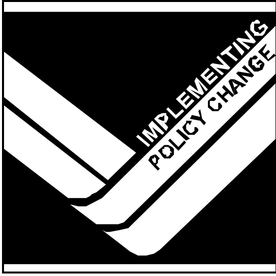


# Working Papers

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# SUSTAINING ECONOMIC REFORM IN SUB-SAHARAN AFRICA: ISSUES AND IMPLICATIONS FOR USAID

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## Introduction and Overview

This paper examines a range of issues involved in the sustainability of economic reform in the new political circumstances evolving in sub-Saharan Africa. The paper draws from a range of disparate sources: literature on the politics of economic reform, both in Africa and elsewhere in the developing world; literature on the transition to democracy, which focuses predominantly on Southern Europe and Latin America; various assessments of the impact of structural adjustment in Africa, including both program and project evaluations and broader cross-national and aggregate studies; literature on governance in Africa; and on-going coverage, largely journalistic, of the process of democratization in Africa.

The paper is a direct follow-on to the analysis initiated in "Beyond Policy Reform in Africa: Sustaining Development Through Strengthening Entrepreneurship and the Non-Governmental Sector," (Gordon 1991). The current paper focuses on the interplay between the economic/technical and the political dimensions of reform, and on how AID operations might more effectively promote the sustainability of reform.

Section One briefly reviews both the background to "top-down" policy reform efforts and how adjustment themes came to play a more serious role in African policy agendas in the late 1980s. Section Two examines the results of economic reform in Africa and discusses why they have been relatively disappointing, focusing on the phenomenon of partial reform, the inter-related problems of weak markets and weak states, and the ambivalent role that donor support has played. Section Three addresses the political economy of structural adjustment, making transparent the implicit political model followed by the donors and discussing how adjustment undermined the existing pattern of politics and governance. It also discusses why CFA countries are highly unlikely to sustain economic reform in the absence of changes in the franc zone monetary arrangements. Section Four explores the new political environments emerging in Africa, arguing that democratization provides new opportunities for economic reform and emphasizing the

inter-dependence between political liberalization and economic reform. Section Five sets out four key dimensions for facilitating the sustainability of economic reform: 1) enhancing civil society; 2) establishing the institutional foundations for markets; 3) changing the role of government; and 4) improving technical capacity, especially in the area of policy implementation. Section Six presents the implications of the analysis for AID operations, discussing options for how AID might respond to the new political environment in ways that will facilitate the sustainability of economic reform.

## Section One: The Background and Context of Adjustment

In the course of the 1980s, two-thirds of the countries of sub-Saharan Africa initiated economic reform programs. The domestic context for the initiation of policy reform was the deepening economic crisis generated by changing international economic conditions and by the failure of the development strategies and policies implemented by virtually all African governments in the two decades following independence. These development strategies had emphasized: 1) the leading role of the state as the engine of economic growth and development; 2) the primacy of industry over agriculture, and the creation of a thorough-going import substitution regime to promote industrialization; and 3) a pervasive hostility to the private sector and to the market as an allocation mechanism.

This development strategy was followed with a vengeance in a set of countries ideologically committed to socialism. Thus, in Guinea, Ghana, Tanzania, Ethiopia, Angola, Mozambique and Madagascar, the state took over banks, trading companies, supply networks for agricultural inputs and outputs, and sought to re-define the structure and organization of both agricultural and industrial production. In virtually all of these countries (Tanzania is a partial exception), economic development was an unmitigated disaster and led to a process of mutually-reinforcing economic and socio-political decline.

What was less clear until later was that even in the African countries which followed a much milder version of the strategy (states such as Kenya, Cameroon, Cote d'Ivoire, Senegal and Malawi), the impact of such a strategy, over time, was to limit the possibilities for growth and to generate an unsustainable current account deficit. Thus, the countries that in the African context were "high growth" during the 1960s and 1970s lagged well behind even modest achievers elsewhere in the developing world, and were highly vulnerable to external shocks and subsequent economic downturns.

In almost every sub-Saharan African country, these development strategies were married to a particular authoritarian regime-type, what the eminent political scientist Richard Sklar has termed the development dictatorship. African development dictatorships promised effective economic performance and rising living standards through state-centred development and heavy regulation of the private sector. In return, they claimed the right to maintain a centralized and authoritarian system of governance.

For the mass of the population, the negative economic impact of the development strategies followed by governments was mitigated by the often very successful efforts by African producers and traders, especially in the rural areas, to develop parallel markets. These parallel markets tended to be most extensive in sectors in which governments tried the hardest to pre-empt market forces, and in countries in which state capacity eroded most rapidly. Ironically, the more African states attempted to impose controls, the more their actual ability to influence and direct the economy diminished, as the informal economy expanded. The most important signal of this loss of state capacity was the weakening of the tax base. Parallel markets were particularly important in foreign exchange markets, urban food markets, and cross-border trade. The development of parallel markets and the informal economy was a successful popular defensive strategy in the context of predatory states and "dirigiste" economic policies; it maintained incentives for production, generated income, and ensured continued provision of the goods and services central for survival.

But the trajectory of private sector development into the informal sector does not provide the context for dynamic economic growth. The informal sector is marked by high transaction costs and other losses associated with avoiding participation in the official economy. Businesses tend to remain small and are usually unable to generate economies of scale and the technical improvements needed for dynamic industrial upgrading. In the formal sector, business confidence is eroded, leading to capital flight and the expansion of rent-seeking, rather than efficiency-seeking, behavior. Capital markets deteriorate. While the informal sector is an important and dynamic part of African economies, it is important to recognize that nowhere has the informal sector formed the basis for rapid and sustained economic growth. It is unlikely to do so in Africa.By the early 1980s, in the context of international recession, most African countries faced economic

crises defined by both an inability to generate foreign exchange to purchase vital imports and an inability to generate budget revenues to support civil service salaries, provide government services, and maintain infrastructure. In these circumstances adjustment was inevitable. In general, African countries faced two broad alternatives. They could either undertake "ad hoc" adjustment, further tightening controls over foreign exchange while increasing the domestic money supply to generate an "inflation tax" to increase government revenues; or they could pursue coherent stabilization and adjustment programs aimed at restoring domestic and external imbalances. The inclination of virtually all African governments was towards the former; what made the latter attractive was less the substance of what it proposed, and more the fact that it had extensive donor resources -- from the IMF, World Bank, and bi-lateral donors -- attached to it. More than anything, financially-strapped African governments needed resources; that is why donor-supported adjustment programs became attractive to them. The quest for resources, rather than the quest for adjustment, drove the early phase of economic reform in virtually every African country.

Thus ensued the era of "top-down" policy reform as the IMF, World Bank, and bi-lateral donor agencies, especially AID, exerted considerable pressure on generally unconvinced African governments to undertake coherent stabilization and structural adjustment programs. The instrument of external pressure was "conditionality," whereby quick-disbursing non-project loans and grants were predicated on countries committing themselves to undertake specific adjustment measures.

Economic reform programs were initiated at the macro-economic level and in various specific sectors. At the macro-level, the programs concentrated on depreciating over-valued exchange rates and restoring budgetary balance. In the first half of the 1980s, adjustment efforts were sporadic and, at best, half-hearted. For many countries, externally-supported adjustment efforts became part and parcel of the calculus of "ad hoc" adjustment. Programs were entered into and new financial resources were committed by the donors; but when the going got tough, the lure of controls and printing money remained strong. This was especially true for governments with strategic ties to the United States, specifically Sudan, Zaire, and Liberia. These countries effectively leveraged US and other donor funds for "adjustment," while undertaking very little actual reform. Their leaders correctly perceived that their strategic ties to the US would protect them from being cut off despite non-performance. Nevertheless, in the first half of the decade, donor-supported economic reform activities in Africa were important in placing new issues and ideas on the policy agendas and into the public debates in many states, and, in a handful of countries, in initiating real adjustment efforts. This created the base upon which the more serious efforts of the latter half of the 1980s would ensue.

In the second half of the decade, there was a broader and more serious effort at economic adjustment. The economic crisis was deepening and ad-hoc adjustment efforts were themselves predictably unsustainable. A broader group of African economic technocrats became convinced of the necessity of coherent adjustment. Internationally, there was a growing consensus concerning the lack of alternatives to market-based adjustment. At the same time, at least a number of political leaders came to believe that the costs of adjustment might be less than the costs of continued economic decline, especially given the carrot of donor resources for those countries initiating reform. Thus, the tide towards adjustment swung. As the decade of the 1980s came to a close, most African countries were involved in formal adjustment programs supported by the international donors.

