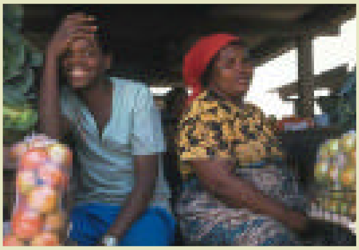
Asia and Africa in the Global Economy

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Introduction: Sub-Saharan Africa and Southeast Asia in the Global Economy

Background

Since the growth performance of Southeast Asia (SE Asia) and Sub-Saharan Africa (SSA) began to diverge markedly in the 1980s, the highly positive economic performance of Southeast Asia in the precrisis period had frequently been juxtaposed with the much less commendable achievements of Sub-Saharan Africa in the past. (See Table 1.1 and Figure 1.1 for comparative economic growth performance of Asia and Africa during this period). While the performance at both the macro- and micro levels show great disparity, one of the most obvious differences in the performance and economic structure of the two regions has been the extent of participation in the global economy. As Asia has increased its participation in the world economy so has Africa shrunk its participation. Prior to the onset of the Asian crisis in 1997, the economic performance of four Southeast Asian countries – Indonesia, Malaysia, Singapore, and Thailand – was popularly regarded as a ''miracle'' along with that of other high-performing economies of Northeast Asia, i.e., Japan, Hong Kong, South Korea, and Taiwan. Their development experiences were popularly presented to policy makers in Africa as attractive examples to draw lessons from.

Indeed, following aggressively the ''outward-oriented development strategy,'' many East Asian economies had not only accelerated the process of integration into the world economy but also upgraded their modes

Table 1.1 Growth in GDP per Capita % per Annum for 1961–1996

	1961–72	1973–80	1981–90	1986–96
Africa	1.3	0.7	−0.9	−1.0
East Asia	7.0	7.1	9.4	7.2
Southeast Asia	3.2	4.9	4.3	6.6[a]
South Asia	1.3	1.6	3.3	2.9

Source: World Bank, Economic and Social Database.
a. Malaysia, Indonesia, Thailand only for 1985–1995.

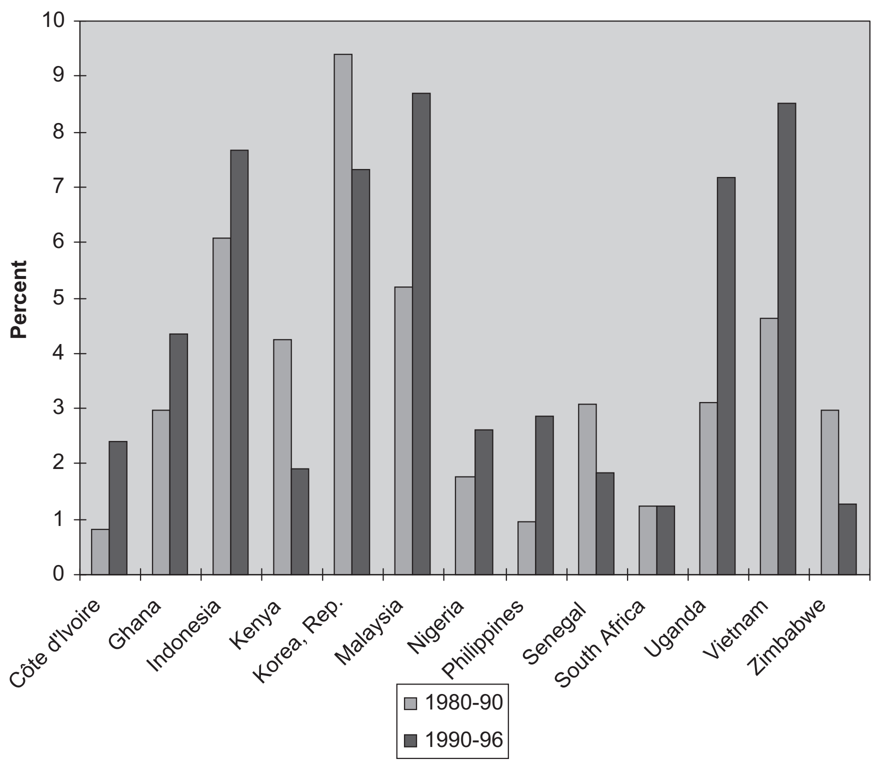

Figure 1.1 Average Annual Growth of GDP, 1980–1996

of linkages in the years of their rapid economic growth. In contrast, the majority of SSA countries had failed to take advantage of the opportunities provided by increasing international economic interactions. In the 1970s and 1980s, instead of becoming more integrated into the world economy, they were largely marginalised and experienced slow growth and stagnation. With growing recognition of their disadvantageous positions, over the past decade SSA countries have increasingly searched for ways to accelerate their participation in the global economy.

Interestingly, the East Asian crisis erupted in the wake of this gradual embrace of globalization by African countries.[1] The crisis, which started as a financial crisis arising primarily as financial *excess*, not a crisis of fundamentals, has clearly exposed the severe difficulties in managing national economies in the highly regionally integrated and globalizing environments. The event has helped to raise a critical question for Sub-Saharan Africa: how to manage the process of *strategic integration* into the global economy. As Senbet notes, the lessons from the Asian crisis, if drawn correctly, can help SSA countries to draw a strategy towards sustainable globalization.[2]

The question of strategic integration is important for several reasons. First, as globalization is not a process proceeding neutrally in a policy vacuum, there is a significant degree of discretion in policies towards integration. The forms of integration are likely to be greatly affected by national policies towards the multidimensional process of integration, including policies on trade, finance, technology, industrial structure, competition, and migration. The optimal level of openness may differ for each aspect, which itself depends critically on the stage of development among other factors. This leads to a strategic question: what is the best policy mix to achieve integration, or what is a measured and properly sequenced set of policies towards trade, foreign direct investment, and capital flows?

