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Balancing society and market:

Public policy and growth for Africa

Ditchley Park Lecture

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7 July 2006

Introduction

Thank you for inviting me to address you today.

This year marks the tenth anniversary of my tenure as minister of finance of the Republic of South Africa – a ten year period that has been marked by international financial crises, preceded ominously two years earlier by the 1994 crisis in Mexico, continuing through the Asian crisis in 1997, and the Russian crisis in 1998, and flaring up again in 2001. Large shifts in investment portfolios have sparked contagion again this year, prompted by inflation concerns and interest rate hikes in the world's largest economy – and supported by unprecedented current account deficits and surpluses across the major world economies.[1] These global financial and economic imbalances put at risk the growth, poverty and development achievements of poorer countries, and pose

[1] **The US current account deficit in 2005 was 6.4 percent of GDP or US$804 billion. The budget deficit, although not unprecedented, was 4.3 percent of GDP, or US$564 billion.**

special challenges for the developing world.[2] I want to speak to you today about some of those challenges.

In doing so, I want to venture into difficult terrain for governments – to provide some perspective on the case for an organic and national policy response to the international environment, and to globalisation in particular, that takes advantage of the vast gains to be had from economic integration. And I want to make a case that is cognisant of and sensitive to the responsibilities of national governments and the power of the state in the face of globalisation's risks. Above all, this perspective must strive for a positive contribution from markets and states to the fulfilment of human economic, cultural and social development.

This latter goal merits further consideration, not least because it in some senses captures the essence of what elected governments ought to be about. Economics and finance are of course critical areas of public policy, and human welfare has increased as a result of the application of economics to social organisation as well as relations and a wide variety of other public issues. Nonetheless, we need to remain conscious of the temptation to too fully apply the logic of the market to all human endeavours.

We live in a time in which the virtues of 'economic man' are lauded above most other facets of humankind – often to the detriment of our fully comprehending and ensuring the role of community and state in public policy. This has implications for how state and market are organised at the domestic level and the institutions that give life to both, for regional initiatives to create cross-border economic activity, and for what we do as an international community to address poverty through aid and the international financial system.

In the 1940s Karl Polanyi wrote about another period in our history where we allowed economics to over-determine social relations – he described how radical liberalism of the 19th Century denied the "reality of society" and enabled an unprecedented creation of wealth in the hands of elites.[3] In his view, the unemployment and destitution that was an integral part of that wealth creation (and the shift from agricultural to industrial societies) resulted eventually in the misery of fascism in Europe. History's lesson was of the need to prevent the aggregation of social and economic power in the hands of too few, by regulating economic power in a way that maximises the freedoms of those without power. Regulation of markets and making them reasonably competitive (or possible to enter) became a critical element of a public policy that sought to steer in a

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[2] **The global imbalances are caused by positive shifts in saving (higher foreign reserves and lower budget deficits) and negative shifts in investment in countries outside the US, negative shifts in saving (a larger budget deficit and household debt) and positive (though mild) shifts in investment within the US, and portfolio shifts toward US assets (which help to perpetuate the imbalances). By themselves, budget deficits should lead to higher interest rates or a weaker dollar. However, portfolio flows to the US are keeping interest rates artificially low. See Olivier Blanchard, "Notes on global imbalances," IMF Conference on Global Imbalances, April 2006.**

[3] **Karl Polanyi, *The Great Transformation: the political and economic origins of our time*, (1944).**

sustainable way between the rights of the individual and those of community and society.

From a practical point of view, such balances that Polanyi emphasises are difficult to achieve. In a range of European countries in recent decades, the challenges presented by inflation, unemployment and globalisation have made many people question the basic social balances achieved in the post-war era. Offshoots of that questioning include the difficulties experienced in the *banlieues* of Paris and the insecurities expressed around immigration and migration across the north.