The political context of economic reform in Africa has been dramatically altered by the events of the past three years. Already weakened by their dismal economic performance, African development dictatorships became the target of rising popular protest in the aftermath of the revolutions in Eastern Europe and the collapse of communism. The contagion effect of political change has been rapid. In 1989 and 1990, the main affected area was West Africa, beginning with Benin. In 1991, the defeat of President Kaunda in the Zambian election quickly followed by President Moi's capitulation to donor pressures for political reform in Kenya, put political change on the agenda in all of East and Southern Africa as well.

New regimes have come to power in a number of countries, several through genuine multi-party elections. In other countries, the process of political change is at an earlier stage, but appears to be heading in a similar direction. Political change is forcing donors to re-examine their approach to economic reform and to development issues in general. While it is not yet clear where the process of politicalliberalization is leading, there is no question that political factors will be crucial in influencing the sustainability of economic reform.

## Section Two: What Has Been the Economic Response to Adjustment in Africa And Why

In examining the 1980s policy reform efforts of ten representative African countries, David Sahn (1992) and his colleagues at Cornell University found that, "Measured against the failed policies that pre-dated the reforms, considerable progress has been made... both in terms of policy change and performance outcomes." This finding is consistent with that of the World Bank's recent "Third Report on Adjustment Lending," which concludes that policy reform and adjustment support has restored growth in actively adjusting African countries to the "moderate levels" of the 1970s. Both the Cornell and the World Bank studies agree that two elements of structural adjustment that appear to show considerable, and sustained, success in a number of African countries are exchange rate reform and pricing and marketing reform for food crops.

Outside of the CFA zone, virtually all countries that have undertaken donor-supported adjustment programs have succeeded in lowering the spread between official and parallel exchange rates, and, indeed, in depreciating their real effective exchange rate. This is significant since many critics of adjustment had argued that it would not be possible to depreciate the real exchange rate in African circumstances. More recently, there has been a growing trend for countries to go beyond periodic devaluations to establish market-oriented exchange rate regimes, either through legalizing foreign currency trading or through some form of foreign exchange auction.

The importance, both economic and political, of exchange rate reform should not be minimized. The exchange rate is the single most important price in any economy, and over-valued exchange rates distort all other prices. Experience in a range of developing countries has emphasized the importance of exchange rate depreciation to the success of associated trade reform efforts, especially tariff reduction. Politically, exchange rate depreciation and the ending of official monopolies over the allocation of foreign exchange restrict what was one of the most important sources of rent-seeking behavior. They also increase the autonomy of the commercial sector vis-a-vis the state. The ultimate sustainability of exchange rate reform is yet to be secured, however, given that, in virtually all cases, existing exchange rates are maintained by very high levels of foreign aid, while export responses, while varying greatly, have generally been less than expected.

Given the centrality of agriculture in most African countries, the incidence of success in food pricing and marketing reform is also very significant. The impetus to reform of food pricing and marketing policy has been two-fold; first, the increasing financial costs, and second, the diminished political value, of pre-existing arrangements. In some countries, cereals boards ran up massive deficits in trying to defend floor prices that were set too high. Often, marketing boards also became the dumping ground for politically-driven job creation. At the same time, in a number of countries, there was the practical breakdown of the state-dominated marketing channels and the shift of both production and trade into the informal sector. Thus, in many countries, either the political benefits of the old system had already largely worn away, and/or the costs of maintaining those benefits were becoming prohibitive.

One of the most interesting findings of the Cornell study is that raising incentives for farmers has generally not been at the expense of consumers. Part of the reason is that, in many African countries, few consumers in practice had access to officially priced food. Part of the reason is that lower marketing margins generated by increased efficiency throughout the marketing chain has allowed both producers and consumers to gain. It is not surprising, then, that food policy reforms have tended to be politically sustained.

While the successes of structural adjustment efforts in Africa are important, the fact remains that, in many ways, the overall results of economic reform have been less than encouraging; and the sustainability of reform efforts remains tenuous, especially given the new environment of political liberalization. The World Bank concedes that the growth rates achieved for the actively adjusting countries of sub-Saharan Africa (around 3.5% per annum) lag well-behind those for adjusting countries in other regions. Export and savings responses have been weak and, not counting donor-provided resources, investment levels are still exceedingly low. In particular, the private investment supply response that will be needed to sustain economic recovery and growth has not been forthcoming. A group of "adjustment stars" is yet to emerge in sub-Saharan Africa, and adjustment efforts in the best performing countries remain dependent upon extraordinarily large donor transfers (for instance, donor resources comprise between 15 and 20 percent of Ghana's GDP).

A large number of case studies have looked at the evolution of structural adjustment programs in particular African countries. In addition, the World

Bank and several large academic research projects have assessed the general progress of adjustment efforts. Despite the fact that the process of adjustment shows tremendous variation across countries, three interrelated general themes emerge from all of these studies concerning why adjustment in Africa has not yielded more dynamic results.

The first explanation for the relatively weak impact is that the overall context for a rapid supply and investment response to adjustment efforts in Africa is simply not present. This is a result of the general context of underdevelopment. The World Bank argues that a weak human resource base, inadequate and deteriorating infrastructure, weak integration into the world economy, and less diversified economic structures all limit a more dynamic supply response. The data from Africa and other regions is consistent with the hypothesis that the more developed a country, the better it is able to respond to adjustment. Thus, the longer-term success of African adjustment efforts will depend upon addressing these underlying constraints. This suggests that the high expectations that were generated about the impact of adjustment were flawed from the beginning.

A second, and interrelated, explanation of the weak impact of adjustment is that, in Africa, both markets and states are weak and fragile. Several recent World Bank evaluations of their agricultural marketing activities in Africa have stressed that too little attention was played to strengthening the framework within which markets operate. In general, adjustment efforts in Africa have focused on cutting back inappropriate state intervention in the assumption that markets will then operate effectively. But this is not automatically the case. The problems of weak markets and weak states are intimately inter-connected. As Robert Klitgaard (1992) has recently written, “Fair and efficient markets do not occur by accident; they are the product of, among other things, intelligent laws and public policies... For free markets to work better, the government must also work better.” While hardly a radical assertion, Klitgaard's comments go against the assumptions of both free marketers and informal sector enthusiasts, each of whom have focused on freeing economic actors from the clutches of the state; on “exit” rather than on “voice,” in Albert Hirschman's terms.

The third explanation for the limited impact of adjustment is that existing programs have not been very successful in promoting reform in several crucial areas such as fiscal policy and the public service, the regulatory environment affecting private investment, and export crop pricing and marketing. David Sahn, in the Cornell study (1992), concludes that, “In many instances, policy change has lagged behind rhetoric as implementation of reforms has often proved more perilous than planning them.”

Fiscal deficits have proved very difficult to attack, on both the revenue and the expenditure side. Discuss in more detail below are the political origins of fiscal reform failure. Even those countries that have had some success in reducing budget deficits have tended to do so in ways that negatively affect medium and longer-term development potential. In virtually no country has fiscal reform enabled the budget to become a real tool for effectively promoting the development process. Budget cut-backs have tended to target investment rather than consumption, with maintenance being especially neglected. Civil service reform programs have tended to lag far behind schedule, with virtually no success in either cutting the public sector wage bill nor in providing senior technical staff with competitive wage packages.

Reform of the regulatory environment affecting private investment has also been lagging. Several of the case-studies of AID-supported reform efforts in Africa undertaken by the Center for Development Information and Evaluation (CDIE) have emphasized the lack of “complementary measures” in the regulatory environment that have limited the impact of trade reform and industrial sector reform initiatives. In many donor-supported reform programs, there has been detailed conditionality for exchange rate reform and for trade liberalization, while the conditionality for regulatory reform has been limited and fuzzy.

Sahn (1992) contrasts the experience of substantial reform in food crops to that of limited reform in export crops. The origins of this difference lie in export crops continuing role as a major source of taxation revenue for many African governments. While the incidence of export taxation has diminished in many countries, governments have generally viewed that as all the more reason to maintain their ability to tax what they can. Thus, the reform imperative has been much weaker in the export crop sector than it has been in the food crop sector. As a result, the export supply response to adjustment has been limited, generating continued balance-of-payments pressures and import constraint. The lack of success in export crop policy reform has quite serious implications for the overall sustainability of the reform process.

Taken together, the limited extent of reform in the budget and overall public management, in the regulatory regime facing private investors, and in

export crop pricing and marketing, present a picture of reform outcomes substantially less successful than those discussed earlier for exchange rate management and food crop policy. The reform cup in Africa can be thought of as either half full or half empty. But, either way one looks at it, the cup has not been full enough to provide an enabling environment for private investment.