Certainly, the excessive pace and incorrect sequencing of liberalisation in an attempt to reap greater benefits from the globalization process can result in severe difficulties. The severity of problems that can arise from mismanagement of financial policies in particular has been amply demonstrated by the recent Asian and global financial crises. It has shown that the risks associated with financial globalization are high, as international capital flows are inherently volatile, which can expose vulnerable and fragile economies to highly volatile external forces.[3] Thus, opening up the economies to the powerful external forces shaping the globalization process requires careful strategic thinking with regard to the forms, pace, sequencing, phasing, and time frame for integrating the economy more fully into the global economy.

Secondly, the benefits from globalization are unevenly distributed. It has been observed that income levels tend to diverge rather than converge among participating national economies and across regions as globalization proceeds. There are winners and losers from the ongoing process and income inequality tends to be amplified. Moreover, net benefits from globalization are not necessarily guaranteed. Depending on the nature and forms of integration, countries may benefit from dynamism and growth within the global economy, but integration into the international economy by itself does not ensure these benefits. Furthermore, the initial adjustment costs arising out of increased integration may include worsening poverty for some groups.

Thus, while potentially offering participating countries new opportunities for accelerating growth and development, increased integration also poses great challenges for economic management problems policy makers have to engage with. This is particularly the case since risks and costs involved in integration can be large for fragile low-income economies. Such risks and costs have sparked a heated debate on net gains/costs associated with the globalization trend and generated many theoretical and empirical studies on the *globalization-growth-income distribution nexus* and the *income convergence* thesis. They have also led to vibrant antiglobalization protests worldwide, reflecting a widespread unease with the globalization process.

Discussions of what accounts for the divergence of growth and development between Africa and Asia have so far been held in terms of factors including differences in economic policies, initial development conditions, and resource endowments; the geopolitical ties to the industrial economies; domestic governance arrangements; culture and its role in economic decision making; etc. While the scope of the list may vary considerably, depending on which countries are being compared, the fact that a combination of policy, institutional, and structural conditions explains crucial developmental differences is quite generally accepted. What is not in general agreement is the relative weight to be attached to each of these three categories and the manner in which they interacted.

On the policy front, the divergence of the growth performance in the two regions has been largely attributed to the contrasting policies adopted towards international trade and investment. In particular, the debate has been conducted in a sharply dichotomous way – between outward-oriented versus inward-oriented strategy, export promotion versus import substitution, or interventionist versus laissez-faire approaches. A consequence of these different policy orientations of the two regions is also reflected in their institutional developments. It has been argued that institutional environments which prevailed in East Asia are conducive to private investment, while African institutions often widened and deepened the state's role in all facets of economic decision making, in a way that minimised private risk taking and hence investments. Naturally, policies and institutions have interacted with other conditions, such as initial resource endowments or political, social, and cultural factors, to produce diverse savings-investment-growth nexuses in the two regions.

There are several studies, including the East Asian Miracle study,[4] which examine key conditions for success of economic management in

East Asian countries and draw lessons from the Asian experiences for the other developing countries. They suggest that policy choices that included maintaining sound fundamentals like a stable macroeconomy, high human capital, effective and secure financial systems, and openness to foreign technology were mixed with selective interventions that included export push, financial repression, directed credit, and selective promotion of industries. These policies worked within an institutional framework that was characterised by technocratic insulation, high-quality civil service, and sound monitoring. The outcome was the competitive discipline that led to accumulation of human capital, high savings, and high investment, as well as efficient allocation through the effective use of the human capital and high returns on investment. In addition to accumulation and efficient allocation, there was productivity change coming from productivity-based catching up and rapid technological change. The outcome of these processes is the achievement of rapid and sustained growth as well as a more equal income distribution.

However, the World Bank study rejects the replicability and appropriateness of interventionist policies for other developing countries and recommends that they focus on fundamentals and thereby create a market-friendly environment rather than on getting interventions to work. A similar position is taken by Lindauer and Roemer.[5] They suggest that Southeast Asia, in preference to East Asia, would be a good model for Africa on account of institutional legacies and human resource endowments. However, these policy conclusions have been severely challenged by a number of academics for failing to understand the interdependence between fundamentals and selective interventions as well as between economic policies and institutional factors.[6] Clearly, for more meaningful comparative studies, it is crucial to take one step back from such over-simplified generalised conclusions.

This book is a systematic attempt to decipher different experiences in Sub-Saharan Africa and Southeast Asia as they have interacted with an ever changing global economy, with a view to understanding economic policies and institutional environments in the two regions that could account for their diverse development outcomes. The book is a collection of the selected papers that were first presented at the International Conference, "Asia and Africa in the Global Economy," in Tokyo in August 1998, in the background of the unfolding Asian and global financial crisis. The Conference was organised jointly by the United Nations University and the African Economic Research Consortium (AERC), and it was the second workshop jointly hosted by the two institutions to discuss comparative development experiences in Africa and Asia.[7] While the first workshop covered both Northeast Asia and Southeast Asia concerning the wide-ranging macroeconomic and sectoral aspects in comparison with those of Sub-Saharan African countries, the scope of the second workshop was narrower, with a focus on the comparison between Southeast Asia and Sub-Saharan Africa in the background of the globalization process. Many of the papers were revised subsequently, taking into account fast evolving events both in Southeast Asia and Sub-Saharan Africa.

