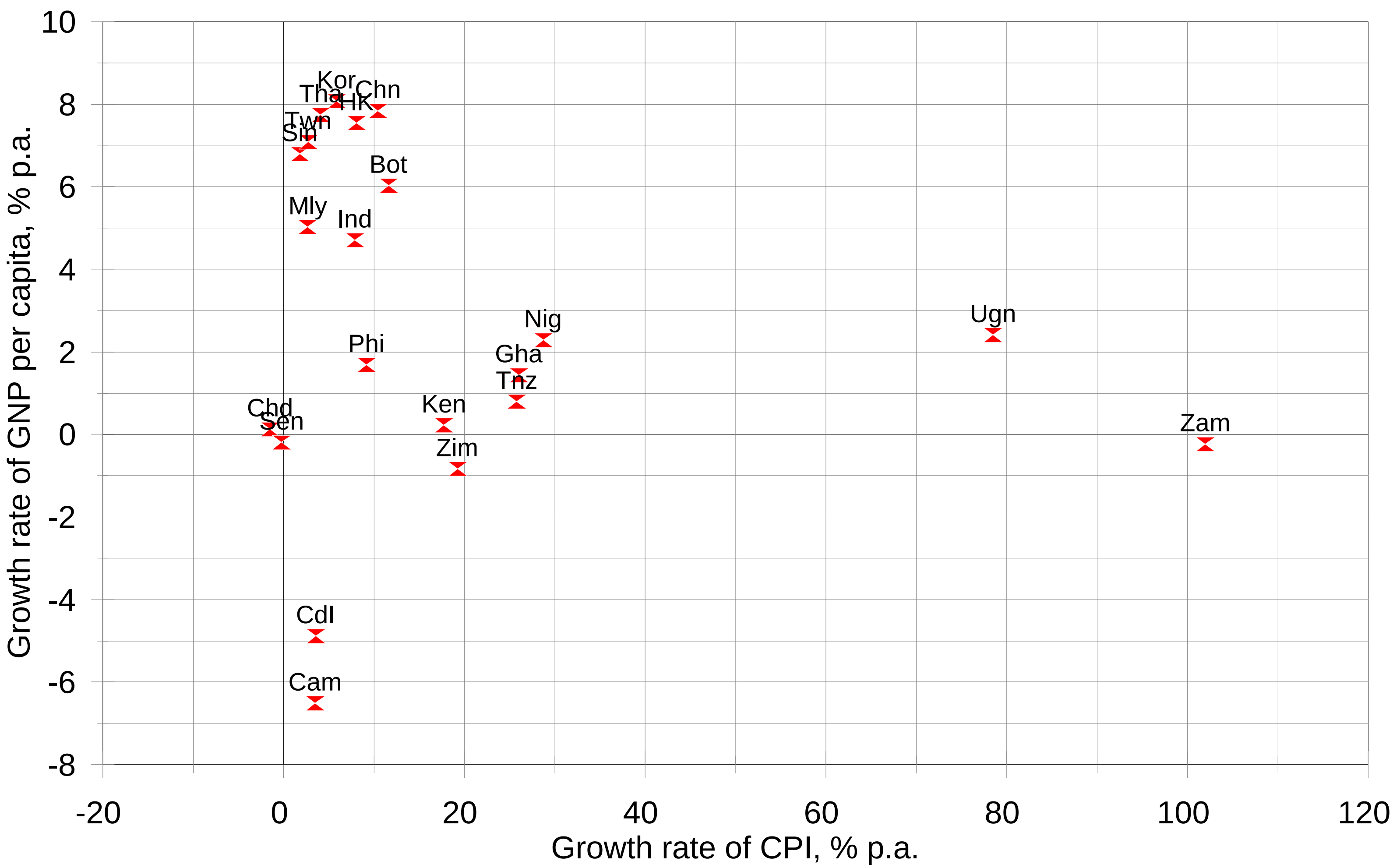

Figure 10: Real Interest Rates, Loans
Average. 1985 to 1993, % p.a.