The interaction of three sets of factors - general underdevelopment, the weakness of both markets and states, and the limited extent of reform in key areas - largely explains why the impact of adjustment in Africa, while significant, has been less than what is needed to put Africa back on a track towards sustainable development.

In most sub-Saharan countries that have initiated reform, the dynamics of the reform process in the 1980s led to neither a collapse of adjustment efforts nor to fundamental transformation and dynamic economic growth, but rather to a sub-optimal mix of partial policy measures. What has transpired under structural adjustment programs in Africa is not the transition to a market-driven, private sector-led economy but “partial reform.” In a typical “partial reform” syndrome, a willingness to initiate adjustment measures is not supplemented by the basic institutional and attitudinal changes needed to carry through a transformation to market-oriented and private sector-led growth. Adjustment efforts have some success in eliminating the worst distortions and in restoring low-level economic growth, but do not really transform either policy-making or the overall economic environment.

Partial reform has been particularly problematic in the CFA countries. There, the fact that the nominal devaluation policy instrument is not available has made adjustment much more technically and politically difficult. We earlier discussed the benefits of the exchange rate reforms undertaken elsewhere in Africa. All of those benefits have been denied reformers in the CFA states. The overvaluation and uncertainty attached to the CFA franc directly limits export competitiveness and new foreign investment, while the convertibility of the CFA franc facilitates capital flight. In these countries, the burden of macro-economic adjustment becomes concentrated on the budget, while productive sector reforms are made especially politically unpalatable. Consider briefly the politics of trade reform. In the absence of a devaluation, eliminating quantitative restrictions and/or lowering tariffs immediately threatens much, if not most, of the domestic industrial base. In several CFA countries, including Senegal, this has ignited opposition from both business interests and unions, undermining the adjustment program.

What are the origins of the “partial reform” syndrome. One important factor has been the basic orientation of donor-supported adjustment programs, which focus overwhelmingly on undermining the predatory and neo-mercantilist state in Africa, rather than on facilitating the emergence of the developmental state. But, the transition to a market economy necessitates the more effective provision of public goods. These must include the traditional public goods like social peace, a credible legal framework, physical infrastructure and social services, each of which was so poorly provided by African development dictatorships. African countries also need a whole set of “new” public goods: policies that promote and protect competition, skilled management of the macro-economic framework, an effective capacity to privatize state-owned enterprises, sophisticated regulation of liberalized capital markets, the ability to reconcile development and environment concerns, and a framework for information dissemination relevant to the high-tech era. All of these public goods, both old and new, are in very short supply in Africa. They will remain in short supply until the developmental state is created.

Both internal and external political factors affect the partial reform syndrome. The complexities of the internal side will be addressed in the next section of the paper. Let us now consider how external factors have come into play. Donor-supported “top-down” reform efforts in Africa have been crucial in initiating policy change, and in promoting reform in areas in which are technically blunt, politically manageable, and institutionally non-complex. The exchange rate is a prime example of this. But, donors have also had a tendency to sustain the partial reform syndrome. Cheryl Christensen (1981) argues that this occurs for three reasons.

First, donors develop comfortable working relations with their counterparts (basically a good thing); but these relationships often give donors both a false sense of the political viability of reform and a vested interest in bureaucratic stability when the needs of the reform process point to the necessity of more dramatic change. Donor relations with reform champions Mamadou Toure in Senegal and Philip Ndegwa and Harris Mule in Kenya are examples of this. Donors thought that substantial external support would assist these reformers; but Toure, Ndegwa and Mule have all left government, while the partial reform syndrome continues to blunt adjustment efforts in both Senegal and Kenya.

Second, donors are pushed by their own significant investments into follow-on lending to avoid the prospect of losses. The IMF and World Bank efforts to continue their operations in Zambia in 1989 and 1990 was an example of this. A similar situation may be developing in Kenya. In a similar fashion, donors in general are under pressure to expend resources and tend to be biased in the direction of over-optimism about what donor-supported programs can achieve.

Finally, diverse donor interests (especially strategic ties) provide maneuvering room for hesitant governments, limiting the imperative to sustain the reform process. US relations with Liberia and Zaire clearly had this affect. French relations with Senegal, Cameroon, and Côte d'Ivoire follow a similar pattern, as do British relations with Kenya.

This discussion of the economic impact of reform already raises a number of key sustainability issues for AID, especially the need to facilitate the more rapid and efficient provision of public goods and the need to facilitate the deepening of adjustment beyond partial reform. This paper has not yet addressed the political strategies that drove adjustment from both the donor and recipient perspectives, the political impact of adjustment, and the new political environments brought on by recent dramatic changes in Africa. These issues are now discussed below.

## Section Three: The Political Economy of Structural Adjustment in Africa

### A. Political Strategies of Policy Reform

It has often been commented that while structural adjustment efforts have been backed by an economic theory, they lack a political theory. Neither side of this assertion is quite true. While it is certainly the case that stabilization programs have been based on a well-articulated theory (the monetary approach to the balance-of-payments), structural adjustment efforts have been driven more by an overriding theme - the greater efficiency of markets - rather than by any formal theory linking different elements of an adjustment program.

Politically, structural adjustment has been heavily influenced by a political theory, that of neo-classical political economy. Merilee Grindle (1989) writes, "Neo-classical political economy provides a compelling explanation of economically irrational policy outcomes in developing countries. It asserts that individuals, politicians, bureaucrats and states purposely use the authority of the state to distort economic interactions to their own benefit." Within the donor community in the 1980s, neo-classical political economy was increasingly influential in interpreting ineffective developing country policies. This was a major step over the earlier donor perspective that ineffective policies were due to "bad" choices. But while neo-classical political economy provides effective tools for understanding bad policies, it offers little explanation or guidance for how to reform these policies. If a particular control regime is contributing to a range of individual and institutional interests, quoting Grindle (1989), "there is nothing to explain how or why these politically useful mechanisms would be traded in for mechanisms that offer ... less individual utility."

But, if neo-classical political economy fails to provide a theory of economic reform, it was nevertheless the case that donors did bring an implicit political strategy to their efforts to promote adjustment. The implicit donor political strategy of reform had three components: first, gain leverage over recipient governments through the carrot and stick of conditionality; second, use that leverage to diminish the role of the state; and, third, use leverage to shift influence over policy decisions from politicians to technocrats. Thus, policy conditionality would serve to initiate the reform process, while empowering technocrats was viewed as the instrument for sustaining policy reform.

Throughout most of the 1980s, donor efforts to generate economic reform focused on gaining the support of key decision-makers: senior politicians and top economic technocrats. This approach corresponded to the hierarchical structure of the development dictatorships that dominated the African political landscape, but provided a narrow political base from which to promote reform. Donors have believed that technocrats could rise above petty political rationality, especially if backed by the resources of conditionality-based donor programs. Donor strategies were marked by a search for the appropriate high-level technocratic client, and by efforts to buffer such clients from political pressures in the short-run and to create more "rule-driven" mechanisms for policy choice that could be supervised by technocrats in the long-run. (Examples of "rule-driven" policy choice mechanisms are exchange rate formulas based upon maintaining a stable real effective exchange rate or agricultural pricing models driven by tracking border prices.) What was envisioned was a leaner, but much more effective, state with policy-making dominated by an empowered technocratic elite.

Ironically, despite the critique of the African state implicit in the donor approach to policy reform, donor strategies corresponded quite nicely to the apolitical rhetoric and hierarchical nature of the existing African development dictatorships; and, in fact, sought to shift from one narrow focus of decision-making, i.e. top politicians, to another, i.e. top technocrats. Donors have had some success in some countries with this approach. In Malawi, for example, President Banda has been successfully removed from direct control over Press Holdings and decision-making power given to technocrats. But where technocrats have been successful, they have often not fit the apolitical image they have in the donor mind. David Leonard, in his recent book African Successes (1991), has examined the careers of several highly successful development managers in Kenya, including the technocrats behind the Kenyan adjustment program. What he describes are individuals who combine Western-taught technical expertise with tremendous skill for bureaucratic maneuvering and on-going efforts to sustain their own local political and cultural relevance.

The technocratic and apolitical approach to the policy reform process in the donor strategy also has little in common with the actual policy processes in western democracies which have sustained high levels of economic growth. Neo-classical political economy "pessimists" perceive in the conflict among interests a clear threat to the ability of government to develop policies that are rational for society in general. A more optimistic view of the policy process in Western democracies, in contrast, sees the public interest emerging out of the interplay of competing interests, bureaucratic influences, and technical analyses in a way somewhat analogous to the efficiency achieved by the competition of firms in the marketplace.