Book Outline

The book contains thirteen other chapters that focus on specific issues considered relevant to presenting the circumstances under which African nations were held back from active participation in global markets, while the Asian economies were fast expanding their participation. All contributors to this volume accept the key role that engagement with the global economy played in advancing the development paths of the high-performing Southeast Asian economies. This Southeast Asian experience is a sharp contrast with that of the countries in Sub-Saharan Africa. Thus, we proceed from the position that the integration of these economies into the global economy facilitated access to resources and markets that helped to transform production and improve productivity significantly. We all recognise the importance that both policies and institutional development played in facilitating this integration into the world economy. However, while sharing this common ground, each contributor tries to explore different aspects of the development path of the two regions from her or his own perspective.

The Dynamics of Globalization

The book starts with a discussion of the extent of globalization by Laurence Harris (Chapter 2). The chapter presents what Harris calls "eight sceptical theses" on the dynamics of globalization. While Harris points out that the process that is today widely referred to as globalization has been significant over the last three decades, there is no need to believe that individual economies are no longer in a position to influence their own roles in the rapidly changing world economy. Harris first sees the so-called globalized economy as a *fractured* one, since international flows of trade and investment have formed regional blocs rather than a unified global economy. There is still no indication of a movement towards the law of one price, a hallmark of integration, a major indicator of globalization. What the recent trend in global flows suggests is therefore "an accentuated tendency towards greater interaction and integration, a tendency towards a greater degree of globalization."

Harris also suggests that some trends that have been seen as leading inexorably towards more general globalization will not necessarily continue into the future; they may be seen, instead, as a temporary "catching up," restoring international economic relations to a level of integration comparable to the pre-1914 world economy. He envisages that the recent trends may even be temporarily reversed by renewed protectionism, instability, or world depression anytime in the future. Furthermore, the progress of globalization will meet obstacles in the diversity of countries' forms of organisation, economic structures, and economic behaviour. Therefore, the existence of cultural and historical specificity will create lasting obstacles to globalization and is not obliterated by international competition itself. Consequently, it cannot be expected that economic development will be based on a tendency for ever-fuller globalization. In the end, national economic sovereignty will prevail, as obstacles to further globalization are created by the specifics of the culture and history of countries.

Economic Policies and External Performances

Chapter 3, by Ernest Aryeetey and Machiko Nissanke, presents a systematic comparison of a number of factors and conditions in Southeast Asia and Africa that influenced the integration or the lack of integration, as the case may be. In particular, it explores the critical interrelationships between the economic policies and the external performances of the two regions in a comparative perspective intent on identifying policies that worked best in different areas and the conditions under which their effectiveness was achieved. The chapter first compares East Asia and Sub-Saharan Africa in terms of initial conditions and resource endowments in order to set a context for comparative analysis of the two regions. It then proceeds with a discussion of summary statistics of external performance and the differences in the degree and forms of integration into the global economy and the internal and external conditions that influenced the development policy orientation of the two regions in relation to international transactions. On the basis of these detailed analyses of several critical factors and conditions, the chapter examines various economic policies that influenced the international linkages in the two regions.

Aryeetey and Nissanke present different strategies followed in the two regions, reflecting their respective internal and external conditions. They argue that Africa's initial apparent disengagement from the global economy was the result of a deliberate effort to reduce its dependence, an approach that was driven in many nations by the political imperatives of the time soon after independence. That global economy was seen as being dominated by the same colonial governments that African nations had fought to free themselves of. Based on the pervasive clamour for independence and a fear of neocolonialism through private economic agents, the role of the state and its institutions for safeguarding independence became more important than any other consideration. It was this fear that did not encourage the development of institutions that would foster private participation in the economies of Africa. As private participation was reduced, the pressure to be innovative in production, seek productivity-enhancing technologies, search for international capital, and seek international markets for new sets of goods and services was reduced.

Yet, the capacity of African states as economic agents was severely compromised as the state machinery in many countries was captured by distinct interest groups. This condition, described as "urban bias" by Bates,[8] led to the maintenance of inappropriate macroeconomic and trade policies. In particular, the intervention by the state in the functioning of markets went beyond simple ownership of the capital stock. It affected adversely the interests of exporters through the maintenance of unhealthy producer prices for primary commodities, unrealistic exchange rates, and fiscal programmes that eventually broke the treasury and destabilised economies.

Turning to Southeast Asia, Aryeetey and Nissanke note both the similarities and differences in internal and external conditions. Nation states in Southeast Asia were, as in SSA, created as by-products of European colonialism, with the notable exception of Thailand. Compared to the Northeast Asian economies, they are far less homogeneous in terms of ethnicity, culture, and religious heritage, which has undermined the emergence and sustenance of economic nationalism. Consequently, the basis of developmental states is weaker in Southeast Asia than in Northeast Asia, and successive governments have found the process of policy reform hampered by the need to appease different constituencies based on regional, religious, or ethnic groups. Generally, while local entrepreneurs have not advanced effectively the national agenda of late industrialisation, the interests of foreign business have been promoted above those of the local business community.

However, importantly, in contrast to SSA, technocrats in Southeast Asia have had a considerable degree of autonomy in the area of macroeconomic management. Further, effective alliances were forged from time to time between technocratic advisors, key politicians, and business groups to foster economic growth and investment. Considerable investments were made in agricultural expansion and rural development in the early years, and a large number of labourers were absorbed into the industrial sector as industrialisation proceeded rapidly after the 1970s. Further, in the 1980s and 1990s, Southeast Asian economies have benefited from positive regional effects. The growth and structural transformation of the Southeast Asian economies has been greatly facilitated by the pan-East-Asian dynamism associated with regional industrial restructuring. Direct investment flows by Northeast Asian firms have intensified and accelerated the process of widening and deepening manufacturing networks in the region. Overseas Chinese traders have also played a crucial role in generating dynamism in Southeast Asia.