State and market in Africa

For most developing countries, the articulation and implementation of a balanced public policy is an ongoing and relatively recent endeavour. For many African countries, policy is addressed in an environment of extreme deprivation, skills shortages and weak public institutions. Overcoming those constraints requires broad-based economic growth alongside the imposition of short-term costs that can be alleviated by policy. These 'core and periphery' challenges remain profound for countries that have no public systems for providing the sort of financial or in-kind transfers required to address the needs of those people too old, young, or poor to adapt well to change. [4]

Microeconomic policies to facilitate the shifting of people from old and non-competitive industries to new industries and new forms of economic activity are clearly important.[5] Such policies entail assertive re-skilling, high quality education, and access to social and other forms of capital to help and enable individuals to take advantage of new economic opportunities.

But such policies also entail the movement of people out of established and older communities and livelihoods and into new ones – repeating the conditions of social dislocation and misery described by Polanyi, which involved enclosure and the movement of people from rural to urban settings. And if there is one thing we know about societies it is that few of them embrace change as a way of life. Economic and social dislocation is experienced in the present, while the rewards of growth only in the future.

The distress of African economies and societies means, moreover, that the universal political calculus of assessing who reaps the rewards and suffers the costs of policy change is insufficient. A further delicate calculus is required to assess just how much instability an already fragile economic and social fabric can withstand. Will the political reaction to a reform confound the reform process in its entirety?

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[4] Issues around conditionality also impact on the interest of developing country governments to address these issues. See Nancy Birdsall, "Why it matters who runs the IMF and the World Bank," Centre for Global Development Working Paper #22, January 2003.

[5] Dani Rodrik, "Development strategies for the next century" Harvard University, February 2000.

The good news is that economic reform need not follow the standard Washington Consensus approach, even though most of the policies entailed in it are good for growth in themselves. The point is simply that since the 1980s, research on growth has generated lots of heat but also interesting perspectives. As Rodrik has highlighted, institutional development in an economy need not follow one model and is more likely to be successful if it respects and adapts to local characteristics. And many of the instances where countries successfully and sustainably increased the rate of economic growth, they frequently did it by targeting particular constraints to growth through quite limited reforms.[6]

Clearly, the state has an active role to play in most aspects of economic development, particularly in the ongoing effort to ensure that markets are efficient. But to be able to fulfil that regulatory role, Africa's states need to radically increase their capacity to define appropriate policies and to implement them. Institutional development is a prerequisite for policy definition and even more so for implementation. Regulatory systems and public institutions require the consistent application of skills and intellectual capital to create them and to sustain them. These are resources that are in short supply in developing countries, and in Africa in particular – suggesting the importance of the sustained provision of financial assistance and other means of freeing up resources for development.

Kermal Dervis has expressed the point well:

> As hard as it is to achieve, the world urgently needs a combination of substantial foreign aid in the form of grants, perhaps at least twice the amount that is currently available, with a mechanism to ensure that these resources are actually put to good use. There is really nothing that automatically leads to the inclusion in the world economy of countries that have been marginalised by history, geography, civil war, governance failures, and/or foreign power struggles on their soil. Globalisation does not "work" for these countries…. China and India can use the apparatus of the nation-state to "create" linkages between their own prosperous regions and their poor regions. Somalia and Sierra Leone can do very little on their own to create equivalent linkages between themselves and the dynamic parts of the world economy.[7]

Developing appropriate and effective state institutions will help developing countries to better address their international challenges. Yet many deplore the risks associated with globalisation – with economic integration and international finance – despite the potentially dramatic and positive implications for economic development. Countries need to have "the *desire* to integrate in the world

[6] **Dani Rodrik, "Getting institutions right," Harvard University, April 2004.**
[7] **Kermal Dervis with Ceren Ozer, *A Better Globalisation*, Center for Global Development, 2005.**

economy," just as they need to maintain macroeconomic policies that limit fiscal deficits and the build-up of debt.[8]

I have suggested that the development of domestic markets is needed in African economies. But it is also true that African economies are small – the South African economy with a GDP of about US$235 billion constitutes three-quarters of the GDP of Sub-Saharan Africa.[9] For that reason, regional and continental integration of markets is critical to market development, growth in nascent industries, and for diversification. Without serious advances in trade integration, Africa's economies will remain at the mercy of destabilising terms of trade shocks and other asymmetric shocks that can set development back by decades.