Even before the political crisis of African development dictatorships emerged in 1989, the World Bank and other donors were becoming concerned about the political dimension of the sustainability of reform. The main donor approach was to emphasize the need for host-country "ownership" of the adjustment program and process. But the notion of "ownership" has never been clearly defined, nor does it appear to have had much real impact on how donor policy reform programs are in practice undertaken.

It is interesting to contrast the donor strategy of promoting adjustment with the political strategy of structural adjustment from the perspective of a typical African leader in the 1980s. Many critics of donor-supported adjustment programs describe them as being "forced" upon unwilling governments. But African governments always have had the option, which many exercised, of not undertaking reform programs. We can assume that leaders would not undertake structural adjustment efforts unless they perceived the combination of external resources plus policy reform as less risky than facing the evolving circumstances of economic crisis, i.e. the deepening foreign exchange shortages and growing domestic imbalances. Robert Bates (1992) has argued that, from the recipient perspective, structural adjustment is a last-ditch opportunity to reform a regime from within, while minimizing political costs, in order to restore its viability in a new economic environment. In a phrase, for most African governments, the goal of adjustment is "partial reform."

Thus, while donors have viewed structural adjustment as a political instrument to transform African states, governments generally have seen it as an means of shoring up the status quo. Given these widely differing perspectives, it is not surprising that adjustment became such a highly contested terrain of public policy. Africanist academics, for their part, tended to fear that structural adjustment was politically de-stabilizing, due to the fact that it created increasing economic hardship. But the actual political impact of adjustment has been neither the transformation sought by donors nor the shoring up of the status quo sought by incumbent leaders. While adjustment did undermine African regimes, it did so in a manner that was more complex than that predicted by those who feared that stabilization would cause increasing hardship, and that such hardship would in turn become politically de-stabilizing.

### B. The Political Impact of Economic Reform

The growing political unrest in Africa in the late 1980s was an indication of the failure of both donor-envisioned economic transformation and incumbent-envisioned shoring-up of the status-quo. While "partial reform" was somewhat sustainable at the international level, it has proven to be less sustainable domestically. In turn, its domestic weakness has reverberated at the international level. It is important to understand how the political impact of adjustment has influenced Africa's political crisis. Three major factors interact to explain recent political trends of protest and reform in Africa.

The first is the general failure of African development dictatorships to deliver effective economic performance and rising living standards through state-centred development and heavy regulation of the private sector. This has served to

substantially weaken their claims to political legitimacy, especially among urban middle classes who have formed the core constituency for governments all over Africa.

The second factor explaining protest and reform has been the fallout from the collapse of communism in Eastern Europe. This effect has taken several forms. It discredited socialist and statist models while at the same time undermining the confidence of many African ruling blocs. Simultaneously, it spurred political protest by those disenchanted with the status quo who became emboldened by the success of popular movements in Eastern Europe. Finally, it put the issue of democracy on the agenda of donor countries. The final factor explaining protest and reform is the cumulative political impact of economic reform endeavors. This impact has been felt in several very different ways. But these impacts have been generally mutually reinforcing in ways that have been politically destabilizing for incumbent regimes, despite the interest of African rulers to use structural adjustment to shore up the status quo.

First, structural adjustment programs propelled the expansion of the non-governmental sector. According to Naomi Chazan (1992), “Many governments, cognizant of the role of the voluntary sector in the provision of essential services, relaxed some of the restrictions on organizational life in order to relieve them of direct responsibility for public welfare.” This led to a flowering of both local-level voluntary development organizations and intermediate organizations all over the continent, breaking the organizational monopoly that most African development dictatorships had imposed and creating the beginnings of an organizational counterpoint to the state.

Second, structural adjustment programs facilitated the expansion of the informal economy by weakening, in practice if not always expressly, the ability of the state to restrict informal activities. The informal sectors became, in many countries, the most dynamic area of the economy. The political impact of this, in turn, was the development of a significant resource base outside of the control of the state.

Third, structural adjustment reinforced the effect of the economic crisis in reducing the patronage available to rulers and the amount of rent-seeking in most African political systems. This threatened the control mechanisms in most African states. Nicholas Van de Walle (1992) explains, “The essential problem for state leaders during the reform process is to maintain control of the clientelest networks on which they have based their power, even as they decrease the cost of those networks by ousting old clients or curtailing their access to rent-seeking.”

Paradoxically, in most African states, even as structural adjustment programs were initiated to limit patronage and to restore the fiscal balance, corruption increased and budget deficits worsened. Two processes appear to have occurred. The state's internal discipline collapsed as the system of rewards and loyalty that previously held the system together frayed. This is particularly evident in the growing inability of many African states to raise taxation revenues, even in the context of donor-supported revenue-enhancement projects. In addition, the threat of major policy changes gave a powerful incentive for those administering the systems to get as much as they could in the fear that the tap would soon run dry. As the political crisis hit in the late 1980s, both of these trends were exacerbated as it became “every person for himself,” in the expectation of imminent political change.

If the general weakening of the state has been virtually universal in Africa, it has played out somewhat differently in CFA countries than in other states. In non-CFA countries, foreign exchange depreciation and the erosion of public sector wages went much farther in limiting the incentives for rent-seeking behavior, and, in general, created a context in which access to the state was simply much less valuable. Over time, people's aspirations were increasingly shifted to the private sector. Politically, there was less of an incentive to fight to retain public sector privileges. It is interesting that public sector union militancy has been much greater in CFA countries, in which wage erosion has been less extensive, than in Anglophone states in which real wages shrank in the 1980s to a fraction of their former value.

It is thus not surprising that substantially more of the recent political protest in CFA countries has focused on maintaining urban elite privileges than is the case for political protest in non-CFA countries. In the last section we discussed why the CFA system has made reform technically and economically more difficult. A very similar case can be made at the political level. A recent World Bank sponsored case study of the political economy of reform in Senegal (Ka and Van de Walle 1992) has highlighted the role of exchange rate inflexibility in explaining the limited success of reform efforts despite top level political support from President Diouf and a highly skilled technical team, led by Mamadou Toure, directing the reform program. This analysis suggests that the political environment for policy reform will continue to be poorer in CFA countries than in non-CFA countries.

Fourth, at the same time as the state began to fray from within, structural adjustment programs became the target of many of the urban middle-class protest movements that later became more deeply politicized. Protests generally attacked cuts in housing allowances and school stipends, and price increases for basic goods. But, while at the time this was interpreted as deep-seated opposition to adjustment, looking back the reality seems somewhat more complex. The protests quickly shifted from being against adjustment to being against incumbent regimes. And where opposition movements have taken power, such as in Benin and Zambia, they have tended to be more serious about economic reform than the incumbents they replaced. For example, the MMD government in Zambia has already implemented reforms that go far deeper than any envisioned by Kaunda's UNIP regime. This pattern in the evolution of protest and opposition policy suggests that the logic of economic reform efforts led the urban middle-class to see the solution to their problems in deeper institutional and political change, rather than in a return to the policy status quo ante.

In sum, the political impact of donor-supported structural adjustment was to interact with broader international trends to de-stabilize existing African regimes. But while some have viewed this de-stabilization as threatening viable economic reform programs, this paper posits that a somewhat different reading is called for. If, as this paper has argued, donor-supported adjustment programs were generating sub-optimal partial reform outcomes through a flawed political strategy that focused narrowly on enhancing the influence of technocrats, then it is not a bad thing that this syndrome became less sustainable. While the political impact of structural adjustment has not been what was envisioned by its designers in the donor community, i.e. the replacement of an anti-developmental political elite by a developmental technocratic elite, the undermining of African development dictatorships should be seen as an important <u>success</u> for adjustment, in that it opens up the possibility for fundamental changes in the way in which African countries are governed. The central insight of the entire literature on governance, written both by academics and practitioners, Africans and Westerners, is that such changes are a <u>necessary condition</u> for real economic progress and for sustained long-term development. This paper now turns to examine the new political environments in Africa and how they might affect the economic reform process.

## Section Four: The New Environments of Political Liberalization

The political ferment of the past few years has generated an entirely new political context for economic reform endeavors in sub-Saharan Africa. In general, the new political environments present both challenges and opportunities for economic reform, while the balance between these two impacts varies tremendously from country to country. There is now a large literature on the complex relationship between economic reform and political liberalization, although most of the case material refers to Europe and Latin America. The general conclusions from these analyses is that while in the long-run economic liberalization and democratization are not only compatible but essential to each other, in the shorter-term simultaneous political and economic reforms affect each other in both complementary and conflicting ways.