Reflecting these differences in these historically evolved political and institutional conditions, Aryeetey and Nissanke argue that policies adopted towards international trade and investment in the two regions have varied considerably.

In SSA, the trade policy regimes that prevailed between the time of independence and the adoption of Structural Adjustment Programmes were truly inward looking on both the import and export sides, so that many economies were locked in a permanently de-linked position from the world economy. Protections provided were neither time bound nor performance linked. They could not be used as an effective means to graduate infant industries from protection. Little thought was given to a strategic dynamic path of the trade regimes which should be evolved as industrialisation and economic development proceeds. The need for raising the export-earning capacity was neglected, which was extremely detrimental for a foreign exchange-constrained economy, such as the economies of most of SSA countries with their high dependence on imports for intermediate and capital goods.

In the absence of appropriate coordination among trade, industrial, and technology policies, industrialisation strategies implemented in SSA did not have the required internal consistency and coherence, producing poor results. While trade and investment liberalisation carried a great weight in the Structural Adjustment Programmes, given the unfortunate past experience with the interventionist regimes, strategic visions for development embedded in sectoral policies have been altogether discarded.

In contrast, in Southeast Asia, import substitution strategies were not pursued in a manner as inward looking. Most Southeast Asian economies remained open to the global economy even at the height of the import substitution phase, through exports of primary commodities or processed products. The primary-commodity sector was encouraged to develop as a main source of earning foreign exchange and never penalised. Outward orientation was present throughout, maintaining strong trading links with the world economy. Besides, while industrial development was initially carried out under the regime of import substitution, the growth and diversification of industrial products were realised with the timely adoption of export-promoting measures. Undoubtedly, it is the success of export promotion of selective manufacturing activities that has changed the industrial landscape of these economies. In short, export promotion and import substitution were the two, equally critical, pillars of their outward-oriented industrialisation strategy.

Moreover, import liberalisation was carried out in stages to ensure soft landing to import-substituting industries. While industrial policy lacked coherence compared with Northeast Asian economies and the dependence on FDI has been high, extensive proactive state interventions in facilitating export growth were instrumental for the remarkable success in trade and investment performance in Southeast Asia.

Aryeetey and Nissanke conclude that, despite some similarities, there are critical differences between the two regions in their policy design and implementation context. In particular, they emphasise the need for differentiating between strategic integration and laissez-faire liberalisation in formulating policies intended for achieving integration into the global economy.

Institutions and External Performance in Africa

Chapter 4, by Beatrice Weder, uses internationally available data to look at the possible relationship between the performance of exports from Africa and the nature of Africa's institutions. The variables of interest include the accountability of rule-making, the security of property rights, the predictability of laws, corruption, and political instability. She finds that for a subset of her sample African countries, variations in export performance are best explained by differences in the security of property rights and the rule of law. Her results do not change even after controlling for differences in income, policy distortions, and other measures of political instability. It is also interesting that Weder does not find a relationship between the perceived security of property rights and ethno-cultural factors, including the extent of ethnic division.

The significance of property rights and economic performance in developing countries has been prominent in the literature in the last decade. The work of Knack and Keefer[9] and the recent piece by de Soto[10] have helped to push to the fore the issue of property rights security. While the intuitive nature of the relationship between poor security of property rights and the performance of an economy is appealing, particularly with respect to the likely impact on foreign investors, there is no clear agreement on the means by which the perception of poor security translates into specific investment decisions by different categories of investors, including local producers of export commodities. Even less clear is how this impacts directly on economic performance.

The need to take a more nuanced approach to the relationship between governmental actions and responses of private economic agents and their impact on the economic activity underlies a lot of the discussion in this volume. While the volume accepts the need for governments to pursue strong measures that will secure property rights as a way of enhancing access to international resources and the integration of African economies into the global economy, it is recognised that the security of property rights needs to be a part of a broader institutional development process that builds on local cultural values and societal goals and the perceived direction of the future interaction between the domestic economy and the world economy. In this situation, secure property rights for foreign investors are as important as they are for small domestic producers. It is recognised that a lot of the governance improvement attempts of the last decade in Africa seek to achieve this objective. Obviously the impact of this will be deeper if other aspects of good governance are treated as complementary in this process.

Local Entrepreneurship in Southeast Asia and Sub-Saharan Africa

Chapter 5, by Deborah Brautigam, is an attempt to show the underlying microlevel economic and institutional interactions that facilitated the different perspectives of private economic agents in the two regions. She suggests that the institutional differences have a longer history than recent literature would tend to suggest. A part of the industrial course that Southeast Asia has taken is derived from the fact that Southeast Asia was linked to the great maritime routes of the East, between China and India. Africa had not had an equally significant link to any major world trading routes until the beginning of the slave trade. The latter marked the beginning of the most important but largely negative trading link of Africa with the outside world.

In the era of colonialism Africans were prevented from accumulating capital in any significant way as European institutions acted in concert to concentrate capital in the hands of European trading businesses in Africa. They had no interest in manufacturing. In contrast, entrepreneurs from China, India, Europe, and Japan were already involved in serious manufacturing by 1941 in Southeast Asia. Foreign manufacturing entrepreneurs did not arrive in Africa until much later, indeed, not until later in the nineteenth century. It was therefore not surprising that Southeast Asia moved into manufacturing long before Africa introduced ISI after independence.

