

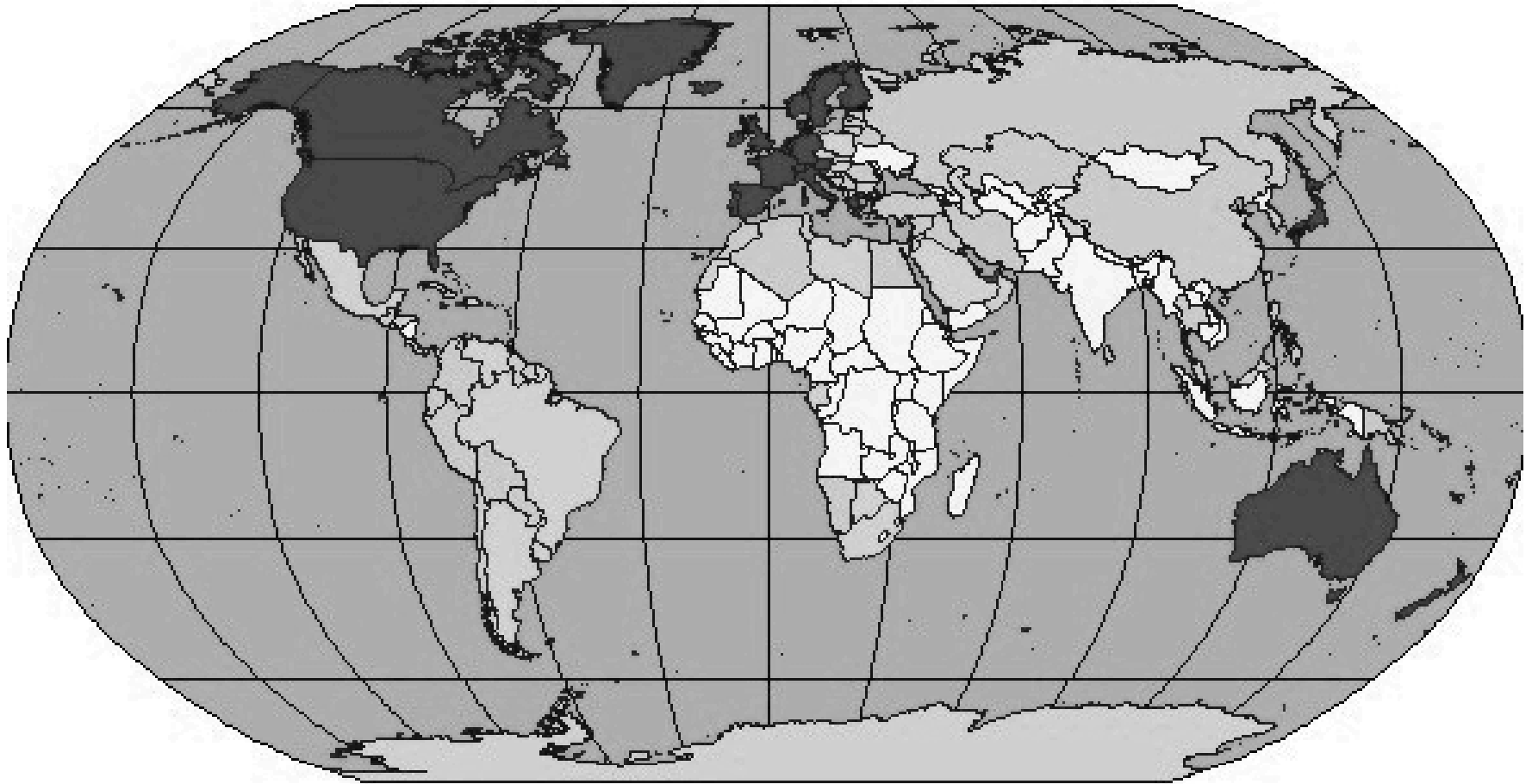
Productivity Growth: The Key to Poverty Reduction in Africa

African Growth and Opportunity Forum

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1.3 billion people, less than **\$1** per day
 $\frac{1}{2}$ world's population, less than **\$2** per day
U.S. average, nearly **\$100** day. **Why?**