Yet to address those shocks and enable more appropriate trade regimes in Africa, related public institutions and systems again require extensive development. Most African economies retain fairly high trade barriers because of weaknesses in revenue collection from other forms of taxation. Reducing trade barriers, therefore, needs to be achieved alongside the development of effective revenue administration. Financial shocks emanating from the cessation or sudden resumption of foreign aid are also often destabilising, especially for African economies, because even small imbalances can disrupt thin markets, and because the adjustment process is often impeded, rather than facilitated, by the policy response.

In particular, adjustment processes usually place the burden of adjustment on politically under-represented social groups, leading to an increase and perpetuation of poverty. Some marginalised groups become permanently locked out of economic opportunity, distorting the distribution of income, reducing the potential growth of the economy, and giving rise to political instability.

Many of these sorts of political economy challenges would be made more tractable if the global trading environment supported production and exports from developing economies. Subsidies and protection perpetuates the dependence of African economies on colonial-era trading relationships and undermines the independence that most countries need to sustain development.

One means of addressing the dependence problem would be for Africa to coalesce national economic demands into politically sound regional economic institutions. This would provide Africa greater institutional leverage to address the need for a fairer global trade regime, some capacity to address the impact of capital flows, and reform of global economic governance.

I want to also suggest, and running contrary to much of the public discourse on the topic, that national sovereignty may be enhanced through integration, despite the piecemeal loss of sovereignty in some areas. When applied to the pressures

[8] Dani Rodrik, "Rethinking economic growth in developing countries," Harvard University, October 2004.
[9] Compared for interest with the annual revenue of Citigroup in 2005 of US$83.6 billion.

of globalisation, this thesis seems to me to hold even more strongly – globalisation can be addressed in regional and global institutions in such a way as to increase the power of states and better reflect the social and economic preferences of their citizens.

This idea seems especially pertinent and potentially rewarding in a regional context. Limited infrastructure, non-existent regulation or limited enforcement capacity, thin and undiversified markets for finance, goods and services all limit the extent to which African economies develop. Deeper regional cooperation could occur by basing regional economic communities in Africa on free trade agreements and customs unions of regional neighbours, and then progressively linking them to each other through phased reduction of tariffs and non-tariff barriers.

The practice of trade policy and its outcomes across the continent is of course diverse. While some regions remain in low-level equilibria, others have made great strides in bedding-down policy, creating better regulation and achieving macroeconomic stability, and are reaping the rewards in terms of higher investment and more rapid growth.

To get some sense of the macroeconomic improvement, the average inflation rate for Sub-Saharan Africa from 1995 to 2005 was 18 percent.[10] By 2005 this had fallen to 11 percent, and is expected to be about 8 percent in 2007. The average budget balance in the region is expected to be a surplus of 2.1 percent in 2006. And average GDP growth for 2005 was 5.5 percent and is expected to be 5.8 in 2006. Greatly improved macroeconomic performance will translate into rising employment and income over time, but remains insufficient to address the enormity of the poverty problems affecting the region. Roughly half the population continues to survive on less than $1 a day.

While the developing world has largely embraced the need to shift to open economies, greater competition, and the risks associated with getting policy right or wrong, the developed world continues to flirt with the opposite. Non-tariff barriers – such as phytosanitary criteria – stifle production in developing countries. The lack of progress on the current Doha round of trade talks reflects a disturbing level of insecurity about the economic future in developed economies.

Multilateral trade relationships also require a change in focus. Africa's approach to the WTO needs to emphasise long-term gains from progressive liberalisation, supported by the specific effort to remove trade-distorting subsidies in developed economies.[11] In some ways, agreement at a multilateral level may provide

[10] **Average inflation for the SSA region peaked at 61 percent in 1994. IMF, WEO 2006.**

[11] **According to a recent study, reduction of merchandise tariffs by developed countries and middle income countries, along with the decoupling of agricultural support and an end to agricultural export subsidies, would produce additional income for developing countries of nearly $350 billion, and would reduce the number of people living below the extreme poverty line of $1 per day by 61 million by 2015.**

momentum to efforts to rationalise Africa's regional trade blocs and lower tariffs remaining between the blocs.