Brautigam looks at the processes for developing local entrepreneurship in the two regions in terms of entrepreneurial accumulation, network formation, and global linkages. She suggests that the Chinese and Indian networks in Southeast Asia are legendary, as are some of the networks of traders known in West Africa. The solidarity networks for countering uncertainty and information networks for spreading knowledge are useful for developing links to the global economy in so far as they facilitate access to resources not immediately available in the local community. Such networks have historically been extremely useful in allowing resources and ideas to come from outside, as well as in facilitating access to the state, a fact that explains the ability of some groups to embark on dynamic industrialisation. In Asia, as new institutions emerged to provide some of the benefits that networks provide, a change in the dynamics also emerged to allow entrepreneurs to become more global in their dealings. Such institutions have been slower in emerging in Africa, thus leaving the networks to continue with the age-old practices of minimising risk in smaller geographical areas.

Brautigam further notes that the role played by local entrepreneurs in the development of foreign joint ventures has been much stronger in Southeast Asia than in Africa. In this respect, she emphasises the special role played by Japanese investors, often as minority partners and acting in concert with locals who controlled major distribution networks throughout the region. Their manner was different from European traders in Africa. The joint ventures brought newer technology and facilitated the transformation of small businesses into more modern commercial ventures on a scale much larger than in Africa. The obvious policy conclusion for Africa would be to develop institutions that create opportunities for indigenous networks to increasingly interact with the rest of the world and obtain access to technology, markets, and resources.

Resource Exports and Resource Processing for Export in Southeast Asia

The Southeast Asia region has undergone considerable structural change over the last three decades, moving from economies dominated by primary exports to ones dominated by manufactured exports and other processed agricultural goods. Even in the area of primary agricultural exports, countries like Malaysia, Thailand, and Indonesia have witnessed a significant expansion in the range of exported goods. In Chapter 6 on the process of structural transformation in Southeast Asia, Jomo and Rock emphasise the significant role played by the state in achieving the desired diversification after several years of narrow export bases that had been developed on the lines of "natural protection." They suggest that the capacity and ability of local entrepreneurs to take advantage of the natural protection offered by rich resources and geography created the flexibility that allowed the postcolonial governments to build on them for export diversification.

Particularly, they strongly argue that the neoliberal interpretation of the state in the second tier newly industrialising countries (NICs) in

Southeast Asia is, at best, an oversimplification. The latter interpretation suggests that selective interventions in these economies have been incoherent, subject to wasteful rent seeking, and irrelevant to their development successes in recent decades. It also regards the recent financial crises as evidence of the failure of such incoherent and rent-seeking micropolicies. However, in reality, governments in the three second-tier NICs, instead of simply relying on static comparative advantage or indulging in wasteful rent-seeking policies, all intervened selectively to diversify their economies away from primary exports. Selective interventions covered a range of activities. Initially, resource rents were used and distributed in the form of selective incentives to promote import substitution industrialisation (ISI). When the returns to ISI declined, selective incentives were put in place to promote export-oriented manufactures, including resource-based industries.

Jomo and Rock note the wide-ranging measures taken by the state in export diversification. The measures covered initiatives in research and extension which were crucial for crop diversification, as well as mineral exploration and geological surveys that have been essential for developing the minerals and oil sectors, especially in Indonesia. There have also been government subsidies, direct protection to support import-substituting industries as well as export-oriented industrialisation. In many cases, intervention took the form of the state seeking to reduce the private costs of entrepreneurs in selected areas and enhancing social benefits as private benefits rose. Rents were shared between the state and the private sector in many instances.

Thus, Jomo and Rock show how selective promotion of export-oriented resource-based industries yielded handsome returns in promoting new crops (such as oil palm in Malaysia and Indonesia and cassava in Thailand) or new resource-processing industries, such as the plywood industry in Indonesia and the prepared meat (primarily chicken exports) industry in Thailand. They emphasise that in each instance, selective incentives figured significantly in the development of internationally competitive industrial capabilities. Their nuanced microanalysis also identifies and critically examines failed government interventions in these countries. However, they emphasise that the recognition of wasteful rent-seeking behavior should be analytically distinguished from developmental interventions successfully offering rents as incentives to motivate desired economic responses.

Primary Exports and Primary Processing for Export in Sub-Saharan Africa

SSA has lost its share of world exports by over 250% over the last thirty years. All categories of exports for all subregions in SSA, including South

Africa, have faced drastic falls in export earnings. As a result, SSA faced serious import compression particularly during the 1980s. While the exports of manufactures have not been anywhere near the targets that many countries have set for themselves, the performance of primary exports has steadily deteriorated, with a sharp decline in market shares for some major commodities. Chapter 7, by William Lyakurwa, argues that, while primary exports remain the most critical link to the global economy for many countries in Sub-Saharan Africa, the importance of the primary-sector exports were underplayed in the early postindependence periods, faced with the expected long-term decline in primary-commodity export prices. As Lyakurwa shows, however, the liberal economic reforms under the Structural Adjustment Programmes have not arrested the steady declining trend in primary exports, while export diversification has yet not taken place on a visible scale. Lyakurwa's econometric investigation of factors behind the discouraging export performance suggests that primary commodity exports have been affected significantly by unstable macroeconomic conditions. He further notes that the poor state of infrastructure in most of Africa, influenced by lagging gross domestic investment, turns out to be important and significant for explaining the poor trend in primary exports.

He concludes that it is crucial to account for institutional developments in order to appreciate more fully the obstacles to export diversification. Indeed, the Southeast Asian experience with export diversification suggests the importance of developing a strong private-sector capacity to respond to government incentives and initiatives. In addition to the broad policy support that is necessary for private-sector engagement, institutional developments will have to be those that can enhance private participation in the economy, particularly in new sectors that enhance exports. Rents accruing to governments will have to be distributed and used so as to encourage new productive areas.