Economic and political reforms complement each other in the following ways: First, given that the incumbent political arrangements are widely regarded as one basic source of economic difficulties, economic reform without political reform lacks credibility. Second, for many African countries, removing the distortions of the interventionist state requires breaking the political power of groups benefiting from the old system, which in turn necessitates political change. Third, political reform provides a tactical opportunity to undertake politically difficult reforms, both by blaming the old system for the need for such reform and through “buying” tough economic measures through the granting of increased freedoms on the political side.

But there are also conflicts, in the short-term, between political and economic reform. The surge of popular demands released by democratization may run directly counter to the need for fiscal and monetary restraint. Credibility and confidence in the continuity of reform measures are needed to engender the investment supply response that makes reform work. The inherent uncertainty of political reform will lead investors to hedge their bets. New democratic systems might need explicit political bargains to hold themselves together; these bargains may run counter to allowing market mechanisms to allocate resources. Finally, political leaders will be stretched to the limits in having to manage both economic and political reform.

With these themes in mind, this paper explores some of the specific aspects of political change in Africa that have implications for the sustainability of economic reform. One important impact of political change has been the creation of a much more diverse set of national political conditions than had previously been the case in sub-Saharan Africa. While in the past some form of neo-patrimonial semi-authoritarianism had held sway in virtually every African country, the picture is now much more complicated. A wide range of political conditions and regime types have emerged, and there are as yet no clear trends or patterns of consolidation. Political fluidity is the order of the day all over Africa. Even where transitions to democracy have occurred, such as in Benin and Zambia, it is not certain that these mark a fundamental change in the nature of politics. Thus, it is extremely difficult to generalize about either the nature of political change or the impact of such changes on economic reform. Nonetheless, some overall points and some tentative implications can be drawn from the current context.

The single most important characteristic of recent political change in sub-Saharan Africa is the diminished ability of existing (or, indeed, new) regimes to monopolize the political, economic and institutional environments as they had for most of the period since independence. This is the essence of political liberalization. In general this has had a very positive impact, expanding the political space for non-governmental organizations and providing opportunities for increased popular political participation. Given the economically stifling impact of government control over business in Africa, the reduction of government influence over the business community and enabling societal interests, including producers and consumers, to organize politically is overwhelmingly likely to have a positive effect on economic policy and economic development over the medium term.

But every political transition has short-term economic costs and also engenders political uncertainty. Because of the legacy of economic decline in most of Africa, these dangers tend to be greater than elsewhere in the world. In some African countries (especially in the Horn of Africa), the impact of the loss of state control has been rapid political deterioration and the emergence of virtual anarchy. Even in countries in which the impact of political de-monopolization has been largely benign, the potential for political fragmentation has been enhanced. The fact that this is substantially the legacy of decades of economic mismanagement is beside the point. The risk of widespread political decay haunts contemporary Africa. Essentially, the same forces that have created the context for political liberalization and new experiments with more democratic forms of governance have also increased the danger of ethnic fragmentation and other forms of political decay.

Economic reform efforts in the 1990s will be undertaken in a context in which the threat of political decay looms. The implications of this are not especially clear, but certain predictions are possible. Where the threat of political decay is less immediate, its visibility elsewhere on the continent might provide leaders with the impetus to make dramatic policy and institutional reforms in order to generate economic growth and strengthen political stability. On the other hand, where the threat is more immediate, it might frighten leaders away from any actions that might in the short-run exacerbate an already fragile political environment.

Recent political changes have created a much more conducive environment for non-governmental organizations (which, as discussed above, had already expanded in number and scope in the 1980s) to become more directly involved in both politics and development policy. Where the de-monopolization of political power has not led to political fragmentation and decay, NGOs are an important factor in the movement towards democratization. At the same time, the non-governmental sector has, in most African countries, only a very limited capacity to effectively influence policy decisions, both due to organizational weakness, other priorities, and limited analytical skills. In addition, the bureaucracies in most African countries are not prepared to respond to the non-governmental sector; they remain oriented to influencing and constraining, in some cases even directly controlling, non-governmental actors.

Both in countries that have undergone significant regime change (such as Zambia and Ethiopia) and in countries where old regimes remain in place or appear to be in some process of transition, decision-making and policy implementation patterns are in flux. This has important implications for economic reform efforts. Even in many countries that are passively or actively resisting democratization efforts, it appears that "top patterns of policy reform are no longer viable. In some of these countries, neo-patrimonial relations that were the glue in political/bureaucratic systems have begun to fray, limiting the likelihood of decisions making their way through the bureaucracy. In others, incumbent regimes have, on their own, recognized the need to broaden the scope of participation in reform efforts.

In new regimes, the uncertainty of decision-making and implementation patterns have complicated economic reform efforts. For instance, in Zambia, maize price reforms, a crucial item on the new MMD government's reform agenda, have become mired in a web of conflicting bureaucratic entities. While the uncertainties that have been created in decision-making and implementation of policy reform create problems for donors, including AID, they also create real opportunities to expand the basis upon which policy dialogue, policy decision-making and policy implementation have been undertaken.

One of the most important political changes now underway in sub-Saharan Africa is the rise of a new type of political leader. These leaders have emerged and operated largely outside of the neo-patrimonial patterns of rewards and loyalty that have dominated African politics since independence. Unlike the earlier generations of African leaders, who were schooled in marxism or fabian socialism and the anti-colonial struggle, these new leaders have been shaped more by technical training and are influenced by the experiences of the Asian NICs and the reforming states of Eastern Europe and the former Soviet Union. Opposition movements and parties in Africa are often marked by a tension between these younger leaders with a new style of politics and older politicians who, for whatever reason, had fallen out with the incumbent regime, but share with incumbents a more traditional political style.

The new generation of African political leaders are generally unfamiliar with the tasks of governing and political management. At the same time, they generally recognize the need for a new approach to economic policy and tend to be market and private sector oriented. They also tend to be oriented to achieving and sustaining political legitimacy not only in terms of results but also in terms of participation and process. In this they differ completely from their political forbears, who promised results at the expense of process (and who lost legitimacy because of their failure to deliver results). Thus, while new African political leaders are likely to be favorably oriented to economic reform, they are also likely to want to seek to generate a broad consensus behind it.

So far in Africa, where democratic political transitions have led to new regimes, the short-term impact on economic reform has tended to be positive. Three factors appear to be especially important in explaining this. The first is the fact that new regimes are generally in dire economic straits and thus have a very strong imperative to establish their bona fides with external funding sources, especially the IMF and the World Bank. In the aftermath of the Cold War, moving forward on economic reform is the only strategy they have to do this. The second factor is that new regimes tend to be somewhat autonomous from interest groups, particularly those which directly benefited from the old regime. This has limited the political constraint that had previously side-tracked important reforms. Finally, many new leaders have understood the importance of “striking while the iron is hot,” i.e. of utilizing newly gained political legitimacy to attack tough issues before their ability to do so is lost. Unfortunately, it is not yet clear whether this initial positive impact of regime change on economic reform will be sustained.

In sub-Saharan Africa, the fates of economic reform and political liberalization are likely to be closely intertwined. Given the political uncertainties generated by the loss of state monopoly power, moving beyond political liberalization to the consolidation of democratic governance will be important for sustaining economic reform efforts. Democratic governance entails five dimensions: public management effectiveness, legitimacy and public responsiveness, accountability, information openness, and pluralism in the policy domain.

In particular, the consolidation of democratic governance will be crucial for improving the investment climate and generating the private investment needed to invigorate a dynamic supply response to reform efforts. It will do so in several ways: First, the consolidation of democratic governance will limit the level of corruption, that has both consumed public resources and either driven away private investment or directed it in inefficient areas. Second, the consolidation of democratic governance will provide the legal context conducive to private investment. Finally, the consolidation of democratic governance will limit the likelihood of political fragmentation and decay and thus promote political stability and a more predictable environment for investors.

Conversely, it is virtually impossible to envision the institutionalization of democratic governance in African states in the absence of economic recovery. Indeed, without economic recovery, more African states will inevitably move in the direction of contemporary Liberia, Sudan and Somalia. Economic recovery, in turn, will depend upon a more substantial policy and institutional reform effort than has hitherto been the case. Thus, in many ways, sustaining the policy reform process in contemporary Africa should be seen as part and parcel of sustaining the democratic transition itself.

## Section Five: Sustaining Economic Reform in the Context of Political Liberalization

In the context of political liberalization in Africa, facilitating the sustainability of economic reform will necessitate donors working at several levels. The traditional approach of policy reform efforts to enhance the influence (through conditionality) and capacity (through technical assistance and training) of key technocrats remains relevant, although it needs to be more realistic about the limits of conditionality and to be refocused on issues of policy implementation and more effective political base-building.