The role of government in the economy therefore remains central to the task of making markets work for local communities and those without capital. Markets need to work with less rent-seeking and more efficiency as a policy rule to maximise investment, employment and growth in income. More generally, geographic and man-made constraints to growth should be priority targets for most African governments.

And in terms of the continent as a whole, public infrastructure development should be more aggressively aligned with the evolution of population centres, rather than remain relics of antiquated and obsolete colonial economic relationships.

As the Commission for Africa report points out, poor infrastructure remains a severe impediment to more rapid growth and poverty reduction:

> In some regions of Africa, farmers lose as much as half of what they produce for lack of adequate post-harvest storage. Across the region, women and girls currently walk an average of six kilometres to collect water. The life of those living in urban slums is made still worse by the lack of infrastructure – only seven percent have access to sewerage services for example, leading to economic costs in terms of health and lost work hours.[12]

Infrastructure needs have become more pressing as China, the US and other major world economies focus their attention ever more on Africa as a provider of raw materials. African countries need market development, efficient and fair public institutions and leadership, and major communications and transport infrastructure that reflects African economies, not just the needs of the world's greatest commodity importers. Africa's development and welfare depends in part on how commodity wealth is used to create intellectual, cultural and social wealth – and in part on how African states align policy for economic development beyond the production of commodities. In addition to institutions and markets, another key area of work is addressing the challenge of international finance, to which I now turn.

International finance and the international financial system

Some of the basic concerns raised by Polanyi about the role of public policy in national economies have regained their former importance because of the expansion of financial and capital markets.

[12] ***Commission for Africa Report*, page 233.**

Not unlike the 19th Century, free flows of capital today play a major role in determining what happens in national and regional economies. And although most of the developed world has moved to floating exchange rates to create room for manoeuvre relative to the international financial and capital markets, interaction with those markets remains largely mediated by fixed exchange rate policies in most of the developing world.[13] We should refresh our understanding of the burden of fixed exchange rates on policy orientation and the internal functioning of developing economies. As Polanyi noted in 1944 of the collapse of the Gold Standard:

> Currency had become the pivot of national politics. Under a modern money economy nobody could fail to experience daily the shrinking or expanding of the financial yardstick; populations became currency-conscious….

The international market forces that national governments contend with today are dynamic and dwarf public resources – daily turnover in global foreign exchange markets increased by nearly 40 percent in real terms between 2001 and 2004 to close to US$2 trillion. The South African rand share of total foreign exchange turnover doubled from 2001 to 2004 to nearly 1 percent.[14]

One of the key realisations in the aftermath of the Asian crisis (and reinforced by Argentina) was that different approaches to exchange rates and domestic regulatory institutions and governance matter, not just for prevention of crises but also for their resolution and the recovery of the stricken economies. To get a handle on domestic weaknesses that make economies prone to crisis, a range of emerging market economies were invited to the discussions on prevention and resolution and helped in the formulation of new codes and standards.

All of this has been immensely beneficial for the international financial system, the strengthening of regulatory and oversight functions in national systems, and the spreading of knowledge. Global economic governance, and hence reform of the international financial architecture, however, remains incomplete. We need a multilateral basis for overcoming future bouts of financial contagion – to maintain the connection between developing economies and international capital and goods markets and enable them to grow and reduce poverty.

At the same time, the international monetary and financial architecture that we have had since the creation of the Bretton Woods system has not kept pace with developments in these vast international markets. Regulation and systems for addressing market turbulence and failure are not adequate to the task they are confronted with. Neither the World Bank nor the International Monetary Fund has the financial or political clout to prevent financial crises, limit them when they

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[13] Inflows and outflows of capital (like shifts in stocks of gold under the 19th century gold standard) force domestic economic adjustment in countries with fixed exchange rates by directly decreasing or increasing the money supply and interest rates.
[14] Before dropping somewhat in 2005. See the Bank of International Settlements (BIS) Triennial Central Bank Survey (released in March 2005).

do occur, or even to materially help national governments to minimise the damage caused to economies by them.

The logical extension of the new role of emerging market economies and other developing countries would have been to reform the governance of multilateral institutions to enable them to take part in the decision making of those bodies. Not only would this strengthen reform efforts, and reduce the contingent costs of future crises, but would also strengthen the legitimacy of those institutions in other parts of the developing world – thereby helping to start developing countries on the right institutional and policy footing as they develop into emerging market economies.