Export-Oriented Industrialisation and Foreign Direct Investment in the ASEAN Countries

While SSA countries continue to find it hard to diversify their exports through industrialisation, Southeast Asian countries have succeeded in the diversification process by effectively using foreign direct investment (FDI). Even though countries in both regions started out showing little or no interest in FDI, this changed rapidly in Southeast Asia, following the Singaporean experience in the early 1970s. Chapter 8, by Thee Kian Wie, discusses the rapid industrial growth and transformation which the ASEAN countries, particularly Indonesia, Malaysia, Singapore, and Thailand, experienced from the mid-1960s through the mid-1990s. In this respect, he presents an interesting chronology of developments that led to the change in policy and attitudes towards FDI for export-oriented industrialisation in Singapore, Malaysia, Thailand, Indonesia, and the Philippines. He evaluates the role of FDI in the industrial development, which was facilitated by this policy shift. In particular, Thee Kian Wee emphasises the importance of foreign direct investment in promoting industrial and technological development by building up a pool of highly skilled managers, technicians, and workers. His analysis shows how foreign direct investment could facilitate the development of economically viable supporting industries, producing a wide range of intermediate inputs for the downstream assembling industries.

However, he also argues that, unlike Singapore and to some extent Malaysia, the other Southeast Asian economies have had difficulty in getting foreign technology applied in a broader spread of the industrial production chain. In this respect, he suggests the critical importance of enhancing the indigenous technological capabilities through the transfer of knowledge from MNCs to local SMEs for sustained economic growth.

Export-Oriented Industrialisation and Foreign Direct Investment in Africa

Chapter 9, by Charles Soludo, argues that export-oriented industrialisation provides the best strategy that could potentially reinvigorate Africa's stalled industrialisation process. However, it is clear that, despite nearly two decades of trade and structural reforms at the behest of the BWIs, industrialisation buoyed by FDI and export orientation has yet to happen. In his view, despite concerted efforts at export orientation, FDI is also unlikely to become a significant African phenomenon in the near future unless some fundamental transformation of the socioeconomic, infrastructural, and institutional arrangements takes place. His arguments are based on his analysis of factors that provide explanations for the slow growth of industrialisation beyond the inadequacy of the macroeconomic environment. Many problems arise from the initial conditions, including infrastructure, capacity and institutional constraints, and other factors, both internal and external. He also highlights the relative absence of an appropriate sociopolitical environment.

After discussing the "accumulationist" and "assimilationist" explanations of the successful economic transformation in East Asia, Soludo raises the question of whether those experiences are replicable in Africa. He suggests that both the more interventionist experience of Northeast Asia and the more liberal Southeast Asia experience may offer lessons for Africa, so long as the obstacles to emulating those approaches effectively are removed. These obstacles centre on the capacity of the state to develop and implement an appropriate policy regime. Importantly, he argues, something beyond ‘‘getting the fundamentals right’’ or ‘‘state interventions through industrial policy’’ is required to create the necessary locational and competitive advantages for industrialisation and FDI to happen. He notes that a majority of countries in SSA are preeminently at a preindustrial stage and are still waiting to establish the minimum set of conditions for private enterprise to flourish. For these kinds of economies, he argues that FDI will unlikely become part of the development story in the foreseeable future, except through forced locational advantages foisted by a successful regional integration scheme.

As a way forward for Africa, Soludo identifies three areas for action: (i) the need for capable states and effective institutions to articulate a long-term industrialisation vision, (ii) a competitive macroeconomic environment that supports the boosting of savings and investment, and (iii) a number of microlevel interventions to develop local competitiveness through an appropriate industrial policy. Such interventions would include the use of subsidies to boost R&D and the development of the infrastructural base. Also considered important for African industrialisation is an appropriate external environment that provides for the right level of regional dynamics in the development of markets, as well as calls for the levelling of the global trading field. He also suggests that an appropriate aid for the donor community is regional project aid, not the current haphazard and largely ineffective national aid.

Management of Financial Flows in Southeast Asia

Chapter 10, by Pakorn Vichyanond, analyses the policy and institutional context of the evolution of the Asian financial crisis. Vichyanond takes the position that the significant growth in capital flows to Asia in the early part of the 1990s led to an overinvestment in the ASEAN countries in the midst of an underlying macroeconomic problem. The untreated macroeconomic problem was reflected by the rapid increase in the current account deficit by the mid-1990s. The fixed exchange rate regime in the midst of a rise in the value of the U.S. dollar affected the competitiveness of exports significantly. In addition, many of the new investments facilitated by the capital inflows suffered from a reduced productivity. After discussing the timeline and causes of the Asian crisis, he argues that formats and end uses of foreign borrowings are very crucial because they have immediate implications upon the vulnerability as well as the debt-servicing capacity of debtor countries.

The institutional issue of interest is the role of governments as rule makers and enforcers and their relations with the private sector. Vichyanond acknowledges the strong interventions of governments in creating the overinvestment. In Indonesia and Korea, the role of the state in facilitating the rise of a number of large corporations that made use of the foreign capital is noted. Particularly in Indonesia, the absence of transparency in the relationship between state and business helped to muddy the waters even further. Governments failed to take corrective action early enough through appropriate macroeconomic policy changes, effective regulation, and sound enforcement of rules and laws. This was because they had become entangled in the web spun by the unusual collaboration between state and business in a number of places. While these failures offer a useful lesson to Africa, they certainly lead to questions about what kind of relationship is most appropriate between the state and the private sector in ensuring both an increased inflow of private capital and a more productive use of such capital in all sectors.

