CHAPTER 1. NATIONAL ECONOMIES: SUSTAINING GROWTH

INTRODUCTION

In the first decade of the twenty-first century many African countries have achieved relatively rapid growth. This has raised hopes that Africa is finally on a path to convergence with Asia and Latin America. The patterns that we see in African economic development are not new; we will see that they replicate several centuries of European history. Europe's history suggests that optimism for Africa will be misplaced unless economic growth is accompanied by serious institutional change. What changes are required? This is not an easy question because we will identify a vicious circle that links poverty, dependence on a few export commodities, and lack of diversification with weak rule of law, corruption, and periodic outbreaks of violence. Vicious circles are difficult to break. How can we break this one?

Box 1.1. Setting the scene

Africa rising? 'The shops are stacked six feet high with goods, the streets outside are jammed with customers and salespeople are sweating profusely under the onslaught. But this is not a high street during the Christmas-shopping season in the rich world. It is the Onitsha market in southern Nigeria, every day of the year. Many call it the world's biggest. Up to 3m people go there daily to buy rice and soap, computers and construction equipment. It is a hub for traders from the Gulf of Guinea, a region blighted by corruption, piracy, poverty and disease but also home to millions of highly motivated entrepreneurs and increasingly prosperous consumers. Over the past decade six of the world's ten fastest-growing countries were African. In eight of the past ten years, Africa has grown faster than East Asia, including Japan' (Source: 'The hopeful continent: Africa rising', The Economist, 3 December 2011).

Using annual data from many countries since 1950, and defining a growth acceleration as a period over at least eight years in which the national growth of GDP per head is at least 3.5 per cent, exceeds the previous growth rate by at least 2 per cent, and leaves the level higher than at any time in the past, 'the largest number of growth accelerations is actually in Africa ... a continent that one hardly associates with economic growth. However, this region still has the lowest probability of a growth transition among all the regions: only 1.9 per cent. ... Financial liberalisation and positive external shocks are associated with growth accelerations that eventually fizzle out. Fundamental economic reform and positive political regime change increase the likelihood of sustained accelerations ... [but] the predictability of these different kinds of growth episodes still remains extremely low.' (Source: Hausman, Pritchett, and Rodrik 2005).

Africa's recent growth 'has largely followed rising commodity prices, and commodities make up the overwhelming share of its exports - never a stable prospect. Indeed, the pessimists argue that Africa is simply riding a commodities wave that is bound to crest and fall and that the region has not yet made the kind of fundamental economic changes that would protect it when the downturn arrives. The manufacturing sector in sub-Saharan Africa, for example, currently accounts for the same small share of overall GDP that it did in the 1970s. What's more, despite the overall decline in poverty, some rapidly growing countries, such as Burkina Faso, Mozambique, and Tanzania, have barely managed to reduce their poverty rates. And although most of Africa's civil wars have ended, political instability remains widespread: in the past year alone, Guinea-Bissau and Mali suffered coups d'état, renewed violence rocked the eastern Democratic Republic of the Congo, and fighting flared on the border between South Sudan and Sudan. At present, about a third of sub-Saharan African countries are in the throes of violent conflict' (Source: Devarajan and Fengler 2013).

AFRICA'S FUTURE: SUSTAINABLE GROWTH?

African countries have achieved impressive rates of economic growth since the mid-1990s, second only to those of East Asia. Can Africa's improved economic performance be sustained? Optimists point not only to a boom caused by high prices for primary commodities, but also to improved macroeconomic policies, democratisation, and the transformation of industrial and service firms by information and communications technologies. However, more pessimistic commentators point to continued political instability, corruption and weaknesses in transport and energy infrastructure.[1]

Both optimists and pessimists have looked back to the period of rapid growth following the end of World War II and its subsequent reversal in the 1970s. Optimists have argued that this reversal reflected the difficult challenges of decolonisation and that Africa has now moved on. Pessimists have suggested that the export led growth of the current boom is similar to that of the 1950s and 1960s. However, a longer view of Africa's economic history suggests that periods of rapid growth followed by reversals have characterised African economic performance for several centuries. These reversals have limited long run improvements in incomes per head. The periods of growth and the reversals alike have been driven by changes in world demand for primary commodities.[2]

Recent research has reconstructed GDP figures for Europe since the thirteenth century. It shows the same pattern for Europe up to the mid-nineteenth century as for Africa recently. There were periods of rapid growth and setbacks. These were based on the success and failure of export commodities, particularly wool.

This research also suggests that average incomes in medieval Europe were substantially higher than previously thought, so that the medieval period should be seen as the starting point of the road to sustained growth, not an embodiment of all things backward. The first transition to modern economic growth occurred in the North Sea area. The North Sea economies were the first to escape the pattern of growth reversals. They were allowed to succeed in this transition by fundamental institutional change.

Box 1.2. GDP as a measure of development

What is GDP? A country's gross domestic product measures everything that is produced within the country. The size of a country's GDP can be taken as a measure of its weight in the world economy. Economic size is important where scale matters: for example for national power, or when the existence of an industry depends on a large market. Thus politicians, diplomats, and defence contractors care most about whether America or China is the world's largest economy. But the size of an economy tells us little about its level of development; both the American and Chinese economies are very large, but China's economy is much less developed than America's.