The issue of the legitimacy of the international financial institutions (IFIs) becomes ever more salient when the costs and benefits of appropriately overcoming the problems of core and periphery are considered. How do the IFIs 'sell' the sort of radical policies that may be needed to help the rural Sahel dweller cope with economic change when their very legitimacy is so easily put into question? How effective is policy advice on the choice to privatise, corporatise, or to nationalise when too often it appears to be driven more by the prevailing political diet rather than a pragmatic assessment of the issues and a clear sense of the long-run public interest?

The impact of certain 'ideas' on advice can run far beyond what is necessitated by the logic of the original insight. To give an example, the IMF continued to advocate the adoption of fixed exchange rates for smaller economies long after there was evidence that international financial markets could distinguish between good and bad performing small economies – and hence small economies could attract more capital inflows by running more sound macroeconomic policies, in contrast to the prevailing wisdom of needing to "import credibility." The 'impossible trinity' wasn't broken in the process, but increasingly sophisticated and liquid financial markets in practice meant that the monetary choice for smaller open economies was no longer so biased towards giving up monetary sovereignty.[15] Smart policies could lower risk premiums and the interest rate spread paid over US treasury bills.

While the rapid development of international financial and capital markets makes life more risky in the sense that more is at stake, they also enable policy choices to be made that in the past were not possible. Policy makers can draw on a much wider array of experiences from more countries and regions of the world

[15] And in some sympathy with Stanley Fischer's "corners hypothesis" it also seems true that countries trying to manage somewhere between fully fixed and fully floating exchange rate regimes were at larger risk of international financial contagion, in part because investors' assessment of policies and decision making can be subject to significant error. As Paul Krugman (Slate, 1999) paraphrased the argument:

> **"[...] The point is that you can't have it all: A country must pick two out of three. It can fix its exchange rate without emasculating its central bank, but only by maintaining controls on capital flows (like China today); it can leave capital movement free but retain monetary autonomy, but only by letting the exchange rate fluctuate (like Britain--or Canada); or it can choose to leave capital free and stabilize the currency, but only by abandoning any ability to adjust interest rates to fight inflation or recession (like Argentina today, or for that matter most of Europe)."**

than ever before to exercise their responsibilities to pursue economic development in the public interest.

The IMF and the World Bank should, at the very least, be at the forefront of efforts to help emerging market economies and developing countries to overcome the constraints they face in accessing international capital or in responding to large and rapid inflows and outflows of capital. Few developing countries can borrow in their own currencies.[16] Borrowing costs can fluctuate greatly, especially for those countries borrowing in dollars. In the event of a currency crisis, interest payments in foreign currency rise, causing deeper recessions. Estimates by Hausmann and Rigobon show that after shocks debt to GDP ratios in a large sample of developing countries have risen 10-20 percent higher than would have been the case with debt denominated in local currency.[17]

One way of dealing with this was the Argentine approach of using a currency board, but this meant, as with any fixed exchange rate regime, that Argentina was adopting US monetary policy. In the 1990s, US dollar appreciation from massive and sustained capital inflows enabled the US to keep interest rates low, but reduced exports. High productivity growth in the US kept the economy growing, but the same could not be said for countries with dollar-debt. Slower growth in exports and lower productivity meant that those countries' service costs rose, and when growth slowed their debt and macroeconomic policies became less sustainable or unsustainable.[18]

At the same time, foreign debt makes it difficult to improve export growth through real depreciation of the exchange rate because the depreciation increases the debt burden and the cost of servicing it.

The upshot is that high foreign currency debt severely constrains policy – both fixing the exchange rate and deliberate depreciation can lead to crisis. All of this is exacerbated by the premiums developing countries are required to pay in order to borrow at all, which for *stable* emerging market borrowers over the past two years have fluctuated between 200 and 500 basis points above the yield on US Treasuries.

Now, consider the problem of African countries that depend on commodity exports, or any small number of exports that constitute the bulk of export earnings. With commodity prices declining over the past several decades, many developing countries don't even need to incur more foreign currency debt to become unsustainable – the trend decline in commodity prices does it for them at any given level of debt.