Globalization of African Financial Markets

While the flow of international finance to Africa in the last decade has been negligible, particularly compared to flows to Southeast Asia, the trend in the middle of the 1990s appeared to suggest a possible turnaround. This was indeed widely believed to be the case until the onset of the Asian financial crisis. Lemma Senbet argues in Chapter 11 that the positive developments that Africa experienced for that brief period are the main reason for the optimism he expresses about Africa's future participation in financial globalization, which provides opportunities for risk sharing, liquidity provision, and transformation. He argues that the positive linkage between finance and economic development is of particular interest to African economies, pointing to a possible indirect linkage between capital market development and poverty alleviation, along with employment creation.

After identifying the benefits that Africa stands to gain from a greater integration into the world financial markets, Senbet outlines the challenges Africa faces in accessing the benefits of financial globalization while controlling globalization risks and the attendant financial crises. The challenges facing Africa in its financial globalization include the characteristics of the malfunctioning domestic markets, such as their thinness, illiquidity, and the weak disclosure and enforceability of rules; and the absence of risk-sharing mechanisms to cover macroeconomic and political risks, as well as foreign exchange risks, the risk of growing Afro-pessimism, and the attendant risks of financial crisis. Senbet attributes the Asian financial crisis to the institutional problems that have led to the dysfunctionality of the financial systems. The inappropriate relationships among governments, business, and financial institutions are blamed for the problems of moral hazard that characterised a number of significant financial transactions, wherein debtors had an incentive to undertake excessive risks and channel capital to inefficient, yet high-risk, investments.

Senbet presents several suggestions on how to meet the challenges with respect to Africa. He focuses on capacity building in the development of local capital markets, including the design of efficient systems for capital market regulation that ensures fairness, full disclosure, and transparency. He emphasises further the need for building human resources and training programmes, as well as fostering an environment for good corporate governance. He also discusses how to promote capital markets development through privatisation and the design of efficient banking regulation. In his view, regional cooperation and the development of regional markets are particularly important in Africa as an effective means for addressing the thinness of individual national markets.

Considering the virtual absence of Africa's global participation as a manifestation of extreme risk and the resulting "marginalisation" of the region, Senbet warns against the wrong lesson to be drawn for Africa from the Asian financial crisis: advocating to avoid globalization in the pursuit of avoiding globalization risks. In his view, that is tantamount to continued "marginalisation," with no opportunity for Africa to access the potential benefits of globalization. Building a capacity for the efficient management of risk and the efficient resolution of crisis is suggested as the more appropriate alternative.

Aid and Development in Southeast Asia

Khan develops in Chapter 12 an asymmetric loss function model to investigate the macroeconomic effects of foreign assistance, focusing on the effect of aid on public-sector variables as opposed to the usual studies of effects on growth. He argues that, for foreign aid to be effective, certain complementary domestic conditions should prevail, which include complementary private investment, human capital, and appropriate governance structures in administrative, political, and civil-society aspects.

Because of increased aid flows to Malaysia, Thailand, and Indonesia in the late 1970s and into the 1980s, Khan argues strongly about the gap-filling role that aid played. Indeed, aid to Indonesia was significant and ensured macroeconomic stability since it helped to close the financial gap throughout the 1980s, particularly when oil prices suffered a decline. The use of aid to finance shortfalls in development budgets was also significant in Malaysia and Thailand in the 1970s and 1980s. In particular, bilateral aid turned out to be more effective in these economies. For example, in Indonesia, aid has been effective in infrastructure projects funded by Japanese bilateral aid. Khan, however, notes that aid has been least effective in social-sector development or human-resource development where the performance of the studied nations was less than predicted on account of their income growth.

In concluding that aid to the three countries has been generally effective, Khan attributes this effectiveness not only to a developmental approach to economic management in these countries but partially to the institutional structures, capacities, and practices at the political-administrative, economic, and civil-society levels. He also suggests that policies of export-led development have been significant, if not instrumental, in mobilising foreign aid for investment purposes. He sees the state as being relatively autonomous in the countries, much more so than in other developing nations, since it permits the adoption of broader-based development agendas. The effects of existing corrupt interest groups are therefore more easily contained, even if not as well as they are in Northeast Asia.

Foreign Aid, Debt, and Development in Africa

For Sub-Saharan Africa, foreign aid has become the strongest link with the rest of the world. Hence, the effects of aid on economic development are one of the most studied and debated topics in recent years. Chapter 13, by Sam Wangwe, examines the trends of foreign aid, the experiences of aid effectiveness and aid management, the debt problem in SSA, and he draws some lessons from these experiences.

Noting the uncertainty associated with future flows as a result of budgetary pressures competing with claims on donor resources, Wangwe discusses the effectiveness of aid and its management in Africa. He claims aid has been effective as a project-funding gap filler. Aid has also helped to bridge the savings-investment gap and the foreign-exchange gap. However, he notes, when a yardstick of graduation is applied, unlike in Southern Asia, no country in SSA, except Botswana, has been weaned from aid. He further suggests that, with the onset of the adjustment regime in the 1980s, the goals of aid became a lot more blurred and the effectiveness of aid much more complicated to evaluate.

Wangwe notes, however, that alongside many disappointments, aid has financed numerous development projects and programmes which have achieved reasonably high internal rates of return, including schools, clinics, health posts, bridges, roads, and manpower training programmes. Emergency aid has been also decisive in helping many SSA countries. However, Wangwe notes the controversy surrounding the macroeconomic growth effects of foreign aid. While arguing for an accommodating macroeconomic environment, he criticises the well-known Burnside-Dollar arguments for greater selectivity in aid allocation, with a focus on the relevance of the policy indices applied and the implications for poor-policy countries. Other issues discussed are the management capacity and the entire absorptive capacity problems of recipients, aid coordination, and the major questions of ownership and conditionality. Wangwe calls for improved aid relationships between donors and recipients in all these areas.