But donor-supported economic reform efforts must also go beyond policy change and beyond the traditional focus on technocrats. Within the public sector, the sustainability of reform will remain problematic as long as African governments fail to transform themselves from instruments of neo-patrimonial political control and predation to instruments of development. African governments need a process of deep institutional restructuring, of democratic fortification, to enable them to be transformed into developmental states. This is unlikely to be possible in the absence of direct donor support.

The sustainability of reform will also depend upon donor activities outside of the public sector. The first of these is enhancing civil society, which will at the same time: 1) hold governments more accountable to their citizens, 2) provide the basis for, and some of the inputs to, a more sustainable policy process, and 3) hold in check the pressures for political fragmentation and decay.

Sustaining economic reform will necessitate donors working to strengthen the institutional context for markets and for the private sector to emerge and proliferate. Without this, the economic growth response to adjustment will continue to be minimal, and reform efforts will remain politically vulnerable. The essence of strengthening the institutional context for market development is the expansion of public goods. While these public goods need to be facilitated by government, experience (as well as the limited fiscal and operational capabilities of virtually every African state) suggests that innovative means for providing such public goods will have to be created.

Thus, from the donor perspective, there are four key dimensions for facilitating the sustainability of economic reform in the context of political liberalization: 1) enhancing civil society; 2) establishing the institutional foundations for markets; 3) changing the role of government; and 4) improving technical capacity, especially in the area of policy implementation. AID can develop support activities on each of these dimensions. In this section, each of the dimensions is discussed in turn, while in the next section specific implications for AID and the Africa Bureau will be addressed.

### A. Enhancing Civil Society

In the new African political context, civil society has a number of crucial roles to play: a key brake on state power, a broker between state interests and non-governmental concerns, and a facilitator of national consolidation. Nurturing civil society is important both for establishing the foundations for durable democratic government and for countering fissiparous tendencies and the impetus towards institutional breakdown discussed above.

But what is civil society? Is it synonymous with the non-governmental sector? With its voluntary wing? Naomi Chazan (1992) argues that one should not equate civil society with non-governmental or voluntary organizations in general. Rather, to be considered part of civil society, an organization must at the same time be: 1) autonomous of government, 2) constrain the power of the state, but 3) contribute to the legitimation of overall state authority. Organizations that have these characteristics are critical building blocks for civil society for they help to inculcate specific notions of limited authority, respect for the rule of law, and conflict resolution.

Most non-governmental organizations in Africa do not fit these criteria, although many may have the ability to grow into them. For example, village community groups, informal credit associations and various religious cults are often inward-oriented, pointedly detached from both market and state, and primarily concerned with protecting themselves from outside influence. They thus undermine the authority of government. Other organizations, such as trade unions and women and youth organizations are so dependent upon government support that they have lost any real autonomy. Finally, regionally- or ethnic- based movements, or fundamentalist groups, either oppose secular authority or seek to take over the state. In general, while the demise of effective political control by African governments has spawned a vast number of non-governmental organizations and groups, civil society per se remains weak in most African countries.

What kinds of groups are likely to facilitate the coalescence of civil society? Groups that have specific, partial, and limited objectives, be they professional organizations, religious groups, developmental NGOs, credit unions, interest-associations, or human rights and civil liberties organizations. Especially important are "linkage organizations" that bring together networks of individual organizations. Civil society, thus defined, appears to be strongest in Anglophone African countries with relatively strong state structures and relatively pluralist political institutions and political cultures, i.e. Kenya, Zimbabwe, Nigeria and Ghana. In Francophone Africa, only Senegal and possibly Cameroon, appear to have the depth of civil society similar to those in the aforementioned anglophone countries.

The expansion of civil society appears to be directly related to the strength of both state and market. According to Chazan (1992), "Where the reach and capacities of the state diminished dramatically (Liberia, Ethiopia, Mozambique), social groups proliferated but civil society contracted. Where the state attempted to control and exploit productive activity, it indirectly bred associations that rejected its paramountcy (Zaire, Tanzania and Sudan)." Michael Bratton (1989a) describes the desired relationship between state and civil society as a "love -- hate" one in which neither can be effective without the other.

Within civil society, there is a special niche for organizations representing business interests. Thus far in Africa, where civil society has played any significant role in economic policy debates and decisions, it is because of the role of organized commercial elites. This fact has led one observer to declare that "the business bourgeoisie constitutes the spine of civil society."

The pluralization and fortification of associational life supports both democratization and economic reform efforts in Africa. The critical issues are how to support the autonomy of organizations with civic propensities, how to bolster organizations that are part of civil society at the expense of those with other objectives, and how to strengthen the civic propensities within existing organizations. Supporting civil society involves several dimensions: direct institutional assistance, a general improvement in communications and the free flow of information, and enhancing state capacities to respond to and manage the demands presented upon government by an active civil society. It is important to remember that civil society is a substitute for neither state nor market, but an important facilitator of both.

### B. Establishing the Institutional Foundations for Markets

Markets involve institutions that must be developed. As discussed earlier, one of the explanations for the limited impact of policy reform efforts so far undertaken in sub-Saharan Africa is that the legal and institutional foundations for free and efficient markets are weak or absent. At independence, African states inherited a set of fragile market-oriented institutions that had been set up to support colonial trading interests. With very few exceptions, in the course of the post-colonial transition, these institutions failed to survive as instruments promoting economic development. Instead, they were transformed into apparatuses that 1) consumed the surplus they extracted, 2) encouraged private actors to shift from efficient productive activities to unproductive rent-seeking, and 3) failed to provide public goods.

Because the underlying conditions in Africa are so difficult, many markets do not work well. A 1992 World Bank review of its projects in agricultural marketing decried the lack of attention given to the institutional side of market development, issues such as market news services, regulated weights and measures, credit for small traders and improved market structures. A defining characteristic of the weak institutional context for markets in Africa is poor information about the quality of goods, services, risks, and people.

The lack of an institutional foundation for market-based development has directly constrained the impact of policy reforms undertaken under structural adjustment programs in Africa. The Cornell study (1992) cites a number of examples of this. The lack of access to credit, weak information, and the lack of credibility of government policy largely explain the failure of the private sector to make a market for fertilizer after deregulation in The Gambia. In Guinea, poor infrastructure and the lack of credit and effective information flows similarly constrained the availability of domestic rice despite improvement in producer incentives. These examples highlight the need for the development of market institutions to supplement policy reform and the disengagement of the former structures of state regulation and control. Fair and efficient markets do not occur by accident; they are the products of intelligent laws and public policy, and effective cooperations between government and the private sector.

What are the key elements of the institutional foundation for markets? A number of these are

general and apply for all countries; others are especially relevant for underdeveloped countries, while others are especially concerned with the transition to a market-based economy. First and foremost is a well-functioning legal system, with clear and simple procedures for enforcing contracts and for defining and defending property rights. Second are capital markets and systems of banking and credit provision that can intermediate savings and effectively enforce rules of repayment. Generally, the development and deepening of capital markets depends upon a stable, and credible, currency. Third are systems for ensuring ample market information on prices, availability, and quality of goods and services, capital and labor. Finally, an infrastructure that effectively links producers and consumers and provides reasonable transportation and communication costs is needed to facilitate both domestic and international trade.

In African countries, where domestic markets are thin and where international economic fluctuations can wreak havoc with production decisions, effective mechanisms for regulating and guiding non-competitive markets are also needed, as are instruments for some degree of price stabilization. This is despite the fact that most African institutions that were initially designed for these roles have played them very poorly. Oversight of financial and technical standards is an area in which African countries are especially weak.

For countries making the transition to a private sector and market-based economy, as are many in sub-Saharan Africa, there are special institutional needs. The first is a capacity to both create a level playing field and to implement and monitor the process of privatization and liquidation of hitherto public sector enterprises. The second is an institutional capacity to aggregate and articulate private sector needs and interests. In the absence of such a voice, the public sector is almost invariably going to make large errors, and the private sector will be less likely to shift their own behavior away from seeking special favors and other forms of rent-seeking to attempting to influence the policy and institutional environment.

The transition to a market-based economy also needs the institutional capacity to ensure the fairness of initiatives undertaken in the transition. Especially important here are credible instruments to prevent the politically well-placed from gaining privileged access to assets, and procedures to prevent and punish collusion and other restrictive business practices. Such instruments are expensive and difficult to create. In purely economic terms they might not appear to be worth the effort; but their political impact is likely to be important for sustaining the transition to a market economy.