What is development? A developed economy is rich so that its GDP is large relative to its population. A first approximation to the level of development of an economy is its GDP divided by the population, or GDP per head. This is not an infallible measure, but it is always a good place to start. However, a developed economy is usually also diversified, so that its citizens, most of whom live in cities, do many different things that complement each other, and what they do is intensive in knowledge, skills, and capital. Some economies are rich without being highly developed because they have oil, gas, or other mineral wealth. They are rich only because other economies that are rich and developed have valuable uses for their resources.

Does GDP measure social welfare? Having a high GDP per head of the population does not guarantee social welfare. It has been said that a large GDP relative to the population captures the potential for wellbeing rather than wellbeing itself. Still, there is evidence from around the world that GDP and wellbeing are somewhat connected. On average, each doubling of GDP per head does tend to increase psychological wellbeing by about the same amount.

GDP growth or level? It is important to distinguish the level of an economy's development from its rate of growth. From the point of view of how we live at any moment the level of GDP per person is surely more important than its growth. However, poor countries can achieve high levels in the foreseeable future only by means of rapid growth, so growth matters too.

What is sustainable growth? Not all growth is sustainable. When growth that takes the form of producing more by using ever more resources and effort, the result is sustainable only while there are resources lying around that are unused. The evidence is increasingly compelling that our world's resources are finite, especially its atmosphere. To be fully sustained in the long run, growth must take the form of producing more from less.

We will compare Africa's growth patterns since 1950 with those of Europe since the 13th century.[3] We will find that most African countries have average real incomes at the same level as in medieval Europe. This suggests grounds for both optimism and caution. Optimism comes from the vastly greater technological possibilities open to African countries today, compared with medieval Europe – mobile phones are just one example. Indeed, China and Russia are now middle-income countries, where 'middle-income' is a multiple of the income levels that were found in medieval Europe. In other words, modern technology has created more room for countries to grow even though they still have corrupt, closed political institutions.

But the same history also suggests the need for caution. European experience shows that the pattern of growth acceleration alternating with reversal can persist for centuries. The transition to modern economic growth is not inevitable. Growth is made sustainable by institutional change. African economies today have achieved levels of development comparable with medieval Europe, but they do not yet have the institutions, such as the rule of law, necessary to eliminate growth reversals and make growth sustainable in the long run. There is a ceiling on what can be achieved without these changes. While African economies are likely to be well below the ceiling, and can continue to grow for a while, their growth is fragile and the ceiling is still there.

AFRICA'S PAST: A LONGER VIEW

What is the evidence from Africa's more distant past? The African story has often been presented as a narrative of unrelenting failure. A good example is the literature inspired by the economist Robert Barro, which sought to explain why African countries grew so slowly between 1960 and 1990.[4] It is sometimes called the 'Africa dummy' literature. In this context an Africa dummy was an artificial statistical variable, set to 1 for African countries and zero for all others. The literature started from the observation that, when researchers looked for factors explaining country growth in a global sample, most of the lack of growth of African countries was explained, statistically speaking, by the fact that they were in Africa (represented by the large negative coefficient of an Africa dummy).

Recent research in African economic history has revised this story.[5] Rather than persistent failure, there have been periods of growth, but these were followed by reversals which typically erased the gains made during the previous spurt. Since 1950, in fact, most African countries have followed this pattern of growth and reversal. The two decades after 1950 saw relatively rapid growth, for example, but this ended with the oil crisis of the 1970s. The 1980s and 1990s saw stagnation or even decline. The recent revival of growth dates from the late 1990s, and the first task was to offset the decline of the previous two decades.

International trade is likely to have stimulated African growth far back into the past. The trans-Saharan trade in gold, slaves and ivory from the early medieval period favoured the emergence of large urban centres and elaborate commercial institutions in West Africa and along the edge of the desert. Like Venice and Genoa in Europe, Timbuktu, centre of the once-mighty Kingdom of Mali, prospered by facilitating international trade. Growing trade between Europe and West Africa (including the Atlantic slave trade) also led to increasing commercialisation. But gains at some times were lost in others. None of these developments – and certainly not the slave trade – led to sustainable growth. Again, in the late nineteenth century many African countries benefited from strong growth in the international economy by selling cash crops at favourable international terms of trade. These gains too were lost in the Great Depression of the 1930s.

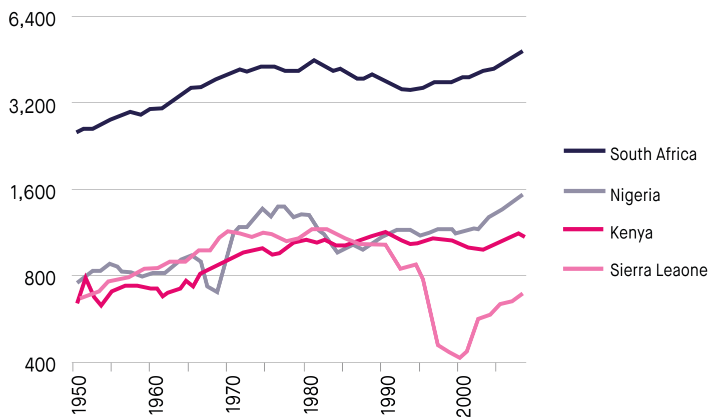
To summarise, the growth that African economies have shown recently has been repeated many times in the past. What are the chances that the outcome anywhere in Africa will be more successful – or more sustainable – than hitherto?