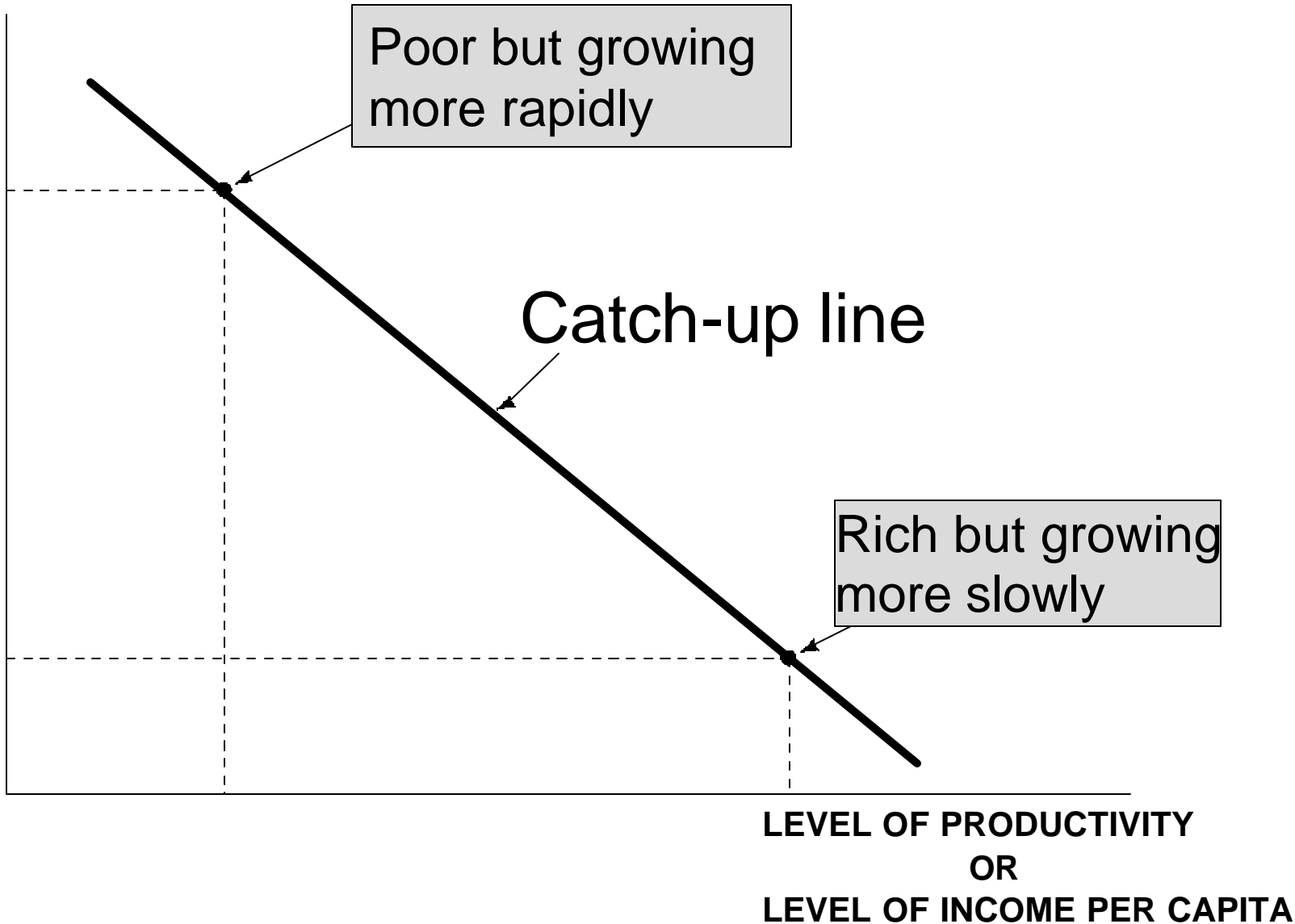
Answer: Productivity Is Low

- *Productivity = output (Y) per hour of work (L) = Y/L*
 - Sometimes called labor productivity
- It's “the explanation” why some countries are rich and other countries are poor
- Countries with few high productivity jobs are poor
- Creating more high productivity jobs—productivity growth—is the only way to reduce poverty.