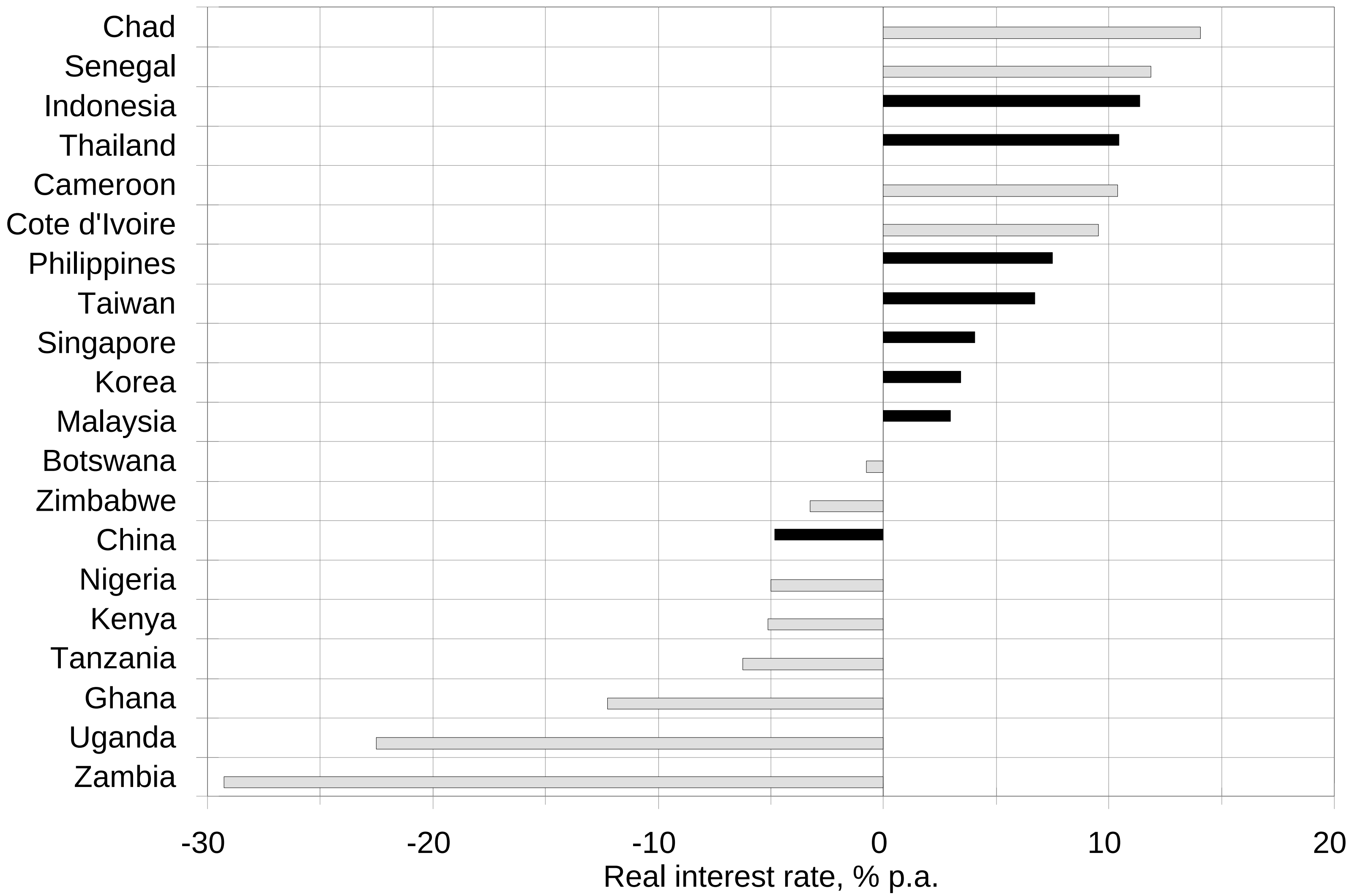

Figure 11: Price Deviations from PPP
Coefficient of Variation, 1970s