Further, Wangwe evaluates the recent rapid growth of debt as a result of reform processes and the new financing requirements. The chapter makes a strong case for debt relief, including relief under HIPCs on the basis of the nonsustainability of existing debt levels and debt service programmes. While supportive of HIPCs, Wangwe notes some reservations with respect to the criteria for selection, the depth of the measures, and the sequencing of eligible countries. In particular, he argues that a conditionality attached continues to have made it difficult to effectively have access to the facilities. He suggests that conditionality needs to be redefined to link more appropriately with agreed-upon criteria of performance by all partners.

Key Challenges of African Development

Chapter 14, by Delphin Rwegasira, identifies key challenges facing Africa in the twenty-first century. Rwegasira notes that, for long-term growth, Africa will have to find ways and means of gainfully opening up and competing in the global economy. For this to be achieved, he suggests several key issues to be addressed. First, Africa will have to create a proinvestment climate, which will involve progress on several fronts: political, administrative, and narrowly economic. Progress on these fronts would importantly depend on the actual availability of resources and on incentives for private investment and a sustained proinvestment climate. Second, creating such a proinvestment climate would in turn require progressive establishment of what has been called ''developmental states,'' that is, creating a competent and independent state bureaucracy and building closer ties between such a bureaucracy and the emerging private sector. In addition, a ''developmental state'' would need to address the broader imperative for capacity building, especially in respect to policy analysis and management.

Third, Rwegasira envisages an enhanced role for regional markets, arguing that regional cooperation and integration would help SSA in a sustained way if the cooperation framework would be conceived within the context of what has come to be called ''open regionalism.'' An ''open-regionalism'' approach would caution against overreliance on the regional market in order to avoid the well-known limitations of import substitution strategies. At the same time it would facilitate greater macroeconomic and institutional coordination, coordination of investment in infrastructure and natural resources, private-sector promotion, and, finally, alignment on bilateral and multilateral external assistance.

The last issue Rwegasira raises concerns diversification and agricultural growth. He notes the problem of the structural vulnerability of African countries, which originated from the very limited diversification. He argues that this is particularly relevant in the agricultural sector, which in a typical country in the region accounts for 70% of total employment, 40% of merchandise exports, and one third of GDP. Better policies to promote stronger agricultural growth would thus not only lead to general economic improvements arising from trade but would also create possibilities of diversification within agriculture. These policies would need to address the major weaknesses that have been identified with African agriculture: seriously inadequate public and private investment in the sector; a very weak physical and research structure; inadequate marketing and support systems; the basic issue of prices and other incentives. Apart from the domestic and external trade benefits that would result, a more diversified agriculture sector would make it easier to advance on the strategic objective of reducing poverty in a more conducive context of agricultural and rural development.

Notes

1. Lemma W. Senbet, "Global Financial Crisis: Implications for Africa," *Journal of African Economies*, AERC Supplement 10 (2001): 104–40.
2. Ibid.
3. For a literature review of risk and cost associated with financial globalisation and a discussion of how to link global finance to economic development by building an institutional foundation, see Machiko Nissanke and Howard Stein, "Financial Globalisation and Economic Development: Toward an Institutional Foundation," *Eastern Economic Journal* (2003, forthcoming).
4. World Bank, *The East Asian Miracle: Economic Growth and Public Policy*, A World Bank Policy Research Report (Washington, D.C.: The World Bank, 1993).
5. David L. Lindauer and Michael Roemer, eds., *Development in Asia and Africa: Legacies and Opportunities* (Cambridge, Massachusetts: Harvard Institute for International Development, 1993).
6. For a critical literature review of the debate sparked by the World Bank Study, see Machiko Nissanke and Ernest Aryeetey, "Comparative Institutional Analysis: Sub-Saharan Africa and East Asia" (framework paper presented at the AERC-UNU Conference on Comparative Development Experiences in Africa and Asia, Johannesburg, November 1997), in *Comparative Development Experiences in Africa and Asia*, eds. Ernest Aryeetey and Machiko Nissanke (Aldershot: Ashgate, 2003).
7. The first workshop on the thematic topic of Comparative Institutional Analysis in Asia and Africa was held in Johannesburg, November 1997, and a collection of the selected papers of the first workshop can be found in Aryeetey and Nissanke, *Comparative Development Experiences in Africa and Asia*.

8. Robert Bates, *Essays on the Political Economy of Rural Africa* (Cambridge: Cambridge University Press; Berkeley, Los Angeles, and London: University of California Press, 1983).
9. Stephen Knack and Philip Keefer, ‘‘Institutions and Economic Performance: Cross-Country Tests Using Alternative Institutional Measures, *Economics and Politics* 7 (1995): 207–27.
10. Hernando de Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (New York: Random House, 2002).

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This book brings a crucial issue to the fore: how to manage the process of *strategic integration* into the global economy. The performance of Asian and African economies over recent decades clearly shows that engagement with the global economy can play a key role in advancing development.

Researchers and policymakers have paid particular attention to the marked divergence in growth in Southeast Asia and sub-Saharan Africa. One of the most obvious differences in their performance and economic structure has been the extent of their participation in the global economy. While many East Asian economies have accelerated their integration into the world economy and upgraded their mode of linkages, the majority of sub-Saharan African countries have been increasingly marginalized. What is less clear, however, is the significance of different policy, institutional, and structural issues – and the manner in which they have interacted – in explaining the divergent performances of Southeast Asia and sub-Saharan Africa.

A strategic approach is important because the benefits and costs of globalisation are unevenly distributed, and because the optimal level of openness may differ for each aspect of trade, investment, capital flows, technology, and stage of development. These considerations have implications for the policy mix needed to achieve integration and determine the pace, sequencing and time-frame for reforms.

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