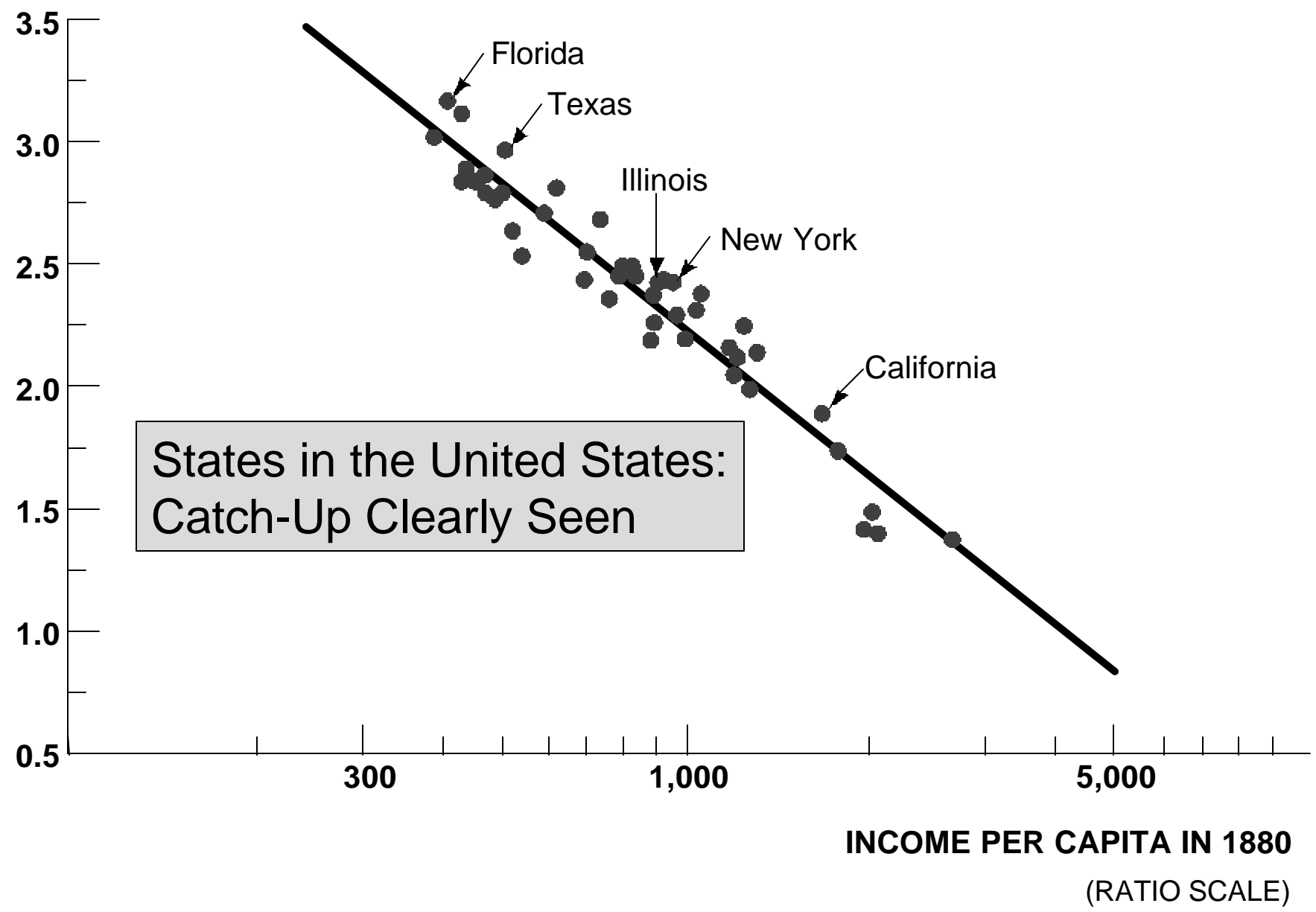
But Why Is Productivity So Low In Poor Countries?

- Productivity (Y/L) depends on:
 - **capital** (K/L) and **technology** (T)
- If there are no impediments to the spread and use of *capital* and *technology*, then countries behind in productivity should **be catching-up**
- Capital and technology would go to where they are relatively scarce because the returns are so high