Here it is important to recognise the diversity of Africa's societies. While there are common factors in the growth of African economies, each region has a different physical and cultural endowment, beginning with its own pre-colonial history and culture. Each part of Africa had a different experience of Western colonialism; it is worth noting that Africa's modern borders are largely a legacy of the colonial period. Post-colonial developments also show great variety.

FOUR CASE STUDIES

To simplify, we will focus on four countries: Kenya, Nigeria, Sierra Leone and South Africa.[7] Figure 1.1 shows the real GDP per head of each country from 1950 through 2008.

Figure 1.1. Real GDP per head in international dollars and 1990 prices, 1950 to 2008: South Africa, Nigeria, Kenya and Sierra Leone



Source: Data from Maddison (2010).

The most striking finding is that today, like other sub-Saharan African countries, they have average incomes on a par with medieval European economies. Indeed, only a handful of African countries have higher incomes than Britain enjoyed at the beginning of the 19th century.

There are differences as well as common patterns. Most obviously, they are not equally poor. South Africa is much richer than Kenya and Nigeria. Sierra Leone used to be close to the others but has fallen behind.

Box 1.3. What are "real GDP" and "international dollars and 1990 prices"

What is real GDP? It is sometimes thought that 'real' GDP is an objective measure of the number of things produced. A moment's thought shows this cannot be the case. It makes no sense to say that an economy that produces nine shirts and one car has made ten things. All the things that are produced must be valued before they are added together. When the values change from year to year (or from one country compared to another), we call it GDP at current prices or 'nominal GDP'. Real GDP implies the use of a single set of unchanging or constant prices, so that the GDP of all the years (or all the countries) is measured using a common standard.

Constant prices. Figure 1 reports GDP per head in constant prices. The basis of valuation is '1990 international dollars'; this is a standard for historical comparisons of economic performance across many years and countries (Maddison, 1995; 2010). Dollars are the unit. 'International' dollars mean that the prices used to value output are average international prices rather than U.S. dollar prices. The year these prices are taken from is 1990.

A measure of absolute poverty. This measure gives rise to a useful benchmark. In 1990, the World Bank poverty level for an individual was a dollar per day, or $365 per year. This suggests that no society can survive for long with average incomes much below $400 in international prices of 1990, taking into account that even the poorest economies have elite families with income many times higher than the poorest. Thus $400 in international prices of 1990 is usually taken as the minimum or 'bare bones' level of subsistence of a society.

Sierra Leone

In Sierra Leone average incomes in 2008 were below $750 (in 1990 prices), making it by far the poorest of the four countries. How did Sierra Leone arrive at this position? The country enjoyed favourable prospects in 1950 owing to its mineral wealth. While it kept pace with other countries until the early 1970s, the transition to an increasingly repressive one-party state in 1973 resulted in GDP per head stagnating at around $1,100 a year through the 1980s. The major decline came with the outbreak of one of Africa's deadliest civil wars in 1991. This war lasted ten years, killing more than one per cent of the population and turning nearly half into refugees.[8] After the war the economy recovered, but average incomes in 2008 remained no higher than in 1950.

Sierra Leone shares many of the features prominent in the literature on Africa's failed states, including the extensive use of patronage to maintain an elite coalition in power, limited control over the use of violence, and vulnerability to external shocks. William Reno describes the reliance on patronage systems as a 'shadow state', in which rulers use their ability to intervene in their countries' economies to strengthen their political base.[9]

In Sierra Leone, a poor country with fragile institutions, 'all politics is real politics; people risk death when they make political mistakes'.[10] Sierra Leone's recent civil war is a prime example. With the transition to independence, which gave a greater political voice to groups that were marginalised during the colonial period, the coalition of coastal elites of that earlier era was no longer sufficient to limit violence. The country's descent into civil war resulted from the combination of this unstable coalition and the effects rippling from conflict in neighbouring Liberia. The 'shadow state' or patronage networks played an important role in state policy, as well as in the promotion of violence in Sierra Leone.

Kenya

In 2008 the average Kenyan had an income of around $1,000 (in 1990 prices). Kenya's economic performance since 1950 has been less volatile than the other three countries, but it shares many of their features. Its economic success in the 1950s and 1960s was due largely to agricultural exports, but Kenya also benefited from its dominant position in East Africa. However, mismanagement of revenue earned in the coffee boom of the 1970s along with the increasing use of state funds for political patronage led to a poor economic performance during much of the 1980s. A brief recovery in the late 1980s came to an end with outbreaks of ethnic violence in the aftermath of highly contested national elections in 1992 and 1997. This was compounded by droughts and high oil prices due to the Gulf War.

Kenya is wealthier today than Sierra Leone, but it is not long since these two countries were at the same level. Today, Kenya's state institutions are also fragile. Recurrent ethnic violence illustrates that competition between patron-client groups can still lead to violence. As a result of the interconnection between ethnicity and party allegiance in Kenya, competition between parties at election time is to a large extent competition between ethnic groups. The link in Kenya between ethnic violence and elections highlights the risks of political competition when violence is barely contained in normal times.

