EAGER Policy Brief

NUMBER 29 / JANUARY 2000

A Pragmatic Approach to Policy Change

African governments and international agencies are now approaching their third decade of attempting to promote economic reform across the continent. Opinions vary on whether the effort has had a positive impact. Some groups argue that Africa is "on the move." Others reach the opposite conclusion pointing to the unserviceable debt, continuing civil strife, and deteriorating social indicators. Still others attempt to tread a middle path.

One factor that has become increasingly clear, however, is that progressively deepening and broadening the development agenda in Africa has largely been counterproductive. Most governments have compounded the difficulties by reaching well beyond their administrative and financial capacities. None of the changes made since the reform efforts began in the late 1970s enables African governments to better handle the agenda. This policy brief examines the types of changes allowing African governments to simplify their agendas in ways that help promote growth and development.

In light of widespread economic decline, the principal goal of most African governments should be to return their economies to sustained growth paths. Accomplishing this will require several clearly identifiable actions. How each of them is phased will change over time as existing policies are implemented, organizations are reformed, and external circumstances change. The actions include:

• bringing the macroeconomic data up to date so that economic policy can become pro-active;

• restoring (or imposing) budget discipline even if, during the initial stages, this requires a brute force mechanism like a "cash budget";

USAID

Equity And Growth through Economic Research– an activity of USAID, Bureau for Africa, Office of Sustainable Development, Strategic Analysis Division

EAGER

• begin removing the restrictions and regulations that provide opportunities for corruption and inhibit enterprise and initiative;

• take positive measures to minimize public enterprise losses by opening restricted markets to competition, accelerating privatization, or negotiating management contracts;

• restraining the expansion of the public service through staff retrenchment, civil service reorganization, keeping wage increases below the rate of inflation, or a hiring freeze;

• reforming the tax and revenue system; and

• focusing attention on improving infrastructure — roads, bridges, railways, airports, hospitals, schools, rural food storage, water and sanitation systems, garbage disposal, and urban drainage.

Both experience and research provides ample justification for this list.

Without current, broad-based data, a pro-active economic policy is impossible. The best that any government (or central bank) can do is react to events as they unfold. Current data enable policymakers to anticipate potential problems and, even if they cannot be avoided, responses can be designed to ameliorate their effects.

Budget discipline is essential for all African countries. There is now a rich literature tracing many of Africa's economic difficulties over the last three decades to financial excess in the public sector. For the future, sustained growth and development will continue to be elusive while governments run deficits. Indeed, while deficits persist there can be no end to Africa's debt problems no matter how generous the various debt relief proposals become.

Removing restrictions and regulations that inhibit enterprise and entrepreneurship is one area where African governments can achieve "stroke-of-the-pen" changes. These can have a profound effect on economic prospects. Examples include the removal of import and export licenses, eliminating exchange controls, ending parastatal monopolies on production and distribution of particular commodities, removing prohibitions on the inter-regional movement of goods, lifting price controls, and eliminating interest rate ceilings and directed credit.

Reform of public enterprises is essential as a means of reducing the public sector deficit, ridding the economy of value-subtracting activities, and expanding opportunities for the private sector. This is one area where the goals of achieving budget discipline and removing restrictions that inhibit enterprise and entrepreneurship overlap.

There has been much comment about the inefficiency and over-staffing of African civil services. With few exceptions, African governments have too many ministries, with too many departments, and too few staff capable of fulfilling their over-extended (and often conflicting) mandates. Rationalization and reduction in this area is long overdue.

Tax reform is an element of improved budget discipline but because of its importance some additional emphasis is warranted. Key elements in any tax reform include the modernization of the tax code, the introduction of more efficient taxes (such as a VAT) that fall on consumption rather than investment, and special efforts to broaden the base, reduce the rates, and eliminate loopholes. A further requirement is a major effort to improve tax compliance.

There are two reasons for having the government focus on infrastructure development. First, infrastructure provides the foundation for rapid economic growth. Well-maintained infrastructure keeps operating costs low for both the public and private sectors. Second, the services derived from (most) infrastructure development are public goods. These services will not normally be provided without public support.

The above program touches upon all areas of the economy: the budget, monetary policy, the financial system, the management of public enterprises, the control of productive assets, the reorganization of the civil service, repair of basic infrastructure, strengthening of economic institutions, and the revamping of social sector programs. None of the policy changes will unfold in a neat (pre-determined) sequence. Once underway, policy reform in these areas will require a variety of additional changes.

A key part of this process is that the government recognizes, as a practical matter, the need for timely and decisive policy responses which build upon (and modify) the effects of earlier policy changes. None of these measures is easy to implement. For example, civil service reform has always been contentious and progress (if any) slow. African governments find action in this area difficult to implement and sustain. Civil servants are not only politically powerful but typically they are the very agents who have to promote reform.

Nonetheless, experience has shown that policy reform can gain momentum as changes in one area can stimulate (or force) changes in others. For instance, the use of a cash budget is an excellent means of forcing improvements in revenue collection. With the government committed to limit its expenditure to revenue raised, the problem of low tax compliance begins to stand out. Governments wishing to raise their expenditure find that they must raise additional revenue. This places a premium on raising tax compliance.

An evident feature of the above steps is that none of them deals with the environment or community development, or numerous other elements that donor agencies have added to the development agenda over time. None of these has been excluded gratuitously. Their absence simply reflects the fact that most African governments can do little, either organizationally or institutionally, to "promote" these areas.

Until reform takes hold and governments re-build their capacities and reputations for prudent action, these areas are better left alone. Doing this may involve some market failures. Experience has shown, however, that these failures have significantly lower social costs than those associated with the bureaucratic failures when governments attempt agendas that are well beyond their capacities.

This policy brief is based on EAGER Research, *Restarting and Sustaining Growth and Development in Africa,* 2000, by James S. Duesenberry [duesenb@fas.harvard.edu], and Malcolm McPherson [mmcphers@hiid.harvard.edu], Harvard Institute for International Development, Cambridge, Massachusetts.

To Order Policy Briefs or Other EAGER Publications

(all EAGER publications are free of charge to residents of Africa)

EAGER Publications/BHM
1800 North Kent Street, Suite 1060
Arlington, Virginia 22209
tel/fax: 703-741-0900/703-741-0909
e-mail: spriddy@eagerproject.com

All EAGER Publications can be downloaded from www.eagerproject.com