**GROWTH RATE OF
PRODUCTIVITY
OR
GROWTH RATE OF
INCOME PER CAPITA**

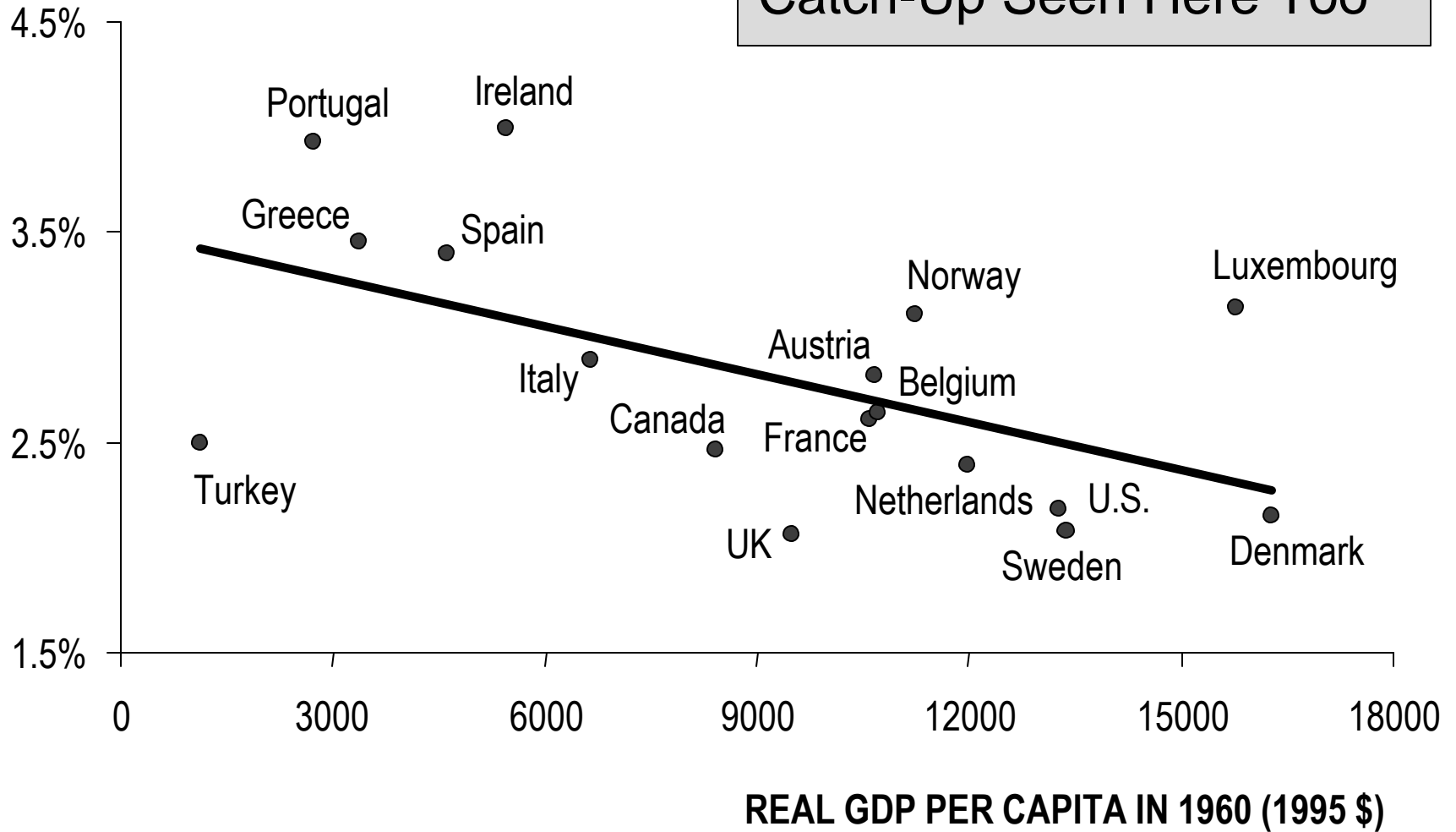


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**GROWTH RATE OF
INCOME PER CAPITA, 1880-1980**