In Kenya, privileged access to economic resources is one of the 'carrots' that can be used to ensure the support of ethnic coalitions. This is reminiscent of the European historian of the 'freedoms' which, according to the economic historian Larry Epstein, undermined market integration in Europe because they took the form of privileges granted to elites in order to sustain their political support.[11]

Nigeria

In Nigeria in 2008 average incomes were around $1,500 (at 1990 prices), substantially higher in Kenya and twice the level of Sierra Leone. In 1958 the World Bank claimed that Nigeria's prospects for growth based on its agricultural exports (including palm oil, cocoa, groundnuts, cotton and rubber) were good, but that they depended on 'Nigerians' success in eliminating tribal or regional antagonisms and maintaining reasonably high standards in public administration'. In fact, post-independence political conflict has resulted in several growth reversals. The Biafran War of the late 1960s reversed earlier gains, and GDP per head fell to below its 1950 level. The oil boom of the 1970s led once again to positive growth, but oil revenue had little lasting impact on per capita GDP, which declined in the 1980s and remained stagnant through the 1990s. Since 2000, oil production and expansions in agriculture and services have led to a period of renewed economic growth, but the country remains overwhelmingly dependent on its energy sector.

A hopeful sign for Nigeria is that politics is not everything. Nigeria is home to many of Africa's largest private corporations, and has a vibrant civil society. As of 2012 the private sector employed 80 per cent of Nigeria's workforce and generated most of its exports.[12] In other words, Nigeria's elite does not fear interests that are organised outside the state as potentially damaging competition that must be suppressed. This is not to say that power and wealth are fully separated, as is needed for an open-access society. Moreover, the state remains vulnerable to factional disputes in which violent religious mobilisations are playing an ominously increasing role.

South Africa

In 2008 average incomes in South Africa stood at nearly $5,000 (in 1990 prices), three times the level in Nigeria. South Africa's advantage has a long history. As early as 1950, the average South African was wealthier than Nigeria today. South Africa became the continent's economic leader following the mineral discoveries of the nineteenth century. Foreign investment and public revenue generated by the gold mines allowed the South African government to pursue an aggressive strategy of state-led industrialisation in the 1920s. Since then South Africa has been the most industrialised economy in sub-Saharan Africa. Manufacturing outpaced mining and agriculture as South Africa's leading industry by the 1970s, and later in that decade its GDP per capita peaked just below $4,500, a level only regained in 2006. During the 1980s, however, protests against the repressive apartheid regime caused Africa to become politically unstable. The gold price fell at the same time. The result was a period of economic contraction. Growth was resumed only with the coming of majority rule in 1994.

Even more than Nigeria, South Africa has a strong corporate sector. While economic growth has been steady since the mid-1990s, high rates of inequality and youth unemployment have limited the benefits of growth to a small proportion of the South African population. In fact the very idea of the 'average' South African is problematic (in a similar way you could well question who is the average Nigerian, Kenyan, or Sierra Leonean). Fault lines in the coalition of the ruling African National Congress and the trade unions threaten to undermine the party's base of political support. Unequal distribution ensures that disputes over ownership and rewards quickly become political and threaten violence.

To summarise, these four countries have shared features as well as differences. One is that economic growth has been significant, but has not been sustained. Growth has been followed by reversal. Another common feature is that an important trigger of reversals has been internal conflict. Nigeria suffered a devastating civil war over the Biafra secession in the late 1960s. South Africa experienced prolonged instability as the apartheid regime disintegrated in the late 1980s. One of Africa's deadliest civil wars broke out in Sierra Leone in 1991, ending only in 2002. And Kenya has seen repeated violence associated with contested election outcomes in 1992, 1997, and 2007.

EUROPE'S PAST: PARALLELS WITH AFRICA TODAY

European history from the thirteenth century to the nineteenth also suggests a pattern of periods of economic growth followed by reversals. The European pattern is consistent with the experience of the African continent to the present day. We base this judgement on new estimates of real national income per head in Europe since the thirteenth century by ourselves and other CAGE associates. We focus on four major European countries: England (later Great Britain), Holland (later Netherlands), Italy and Spain.[13]

Box 1.4. The measure of poverty

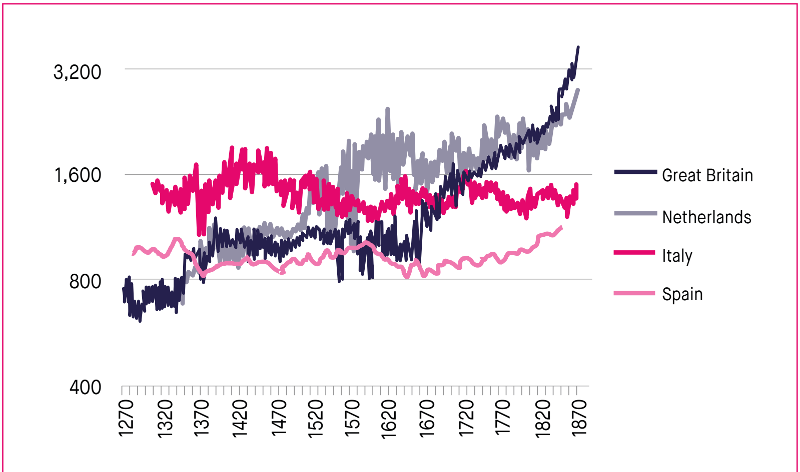
Poverty is not what it used to be. We take $400 in international prices of 1990 as the annual cost of ‘bare bones’ subsistence. Is the purchasing power of $400 dollars the same today as it was in medieval Europe? Not exactly. Today you can buy a smartphone for $400. The price of a smartphone in thirteenth century London was certainly prohibitive and arguably infinite. More generally, the range and variety of goods and services you can buy today with a dollar at 1990 prices is far wider than in any past period. To be poor today is different from being poor in the past because the poor have more choices, even if they are still poor. This illustrates the problem that measuring historical change in living standards cannot be exact. But many dimensions can be estimated with relative precision, for example nutritional quantity and quality, the availability of clothing, shelter, heat, and light, access to the written word, the time taken for news to travel, and so forth. Our estimates of GDP per head reflect what can be measured and this provides the basis of meaningful comparisons over time.