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[16] Barry Eichengreen and Ricardo Hausmann have termed this "original sin." See for instance Eichengreen and Hausmann, "Original Sin: The Road to Redemption," October 2003.
[17] Ricardo Hausmann and Roberto Rigobon, "IDA in UF: On the benefits of changing the currency denomination of concessional lending to low-income countries," draft paper.
[18] So long as it is not offset by lower inflation, lower productivity growth in one country in a fixed exchange rate regime results in a real appreciation of that country's exchange rate, reduced competitiveness and lower profitability.

In recent years, increases in debt predicated on a greater ability to finance repayments as a result of much higher commodity prices merely makes the problem even more pertinent – what will happen in the next few years if and when commodity prices fall?[19] From historical perspective, the lessons are evident. Oxfam's assessment of the effects of declining coffee prices on the Ugandan and Burundi economies is worth reviewing.[20] Burundi depends on coffee for about 80 percent of their total export revenue, so that a cut in prices of 50 percent results in a drop in total export revenue of 40 percent. Over the past year, the price for copper has increased by about 93 percent and by 52 percent since December 2005, vastly increasing the terms of trade of countries like Chile and Zambia and the contribution of copper to national income – but also creating the risk that inappropriate use of the increase in national wealth will end in economic disaster.

The dependence created by the inability of developing countries to raise foreign debt in their own currency could be broken in various ways. Some analysts have suggested that the International Development Association (IDA) lend to developing countries using an inflation-indexed domestic currency unit of account.[21] This could be created from a basket of developing country currencies in order to spread risk, and would require only a very marginal increase in yields to compensate for the additional risk. In times of economic stress, debt burdens would not rise, GDP would be less volatile, and overall welfare significantly improved.

The African continent in particular is highly vulnerable to shocks, be they a sudden drop in the price of an important export commodity, a drought, or exchange rate devaluation. The frequency and severity of shocks has been growing. For example, a Commission for Africa background paper pointed out that 44 African countries have suffered natural disasters in the last 10 years.[22] In addition, 28 African countries are judged to be potentially vulnerable to aid shocks, due to their high aid dependency ratios, and 24 countries are very vulnerable to export shocks, because they depend on only one product for more than 50 percent of their export revenues. And at least 13 African countries have suffered foreign private capital crises over the past 10 years.

Mechanisms for addressing volatile prices for goods on which many countries' economic fortunes are largely or wholly dependent would seem to be a useful thing for the IFIs to focus on, even if not especially novel. At the same time, forms of financial assistance to address balance of payments crises of a broader nature – such as those initiated by financial contagion – should be an important aspect of any serious effort to revamp the tools of the IMF.

Concluding comments

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[19] **This need not be a short-term nominal decline, it can also be a more drawn-out real price fall.**
[20] **Oxfam, *Mugged: Poverty in your coffee cup*, or "Europe and the coffee crisis: a plan for action," OXFAM Briefing Paper 36.**
[21] **Ricardo Hausmann and Roberto Rigobon, "IDA in UF: On the benefits of changing the currency denomination of concessional lending to low-income countries," draft paper.**
[22] **Martin and Bargawi (2004). *Protecting Africa against "Shocks"*, Africa Commission Background Paper.**

The importance of addressing the international environment has been deepened by globalisation, forcing states to adapt to fulfil their old functions. For African states to balance the distribution of economic burdens and opportunities requires creativity and active, capable state institutions – governance reforms and technical capacity building should go hand-in-hand. They need to be inventive and devise new policies and new ways of resolving the problems caused by globalisation – achieving the balances highlighted by Polanyi of providing economic security and income stability at the same time as they encourage economic activity.