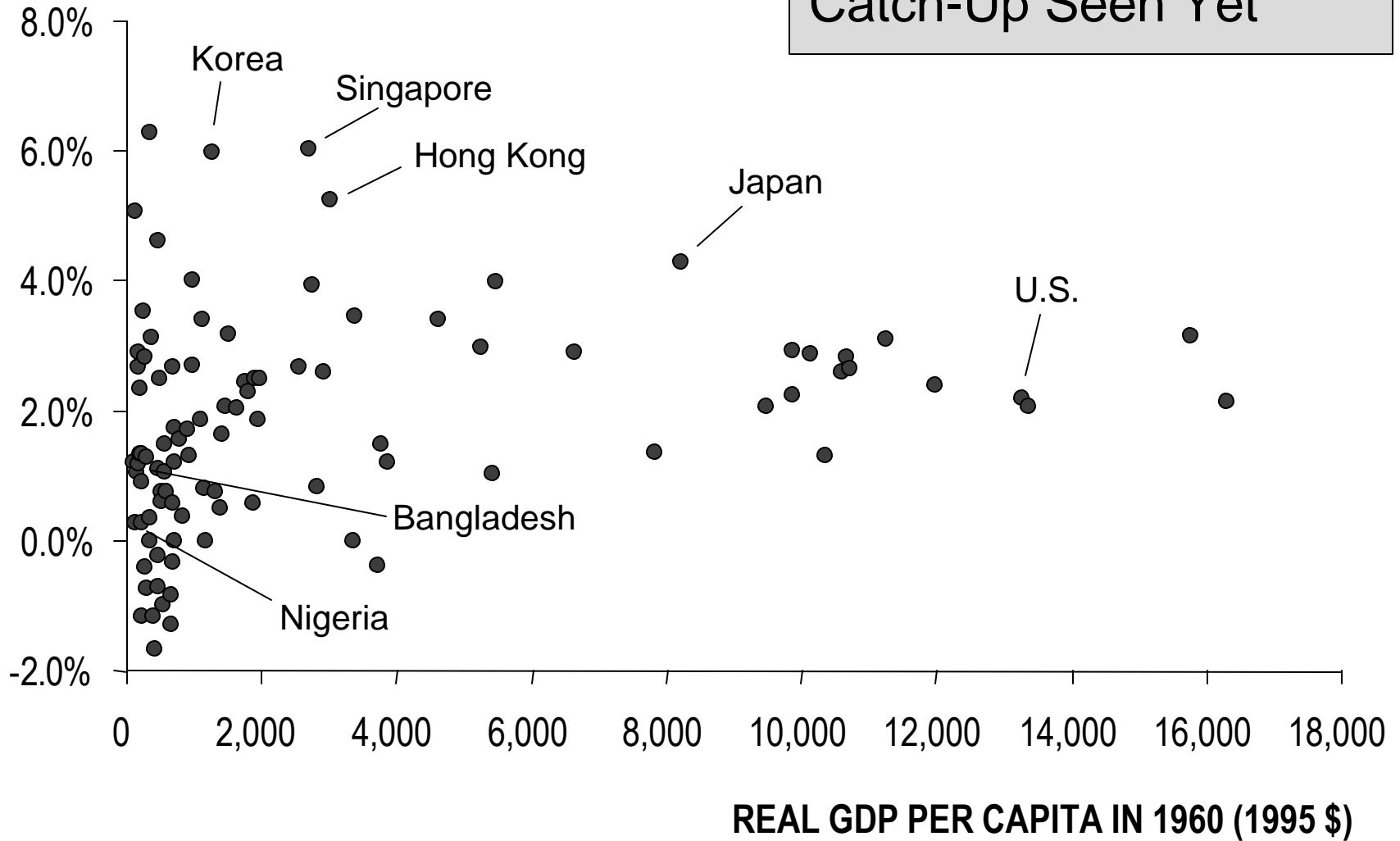
ANNUAL GROWTH RATE OF REAL GDP PER CAPITA, 1960-1999

More Advanced Countries:
Catch-Up Seen Here Too



ANNUAL GROWTH RATE OF REAL GDP PER CAPITA, 1960-1999

All Countries: Not Much Catch-Up Seen Yet



Recent Productivity Trends (1990s)

• East Asia	5.5
• United States	2.1
• Europe	1.2
• Latin America	0.7
• Middle East	-0.1
• Sub-Saharan Africa	-0.5