Today’s poor live longer. Because of advances in health care and disease control, poor people have many more years of active life and health than in the past. In Sierra Leone in 1960, for example, average life expectancy was 30 years, and this was comparable to life expectancy in medieval Europe. Today average incomes in Sierra Leone are no higher than in 1960, but life expectancy has risen from 30 years to 45 years. Poverty means that disease control remains fragile, as the recent Ebola outbreak reminds us. (Source: World Bank, World Development Indicators 2014). Whether it is better to live longer in acute poverty is a matter for debate.

Figure 1.2 shows six centuries of economic growth in Western Europe. By the late Middle Ages Western Europe was already well above bare-bones subsistence, which we take to be $400 (see Box 1.4). On the eve of the Black Death in 1348, average incomes were around $750 in England and Holland and substantially more than this in Italy and Spain. At this point economic growth had already taken place, bringing Western Europe to a level of development similar to that found today in much of sub-Saharan Africa. Despite this, several more centuries would go by before the first of these countries made its breakout to modernity.

The figure underscores the fact that low standards of living in pre-industrial economies are not due to persistent failure. Rather, they are due to inconsistency; the economy succeeds from time to time, but then the gains are lost. Long-term stagnation results from alternating periods of growth and decline. This is illustrated in Figure 1.2 by Italy and Spain.

Figure 1.2. Real GDP per head in international dollars and 1990 prices, 1270 to 1870 Britain, Netherlands, Italy, and Spain



Source: Data from Malanima (2011); Álvarez-Nogal and Prados de la Escosura (2012); Broadberry et al. (2012). Note that the apparent drop of incomes in Holland in the early 19th century is the result of a break in the territorial basis of the estimates, with the pre-1807 data referring to Holland, the richest part of the Netherlands, and the post-1807 data covering the whole of the Netherlands.

Violence contributed to growth reversals. There was hardly any time during this period when two or more of the European powers were not engaged in conflict somewhere.[14] Borders changed frequently, and this also brought discontinuity of the political and legal framework of the disputed territories. Most wars were small and short, but a clear exception was the Thirty Years' War, fought bloodily on the continent of Europe from 1618 to 1648. Although the sea offered protection from external attack, England experienced bouts of internal violence; power struggles within the dominant coalition led to the Wars of the Roses in the fifteenth century and the Civil War of the seventeenth century. The revolt of the Dutch against the Habsburg rule of the Low Countries, which led to the foundation of the Dutch Republic in the late sixteenth century, also illustrates the instability of the Spanish state.

In the eighteenth century, as Figure 1.2 shows, a small part of Europe in the North Sea region broke the mould and made the transition to modern economic growth. The result was a long-term reversal of fortunes. In the early fourteenth century Italy and Spain were richer in average incomes than Britain and Holland. The second half of the fourteenth century was marked by the Black Death and further outbreaks of plague. The first growth spurt in the North Sea region followed the Black Death, after which average incomes remained on a relatively high plateau rather than falling back to their pre-1348 level. This was followed by further waves of growth: first in Holland, during its Golden Age (1500-1650), and then in Britain from the mid-seventeenth century. By the nineteenth century, Britain and Holland had clearly outpaced Italy and Spain. This is sometimes called the Little Divergence.

To what extent are the growth booms and reversals experienced by African countries since 1950 comparable to those that occurred in medieval Europe? Because the European data in Figure 1 cover a much longer period than the African data in Figure 2, European growth may at first sight look smoother than African growth. In fact, however, the scale of reversals is actually quite comparable.

Box 1.5. The Great and Little Divergences

The Great and Little Divergences took place between 1300 and 1800.

In the Great Divergence, Europe became much wealthier than China. The Great Divergence is often also associated with eighteenth-century developments such as the European Enlightenment and the Industrial Revolution, and the first era of globalisation in the nineteenth century. In fact, these came very late in the Great Divergence. The roots of the Great Divergence lie far back in the Middle Ages and so well before these events.

The Little Divergence took place within Europe, and was reflected in the emergence of the North Sea region, England and Holland, as the most prosperous part of the continent. Again, the Little Divergence became obvious in the eighteenth century but its roots can be traced much earlier.

Table 1.1. Real GDP per head: the variability of annual growth in Africa and Europe compared, standard deviations in percentage points

	1270 to 1870	1950 to 2008
Europe:		
UK	6.4	1.8
Netherlands	8.2	2.1
Italy	5.2	2.5
Africa:		
South Africa	...	2.3
Nigeria	...	6.7
Kenya	...	4.2
Sierra Leone	...	6.6

Sources: Africa, as Figure 1.1. Europe, 1270-1879, as Figure 1.2; 1950 to 2008, from Maddison (2010).

Notes: UK is England until 1700 and Great Britain thereafter; Netherlands is Holland until 1807. Spain is excluded, although the same calculations could be done for Spain using the sources cited above. These would suggest an opposite pattern: higher variability since 1950 than before 1870. The reason for this is technical: Spanish GDP in the medieval period is estimated by a methodology that smoothes year-on-year variation, artificially reducing the standard deviation of the annual growth rate.