Finally, one of the institutional foundations for the market is the existence of effective instruments of poverty alleviation and social service provision. Especially in sub-Saharan Africa, where traditional cultures put great emphasis on reciprocity and equity, market-oriented economic reform initiatives are unlikely to be sustained in the absence of explicit institutional mechanisms to address these themes.

### C. Changing the Role of Government

This discussion of the institutional foundations for markets suggests that creating the environment within which markets and the private sector can grow and multiply necessitates a significant, if limited, continuing role for government. This presents a serious dilemma for those committed to African development. As discussed earlier, one of the lessons of African development is the central role that bad government played in causing developmental failure. In the 1980s, the pervasiveness of the consensus about bad government stretched across the ideological spectrum, leading conservatives to turn to laissez-faire, "rule-driven" policies, and the private sector as alternatives to government-directed development, while liberals saw the answer in the informal sector and the expansion of the activities of NGOs. The anti-government mentality reigned.

But, like it or not, government remains central to the process of structural change in Africa, including such changes whose central themes are to reduce the role of the state. In every developing country (including in Africa) where economic reform measures have been undertaken, state managers have played a vanguard role in initiating them. Ironically, the transition to a private sector-led, and politically and institutionally-pluralist, economy in Africa will demand a significant and effective government role. Dismantling the state is not the answer, it must be reconstructed. Transforming the state from a major part of the problem to an important part of the solution must be a central item on the agenda for sustaining the process of economic reform in Africa.

Successful economic reform requires consistent and skilled macroeconomic management, effective public implementation of the privatization process, new efforts to protect the environment, regulations and policies that promote and protect competition, and sophisticated creation and oversight of capital markets and the financial system. In the past, neo-patrimonial African development dictatorships

have been incapable of undertaking these tasks. While political liberalization does not automatically generate an improved context for achieving these aims, it does create the opportunity to seek real changes in the ways that governments operate in Africa.

For free-market reforms to work, state effectiveness must improve. This involves more than articulating the right policies or putting appropriate laws and regulations on the books. A recent Center for International Private Enterprise assessment of the extent of policy reform in developing countries placed many African states on a policy par with a number of Latin American and Asian reforming states. But, in Africa, where good policies exist they are only partially and ineffectually implemented; and where appropriate laws are on the books, they usually coincide with cumbersome and corrupt judicial systems.

Reconstructing government is, both technically and politically, a much more difficult task than paring back the predatory state. As David Sahn (1992) writes, “Cutting government expenditures is easier than identifying constraints to growth and bringing about the changes required to ensure their relaxation.” The scope of the challenge is no less than transforming the budget, and indeed the public sector in general, into an instrument to promote development. Arturo Israel (1990) of the World Bank has highlighted the four key positive public sector functions that are crucial for facilitating the transition to a market-driven, private sector-led economy.

The first is the capacity to design, monitor and implement a consistent set of macroeconomic and sectoral policies. As market and financial liberalization progress, this function becomes more important as governments lose the capacity to mask and stretch out the costs of fiscal indiscipline, inappropriate exchange rate management, and monetary expansion. According to Israel, if this capacity is not in place, nothing else will work very well. In Africa, the strengthening of macroeconomic policy analysis has generally not been effectively linked to efforts to strengthen policy reform implementation and management, especially in the area of fiscal and budgetary policy.

The second function is the capacity to provide a conducive enabling context for the private and public sector activities that will operate in competitive environments. This involves three main sub-categories. The first is dismantling the disabling environment, in particular, modifying or eliminating the functions of state agencies that controlled and dominated the private sector. Key areas here are customs, foreign exchange controls, industrial licensing, and financial controls, among others. The second is the effective maintenance of the level playing field by regulating non-competitive markets and enforcing financial and technical standards. The third is the effective promotion of key sectors, be it export promotion or enhancing domestic food production.

The third function is the capacity to privatize wisely and effectively. Privatization programs have been too narrowly focused on divestiture. Governments need to be able to develop a broader range of options that reflect the reality of very slim markets and high political costs. This involves the preparation of a strategic plan, as well as the capacity to prepare the units for sale or leasing, to ensure the fairness and transparency of transactions, and to implement a public awareness campaign to manage the inevitable political tensions that privatization entails. Finally, governments need the capacity to operate more effectively the enterprises that will remain in the public sector.

The fourth function is the capacity to conduct an effective dialogue with the private sector. In Africa, even those technocrats who have been at the forefront of economic reform efforts have tended to look skeptically at the private sector. Even worse, key public sector agencies that interact with the private sector have looked at business people with a view to control rather than looking at them as clients with needs and preferences, and with a voice that must be taken into account.

In order to achieve these functions, the structures and procedures of African governments will need to be transformed. The political changes now sweeping Africa create conditions in which fundamental changes may be possible. In general, civil service reform is a sine qua non for changing the role of government. The new functions of government require a far smaller number of staff, but a staff with relatively higher skills and training than those that now inhabit most African public services. Some government agencies need to be disbanded while new agencies or units must be created.

A crisis of public incentives plagues African countries. Real wages in the public sector have fallen dramatically. Pay and performance have virtually no connection. As a result public performance atrophies and the fiscal crisis deepens. The rise in employment opportunities in international agencies, and in local consulting for various donors including

USAID, has made remaining in public service financially irrational for honest individuals.

African countries face a classic chicken and egg problem. Public performance cannot be improved until professional and technical staff have incentives to put their full efforts into their work. Yet, these incentives cannot be created until budgetary resources increase. Those increases can only come from improved revenue capacity and broad-based civil service reform. But the former will be the result of improved performance, while the latter is both technically complex and politically challenging.

This dilemma cannot be resolved without donor assistance and support. But new donor efforts in this area will have to go beyond past efforts to improve public administration. These efforts have stressed training, institution building, foreign advisors and better equipment, but have tended to ignore incentives and the realities of the broader organizational and economic environments within which specific agencies operate.

### D. Improving Technical Capacity for Policy Implementation

There is a broad consensus that implementation problems are a major weakness in African reform efforts. Obviously, economic reform must be effectively implemented before it can be sustained!! Donors have paid little attention to enhancing technical capacity to actually implement reform programs. This was partially driven from the belief that African governments should take "ownership" of reform programs. But it often created a situation in which government was left to implement activities that they were only peripherally involved in designing. It is not surprising that implementation has been so problematic.

Much recent donor effort, including by USAID, has gone into enhancing the technical capacity of African governments in the area of policy analysis. The rise of structural adjustment created a huge demand for economic policy analysis to inform the specifics of adjustment programs. But, in practice, much of the policy analysis capacity generated in the 1980s was either lost in human capital flight (for instance, 18 out of 24 mid-level technocrats trained under HIID's project in the Kenyan Ministry of Planning have left government for various multi-lateral agencies), became the source of artifacts to be manipulated in the game of conditionality, or reinforced the "top-down" decision-making style and exercise of authority that dominated African states.

As discussed earlier, donor strategies often sought to insulate technocrats from their political constituencies and superiors as a tactic to promote more effective policy outputs. Where conditionality was effective, such an approach could work in the short-term. But, the experience in Africa has been that in the longer-run technocratic insulation almost invariably losses out to political considerations.

Recent experience suggests that a very different concept of the political role of technocrats and of policy analysis is needed. Arturo Israel (1990), in his review of successful cases of policy formulation and implementation, suggested that what facilitated success was not technical insulation but effective communication among policy analysts, between policy analysts and political decision-makers, and discrete organizational linkages between analytical units and relevant bureaucratic apparatuses responsible for implementation. Similarly, Ka and Van de Walle (1992), in their study of adjustment efforts in Senegal, found that the technical team led by Mamadou Toure was so effectively "insulated" that it lacked any real sense of the organizational consequences and feasibility of what it proposed, and lacked the political linkages into the bureaucracy to leverage effective implementation.

A recent comparative study of the politics of economic adjustment emphasized the theme of "embeddedness" in enabling capacity-building efforts to be successful. Embeddedness refers to the need for technocrats to be able to understand, and work within, the political constellations of the state. It also refers to the need for technocrats to establish linkages with the private sector. Reflecting on Asian successful reformers, Peter Evans (1992) writes, "Embeddedness is necessary because policies must respond to the perceived problems of private actors and rely in the end on private actors for implementation. A concrete network of external allies allows the state to assess, monitor, and shape private responses to policy initiatives, prospectively and after the fact. It extends the state's intelligence and enlarges the prospect that policies will be implemented... Connections to civil society become part of the solution rather than part of the problem."