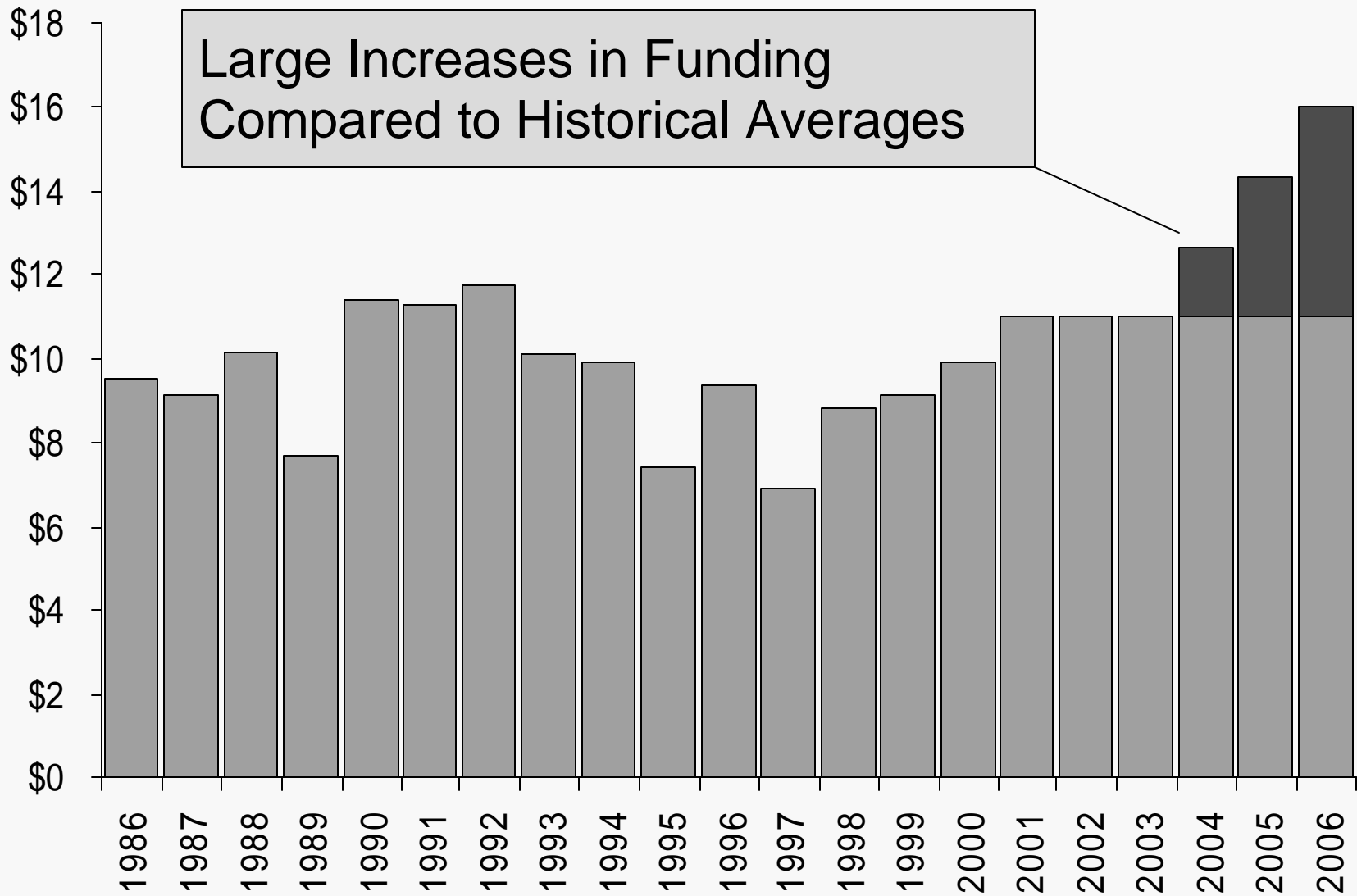
Why Isn't There More Catch-Up

- Poor governance
 - weak rule of law, corruption
 - creates disincentives to invest, to start up new firms, to expand existing firms
- Poor education
 - reduces human capital
 - impedes adoption of new technologies
- Restrictions on economic transactions
 - lack of openness to trade, state monopolies, and excessive regulation
 - reduce incentives for innovation and investment needed to boost productivity

The New Foreign Aid Agenda

- **Increase foreign aid**
 - (1) Funding for Millennium Challenge Account to increase to \$5 billion a year by 2006 — a 50% increase over and above existing U.S. development assistance
 - (2) Contribution to World Bank's International Development Association (IDA) increase by 18%
 - (3) Larger fraction of IDA aid in form of outright grants rather than loans
- Let **good performance** determine which countries get aid for economic development
- Insist on **measurable results**

U.S. OFFICIAL DEVELOPMENT ASSISTANCE US\$ BILLION, 1986-2006



ODA held constant in 2001-06 for presentational purposes

Good Policy Performance is Part of the Millennium Challenge Account

- “Ruling justly”
 - lack of corruption, rule of law
- “Investing in people”
 - good education and health policy
- “Encouraging economic freedom”
 - good trade and macro policy

Measurable Results Are Part of IDA-13

- U.S. Contribution to IDA up by 18%
 - Year One: \$850 million
 - Year Two: \$950 million
 - Year Three: \$1,050 million
- Each \$100 million increment in year two and three depends on measurable results
 - time to start up a business,
 - measles immunization,
 - primary school completion rates.