The variability of economic growth can be measured by the standard deviation of a country's annual growth rate. This reflects the average distance of the growth rate in each year above or below the average over a longer period. Table 1.1 shows that, as European societies have become more developed, the variability of annual growth of their economies has declined. Before 1870 the standard deviation of annual growth was 6 to 8 percentage points for Britain and Holland, and more than 5 percentage points for Italy. Since 1950, in contrast, European economies have grown relatively smoothly, with variation in annual growth rates of less than 3 percentage points.

When we compare our four African economies, we see that economic growth in Nigeria, Kenya, and Sierra Leone has been as variable as economic growth in medieval Europe. Only South Africa has achieved a growth pattern as smooth as that of Western European economies.

HOW DID EUROPE ACHIEVE THE TRANSITION TO MODERN ECONOMIC GROWTH?

From 'limited access' to 'open access'

The Little Divergence culminated in a transition to sustained long-run growth first in Great Britain during the Industrial Revolution, then in other countries of northern Europe with similar institutional frameworks.

The sources of this divergence have been much debated. There are convincing reasons to think that this transition depended on a balancing act: the emergence of a new kind of government that balanced the building of state capacity with constraints on the executive.

England's Glorious Revolution of 1688 illustrates this balancing act.[15] By confirming the supremacy of Parliament, the Glorious Revolution placed effective constraints on the executive powers of the Crown. At the same time, it unified the domestic market by ending local monopolies, and made the tax raising powers of Parliament legitimate; this led the British state to become better funded and more centralised than ever before, giving the government much greater capacity to intervene, particularly in foreign affairs.

It is important to realise, however, that the emergence of a powerful state subject to the rule of law was a lengthy process, not a single event. It is wrong to place all the emphasis on 1688. The Glorious Revolution was just one moment in a lengthy series of institutional developments, the origins of which can be traced as far back as the Magna Carta of 1215 which first limited the rights of the Crown. In between there were movements backward as well as forward. The economic effects of these movements were not felt overnight. A moment's reflection suggests that it takes a long time for people to gain confidence in the law and secure property rights.

Economists Douglas North, John Wallis, and Barry Weingast have written about the balancing act involved in a state that is both powerful enough to be effective, yet also restrained by the rule of law. In their framework the state is not a single actor to be controlled or enabled; rather, how the state works depends on how a society organises itself to limit violence. They classify all societies in two major types of organisation. Access to power is either 'open' or 'limited'. In this view the wealthy democracies are based on open access. With open access, rights are impersonal and belong to everyone equally. The state has a monopoly on violence. States in open access orders are constrained by highly developed civil societies. Civil society is made up of networks and organisations that have legal existence independent of the life of any private person and do not depend on the ruler's political favour. There can be many examples but in economic life the incorporated private enterprise is one of the most important.[16]

Limited-access societies come in many varieties. This is not surprising, since they have dominated through most of human history. But all limited-access societies have common features. One feature of limited-access societies is the everyday experience of violence and threats of violence. Another feature is that under limited access it is men's access to power that is limited; with rare exceptions, women have been excluded altogether (we return to this in Chapter 3). These two features can be linked by the historical fact that men have shown a greater capacity for violence than women.

Limited-access societies, it is argued, evolved to suppress the universal violence of continual banditry and clan warfare. The historian Christopher

Wickham, for example, emphasises the importance of patronage networks in maintaining the small, fragmented states that emerged following the collapse of the Roman Empire.[17] Elite coalitions emerged that had the capacity to monopolise land and resources, subjugate the workers, capture the rents that they created, and agree to share them. Business was politics, and politics was also business. To preserve their wealth, they kept out competitors from outside their ranks, defined by kin, clan, or ethnic group. Thus access was limited. Men like Thomas Cromwell or Dick Whittington could rise to wealth and power from outside only through special personal favour.

A limited-access order could thus suppress conflict, and under peaceful rule the result would be a degree of prosperity. In the right conditions the degree of prosperity might be considerable. Russia and China today provide examples of countries where GDP per head stands at around $10,000 (in international prices of 1990) although they retain limited-access orders. Arguably, this might suggest that all African countries can double or triple their average incomes without much further institutional development. Today, however, both Russia and China face the existential problem of maintaining internal and external stability. Their problems are growing: both countries are increasingly troubled by confrontational ethnic politics and disputed borders. Under these circumstances continued peaceful development is just a hypothesis.

In Europe's limited-access societies, peace was maintained only as long as those making up the elite could deter each other from grabbing bigger shares. These coalitions were vulnerable to disruption by economic and political shocks, ranging from famine, plague, and external attack to changes in the relative value of resources. If the shock was large enough, the result would be foreign war or a collapse into civil conflict.

The 'doorstep conditions' for change

Today's societies based on open access have evolved from limited-access orders. How has this come about? Slowly, in the North-Wallis-Weingast view, European societies began to move across a doorstep from limited access into open access.

This movement was permitted, but not guaranteed, by meeting three 'doorstep conditions'. First, the elite allowed the rule of law to govern the behaviour of its own members, so that no one person was above the law, however wealthy or powerful. Second, civil society grew stronger and both civil society and the state evolved forms of organisation that were impersonal and perpetually-lived, such as bureaucracies and corporations, so that they did not depend on the physical existence of powerful sponsors such as aristocrats or oligarchs. Third, the government consolidated its control of the military, so that armed force did not belong to factions or warlords. Meeting these conditions would eventually support open access to power and resources: everyone could have property rights and everyone had the same political rights. Business and politics could be separate. You could still mix business and politics by choice, but the links would be relatively transparent and open to scrutiny. The links would also be voluntary: you could lose wealth and retain political rights, and you could lose office and keep your wealth.