In the recent AID-sponsored Center for Strategic and International Studies (CSIS 1992) study of the politics of economic reform in Africa, one of the conclusions was that donor involvement in the reform process was far too front-end loaded, focusing on analysis and conditionality, while much of the difficulty in economic reform came after analysis was completed and conditionality-based agreements were signed. One of the main recommendations of the

study was that much more effort be put into facilitating effective implementation of reform programs.

A central part of donor support for improved implementation must be to build local capacity for implementation. This should address not only to the narrowly technical issues involved, but should enhance the capacity of African governments to strategically manage the process of policy implementation. Skills in political/institutional analysis and interventions should be part of this package. Capacity-building for improved implementation should be informed by Gerald Meier's recent comment: “Development economics is on the edge of politics and on the edge of management. To be more effective in policymaking, it must venture more into each territory.”

## Section Six: Implications for USAID Strategies and Operations

The analysis presented in this paper presents a wide range of implications for AID/Africa Bureau strategies and operations. The most important strategic implications are as follows:

**1. The new political contexts in sub-Saharan Africa provide both new challenges and new opportunities for AID's efforts to promote economic reform.** While the new context in many ways will mean a more complicated political environment, and will necessitate new modes of operation by AID, it also provides the opportunity for economic reform “breakthroughs” that in the past were precluded by the very nature of African ruling regimes. This means that, in the context of meaningful political reform, AID missions should be encouraged to “think big,” i.e. to work with host governments to “strike while the iron is hot” on major reforms that address key constraints to the effective transition to a market-based and private sector led economy.

**2. The analysis presented in this paper suggests some useful criteria for focusing AID's economic reform efforts in Africa.** Certain pre-conditions appear to be necessary for the long-term sustainability of reform. Sustaining economic reform is not possible in a state dominated by neopatrimonialism, no matter how strong the technocratic personnel; nor is it possible in a context in which reform of an inappropriate exchange rate regime is precluded. This suggests that AID's policy reform activities in Africa should focus on countries outside the CFA zone that have moved the furthest towards political liberalization.

There is a parallel between reform efforts in neopatrimonial African states and the evolution of reform efforts in communist states of Eastern Europe and the Soviet Union under Gorbachev. Frustration with reform efforts in Kenya, Zambia, and Malawi (not to mention Eastern Europe and the Soviet Union) all suggest the dependence of fundamental economic reform on a prior or at least simultaneous fundamental political reform. This doesn't mean that all economic reform efforts must wait for the demise of neopatrimonial (or communist) regimes, but does suggest that expectations about the extent of reforms that are possible in such political settings should be limited and realistic.

Certain key policy and institutional reforms are pre-requisites for the success of the overall reform process. At the early stage of the reform process, at which virtually all African states now find themselves, exchange rate policy reform is fundamental. Thus, there is limited scope to deepen and sustain economic reform efforts in CFA countries in the absence of basic changes in the franc zone monetary arrangements. AID reform efforts in CFA countries should thus remain modest.

**3. While AID should focus its economic reform efforts on politically-liberalizing non-CFA countries, it should avoid the temptation of trying to create “African winners” through a large and long-term commitment of donor resources.** Recall that donor efforts to support reform, especially through the cash transfer mechanism, have tended to sustain the partial reform syndrome. This suggests that the over-commitment of donor resources, out of a desire to create “African winners,” are likely to be counter-productive. Foreign assistance can never play the central role in creating winners. While it is appropriate to give additional financial support to newly democratic regimes, especially those undertaking difficult reform initiatives, such support should be strictly time-bound, say for a period of two years.

**4. Economic reform “breakthroughs” will not come about by broader and more effectively implemented policy reforms alone**. Policy reform efforts, by themselves, have not been and will not to be, sufficient to address the central development problems that necessitated structural adjustment. Addressing these issues demands: 1) the transformation, and democratic fortification, of African states; 2) the creation of the institutional foundation for markets through the broader and more

effective provision of a wide set of public goods upon which both democratization and economic transitions depend; and 3) the institutionalization of a more effective policy process, especially through strengthening the "demand side" of the process. Thus, AID needs to broaden its approach to economic reform to address each of these dimensions of the reform process. The next three points will address in turn each of these dimensions.

**5. Donor efforts at economic reform in the 1980s have focused on paring back the predatory, neopatrimonial states of sub-Saharan Africa. While this was a necessary step in economic reform; it was not sufficient.** A major lesson of economic success in the Third World is the importance of the developmental state. For many African states that have initiated reform programs and successfully completed some basic reforms, transforming the role of the state has become a prerequisite for sustaining economic reform. While transforming the state is in itself a multi-faceted process, at its center is civil service reform. Achieving fiscal viability and effective organizational capacity both ride on the success of civil service reform. AID missions in certain African countries may be well-placed to play a supporting role in this area. A second key element in the transformation of the African state is the shift from a "control" orientation vis-a-vis the private and non-governmental sectors towards to a "facilitation" orientation. AID missions might be encouraged to work with a key ministry, either in a productive sector (such as the commerce and industry ministry) or in a social sector (such as a health ministry), to effect such an institutional transformation.

**6. Sustaining economic reform basically means generating a transition to a market-based, private sector-led economy. This transition depends upon the creation of a wide range of public goods that are currently in very short supply in Africa.** Some of these public goods are traditional, while others are especially related to the needs of the transition period. Especially important are what David Sahn (1992) refers to as "crowding in" investments, in infrastructure and research; and the key institutional underpinnings for the transition to a market economy, such as capital markets and privatization capacity. Facilitating the more effective provision of these public goods is a classic function of foreign assistance that should be a focus of AID's efforts to sustain economic reform. In the African context of weak public capacity, the provisioning of these public goods will often have to be undertaken by agents other than governments. AID missions should be encouraged to work with governments, the private sector and NGOs on developing financially sustainable programs of enhanced public goods provision.

**7. Political liberalization necessitates a change from the "top down" pattern of policy reform that dominated donor efforts in the 1980s. The political sustainability of policy reform in the new political environments will demand far greater attention to political base-building than had been the case in the 1980s.** While democratic regimes in Africa are likely to be more serious about economic reform than their predecessors, they also base their legitimacy on a more participatory policy process. Sustaining economic reform in this context will necessitate AID paying more attention to the processes by which policies are made and implemented. In the past, donor agencies, including AID, have focused too narrowly on the content of policy. AID can assist governments in 1) ensuring that a range of inputs, especially from those affected by and those responsible for implementing policy, are brought into the policy process; 2) building the institutional capacity to manage a broad-based policy process; and 3) creating the capacity to effectively implement and monitor the impact of policy.

There are also a wide range of more operational implications that flow out of the analysis presented. Some of these are:

**1. In the design of projects and programs in support of privatization and private sector development, AID missions should consistently bear in mind the importance of what CDIE labels "complementary" reforms, in the regulatory and legal arenas.** Unless these are in place, policy reform efforts will not be effective in eliciting the desired investment response.

**2. In general, the availability of accurate information is a crucial element in making markets operational**. A broad flow of information is also central to a democratic political culture and to improving governance. AID-supported economic reform projects and programs should focus on improving the flow, and lowering the cost, of information. These efforts are much more politically viable given the political changes of the past few years. AID missions should put high priority on improving and expanding information flows, in that it will limit the likelihood of retrogression in both the political and economic arenas.

**3. Political liberalization complicates the process of economic reform in that reform opponents and/or those who are negatively affected by the**

**reform are less constrained in organizing and expressing their opposition. Thus, it is increasingly important to have established communication with and input from affected groups in the design stage of AID-supported programs and projects.** It is also more important than ever that governments make effective efforts to publicly defend their reform agendas, especially in controversial areas such as privatization and civil service reform. AID missions can provide support for such activities.

**4. Enhancing public understanding of economic issues can help sustain the economic reform process.** In many African countries, such as Nigeria, economic journalism is woefully backward, and has helped to promote a hostile environment to economic reform. In other countries, such as Kenya, effective economic journalism has played a role in shaping a political environment generally supportive of reform. In the new political contexts, public opinion will play a more important role in determining the viability of reform efforts. AID missions should explore activities that enhance public understanding of economic issues, especially those that involve the mass media.

5. **Missions should be encouraged to undertake pilot-type activities to enhance the "embeddedness" of African governments.** One current example of such an activity is USAID/ Uganda's support for a "national forum on investment and export promotion," that has brought together the political leadership, key technocrats from both policy and operational units, and a range of individuals representing different commercial pursuits. The purpose of the project is not to debate the merits of investment and export promotion, but to develop on-going working relationships and operational action plans that address specific constraints identified by businessmen, government officials and other analysts.

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