Chalmers Johnson's 'developmental state' – implying conscious proactive policy articulation and implementation – is a useful model for most developing countries, in part because of the need to prevent domination of underdeveloped and under-regulated markets by local and international firms and elites with excessive market power.[23]

The idea of the developmental state also reminds us of the importance of public services and basic fairness in the interaction between communities and markets – enabling people to engage in economic activity and protecting them from those who would abuse the predisposition of democracies towards freedom. In large part, the means of achieving those aims is by providing certain types of freedoms to all members of the community. As Amartya Sen has put it: "Development can be seen… as a process of expanding the real freedoms that people enjoy," and by "the removal of major sources of unfreedom: poverty as well as tyranny, poor economic opportunities as well as social deprivation, neglect of public facilities as well as intolerance or over-activity of repressive states."[24]

State capacity and institutional development also matters for how societies respond to the international environment. Weak states tend to view international economic integration as a threat, but integration, like other policy choices, should be subject to economic cost-benefit assessment. National sovereignty may be enhanced through integration, as economic development creates the resources for better defined and implemented policies and public services in areas that matter more – such as education and health. Globalisation too can be addressed in such a way as to increase the power of states and better reflect the social and economic preferences of their citizens. But getting there requires us to see institutional design and the skills to make institutions effective as a clear and critical need for most African countries.

Within the international system, we need to ensure that our multilateral institutions help African and other developing countries to address these issues. Tying us together as an international community, the Monterrey Consensus forged a partnership to address the economic aspects of our problems. Developing countries were meant to undertake policy and institutional reforms.

[23] **Chalmers Johnson, *The Developmental State*, 1999.**
[24] **Amartya Sen, *Development as Freedom*, 1999.**

Developed countries agreed to assist in those efforts and to create an enabling international economic environment.

Tragically, we have made little progress on much of the Consensus. Far too many of the policies and practices of developed countries weigh against it – cultural exclusion, economic protection, political manipulation and favouritism have not disappeared with the dismantling of the Berlin Wall. The underlying disorders are generated, mostly unconsciously and indirectly, from the interaction of insecurity and the need for change that come together in national political systems. That they influence the neutral-sounding processes like donor aid, trade negotiations, and international financial architecture that developing countries depend on for their own development remains intensely problematic.

The drive at the international level – from Monterrey through Gleneagles – has been to win agreement that large chunks of new financial assistance are required up front to lay the basis for countries to develop beyond reliance on foreign financial aid. The means for ensuring that funds are used in a transparent and accountable way – one of the primary complaints of donors – are there. Great strides have been made to set out principles by which the present bureaucratic clutter that passes for aid systems can be cleaned up and made transparent. Direct budget support and other channels for aid can be easily monitored to increase accountability. Stronger government systems – for finance, policy development and implementation – will provide the returns to the upfront assistance by directly reducing the dependence of poor countries on assistance in the first place.

At the Gleneagles Summit – which occurred precisely a year ago – the G8 committed to increasing their aid to Africa by US$25 billion per annum by 2010. Preliminary data shows ODA to developing countries from G8 members increased by US$21 billion in 2005. However, US$17 billion of this went towards writing off debts in Nigeria and Iraq. In its analysis, the DATA report[25] argues that in order to make progress towards the 2010 goal, G8 donors will have to increase their development assistance to Africa by US$ 4 billion each year for the next 5 years.

Insufficient and badly directed development finance, poor advice on policy, difficult questions of trade protection, and inadequate international financial systems all point to the inadequacy of the current decision-making structures for international economic affairs. Reform is necessary, and in my view, if developing countries had a greater say in the running of these institutions, there would be a greater sense of ownership and legitimacy.

In a world of volatile capital flows, powerful financial markets, and destabilising macroeconomic policy decisions, the major financial contributors to the IMF and

[25] **A pressure group founded by Bono and members of the Jubilee Drop the Debt campaign, who have released their summary analysis of the G8's promised to Africa to date on 29 June 2006 (www.data.org)**

World Bank need to recognise the prudential character of reform as the financial costs associated with crisis grow ever higher.

That hope, however, is merely a reflection of a more general point – that for too many societies around the world the idea of a reasonably stable international financial and economic order is quickly becoming a remnant of a multilateral past – even as the social and economic implications of our deeper interdependence raise the risks associated with economic integration.

Where poverty is so pervasive, we need to make certain that the touch of globalisation on our most marginalised populations lifts and nurtures rather than condemns. That is the central task confronting us as leaders in the developing world and as members of the international community if we want to support economic integration and realise human development.