Many other things happened at the same time, contributing to the virtuous circle of economic growth. Violence diminished in society. To lose one's place in the elite ceased to be a death sentence. Under the rule of law it became advantageous to invest and work with others, which meant waiting to earn a productive return on investment, rather than to seize the moment to rob or cheat. As the returns to enterprise and learning increased, the economy diversified and ceased to rely on single-commodity exports. Growth became more resilient.

The open-access society did not lie at the end of a one-way street, however. To meet the doorstep conditions for movement to open access did not guarantee that the move would actually be made. Movement could also go backwards. By 1913 Russia had taken some first steps along this path but the First World War pushed it sideways into communism. In the 1920s Germany was well on the way to a liberal democracy but the Great Depression caused it to relapse into fascism. At best, meeting the doorstep conditions improved the chances of a successful transition in the long run.

These ideas have deep implications for the sources of economic growth. It seems that European countries made their transition to modern economic growth by building up the conditions for open access; it seems likely that open-access social orders are less vulnerable to breaks in progress that throw the economy back. Recent research has confirmed this idea empirically by demonstrating that open access societies show fewer growth reversals.[18] In other words, institutional changes allowed European economies to invest, grow, and diversify. Growth was spread across a widening range of activities, resulting in less dependence on staple commodities that were vulnerable to periodic market setbacks.

WHAT ARE AFRICA'S OBSTACLES TO SUSTAINED GROWTH?

In similar fashion to the literature on Europe, studies of obstacles to growth in Africa have explored the tension between the need to increase the capacity of the state and the importance of constraining its ability to violate property rights.[19] As two Africa specialists have written, the challenge

> ...that every society faces is to provide the state with the means to fulfil its legitimate duties, while at the same time preventing it from misusing these means to suppress dissent and expropriate private wealth.[20]

In a recent survey, Daron Acemoglu and James Robinson bring these strands of thinking together, arguing that:

> To generate sustained economic development requires not just the formation of centralised polities, but also the removal of [their] absolutist and patrimonial tendencies.[21]

They argue that it was the late formation of centralised states, together with their absolutist nature, that provided the foundation for Africa's relative poverty today. African states are too often endowed with too little power to collect taxes, enforce property rights, and regulate violence, combined with too much power to extract bribes and confiscate the fruits of enterprise.

The idea of a 'gatekeeper state' links limited capacity to govern with predatory tendencies. A gatekeeper state maintains its authority by controlling access to external markets. The result is that those who need access to external markets in order to import goods and make trading profits have no choice but to cooperate with government officials and recognise official authority.

While Sierra Leone provides one illustration, the idea of a gatekeeper state can be applied more widely to pre-colonial, colonial and post-independence states in Africa.[22] Colonial institutions had many deficiencies, and this is one reason why the expansion of the franchise and political competition that came with independence gave rise to optimism about Africa's future in the 1950s and 1960s. Unfortunately, the democratic institutions introduced at independence came under almost immediate threat in many of these countries, as public funds were used for patronage projects and democratic governments were replaced by military dictatorships and one-party states. The return of many African countries to democracy since the 1990s, like the Arab Spring of more recent years, has again revived optimism, but the underlying fault lines that make democracy unstable are still visible.

To summarise, African economies face shared obstacles to economic growth. Table 1.2 offers some simple measures of these obstacles.

First, as already shown in Table 1.2, in most African countries economic growth is not sustained; growth is followed after a time by reversal. When future prosperity is unreliable, the incentive to invest in the future and work together for the future is weakened by comparison with incentives to grab something now at others' expense.

Second, growth is unstable in part because African economies tend to show reliance on a narrow range of activities, usually based in agriculture and resource extraction. Farmers produce a few crops and export commodities. Table 1.2 shows that in recent years Nigeria still retained two out of every five workers in agriculture, and Kenya three out of five. This level of dependence on agriculture was last seen in England in the eighteenth century and elsewhere in Western Europe in the nineteenth century. Only South Africa is significantly more industrialised.

Table 1.2. Development indicators: South Africa, Nigeria, Kenya and Sierra Leone

	South Africa	Nigeria	Kenya	Sierra Leone
GDP/head in 2008[a]	4,793	1,524	1,098	686
Standard deviation of annual GDP/head growth rate, 1950 to 2008, in percentage points[b]	2.3	6.7	4.2	6.6
Agriculture, per cent of labour force[c]	15.0	58.9	48.3	...
Tax revenues, per cent of GDP[d]	27.8	14.8	25.7	13.8
Firms expecting to give gifts when meeting tax officials, per cent[c]	3.1	22.9	32.3	8.6
Intentional homicides per 100,000 people in 2012[e]	31.0	20.0	6.4	1.9

Sources:

a As Figure 1.1.

b As Table 1.1.

c World Bank, World Development Indicators 2014, available at http://data.worldbank.org/data-catalog/world-development-indicators/ (accessed 15 September 2014). Figures are for 2012 or the nearest available year.

d African Economic Outlook, available at http://www.africaneconomicoutlook.org/en/statistics/ (accessed 15 September 2014).

e United Nations Office on Drugs and Crime, 'Homicide Counts and Rates 2000-2012', available at https://www.unodc.org/gsh/en/data.html (accessed 15 September 2014). Figures are for 2012.

Third, African growth is unstable because violence is poorly suppressed. In 2012, as Table 1.2 reports, Kenya reported 6.4 intentional homicides per 100,000, Nigeria 20, and South Africa 31 (Sierra Leone reported only 1.9;

it is unclear whether the latter figure reflects genuine war weariness or just deficient reporting). In Northwestern Europe, by comparison, homicide rates have been below 3 per 100,000 for more than 300 years (Eisner 2003).[23] Of course there are many kinds of violence and Europe has also experienced violent wars and imposed warfare on others. On one estimate, from 1960 to 2002 more than one and a half million people were killed in battles in Africa, about 40 per cent of the global total. This made Africa the deadliest of the world's regions over that period. More than that, because Africa contains around only around 13 per cent of the world's population, the probability of death in armed conflict in that region was more than four times that in the rest of the world.[24]

Finally, just as they lack capacity to control violence in a lawful way, many African states show limited capacity to tax, spend, and regulate within the law. A state that cannot raise taxes cannot supply public goods, including protection against violence and clean law enforcement. When protection is granted only in return for gifts and bribes, there is a vicious circle: security is privatised, justice is replaced by privilege (literally, 'private law'), and no one wants to pay the tax on top of a bribe. In the seventeenth century growing fiscal capacity was an important signal of the superior quality of the institutions of governance emerging in the North Sea region.

As economists we are particularly interested in learning about a state's fiscal capacity. Where revenues are raised in Africa, they tend to come either from resource rents such as Nigeria's oil revenues, or from taxes on agriculture and trade that significantly worsen the efficiency with which resources are allocated across the economy. Naturally, scholars have debated whether such deficiencies have their roots in the colonial and even pre-colonial past.

Some recent research has stressed that colonial rule shaped the modern tax capacity of African states. But other research has stressed the greater influence of post-independence political imperatives.[25] In practice, neither distant history nor the recent past can be ignored. The importance of history is shown by the relative positions of our four case studies, shown in Table 1.2, which are of long standing. While benefiting from tax reforms since

1995, South Africa already raised considerably more revenue per capita in the first half of the twentieth century. Nigeria, on the other hand, has underperformed relative to expectations both during the colonial period and since 1960, while Kenya has done substantially better, even during the colonial period. One possible explanation is that settler regimes such as those in South Africa and Kenya developed more effective tax systems that were less dependent on trade taxes, because they needed coercive strength.[26]

But history cannot explain everything. Sierra Leone's revenue collections dipped very low during the civil war. Until this time, however, Sierra Leone raised considerably more revenue per capita than Nigeria, illustrating how violence can undermine fiscal capacity.

The direct link from violence to poor fiscal capacity is not the only one that is possible. Deficient fiscal capacity causes the government to lose tax revenues partly because its agents want more income than their salaries provide. Underpaid officials become corrupt and steal revenues before they reach the exchequer. Deprived of revenues, the government cannot redistribute resources legitimately to its political base, so politicians instead resort to secret patronage, which hollows out the state's legitimate functions.[27] In that setting efforts to clean things up disrupt established interests and expectations, and provoke resistance, which can turn violent. The result is to make corruption and violence alternatives: if you try to have less corruption, you may get more violence. And the converse may be true as well.

MOVING TOWARDS THE RULE OF LAW

The rule of law as infrastructure

This chapter implies that one of the most important projects that any society can embark on is to build the rule of law. The rule of law is part of a society's infrastructure. What is infrastructure? Usually we think of infrastructure as physical systems. Infrastructure is the systems that deliver goods, electric power, clean water, and other essential services. When the infrastructure works well we rely on it and we expect it to be there. We press the switch and a light comes on. We flush the toilet and the sewage flows away, out of sight. We don't even think about it.

The rule of law is also infrastructure. Arguably it is more important than any power cable or drainage system. This is because the ability of any society to lay cables and sewers rests in part on the expectation of officials that the primary purpose of the contract is to build the network, not to pay off supporters. It also relies on the expectation of the contractor that the equipment will not be stolen, the manager will not be abducted and held to ransom, and the contract will be paid on completion. When the rule of law is in place, the contract is turned into a switch you press so that capital is created.[28]

Good policy will invest, first and foremost, in the rule of law. This means establishing simple laws that favour fair dealing, a police force that is professionally trained and equipped, courts that deliver justice openly and without favour, salaries that enable officials to live without bribes, and a culture that stigmatises backhanders and malfeasance.

On one interpretation, the implied policy advice to government would be: Enforce the law. But enforcing the law is not the same as accepting the rule of law. We reject the view that any government can simply coerce society into accepting the rule of law. That is not where the rule of law comes from. Rather, the first step is for the elite members of a society to organise themselves in such a way that they can give up private violence and allow the state to monopolise violence. The rule of law comes first from its social acceptance, and only then from its imposition.

Policy matters

The question then becomes: What can policy do to promote acceptance of the rule of law? A key to this is 'organisation': the elite members of a society must organise themselves in such a way as to reduce the resort to violence and agree to subject themselves to the rule of law. Here better organisation is organisation that is more coherent and capable, above all more durable. The more durable are the state and private organisations such as incorporated enterprises, the easier it will be for all society's members to cooperate for the sake of future gains from investment and education, rather than fight each other for immediate spoils.

An issue for policy makers is that the organisations that need this investment are often under attack in the public arena – sometimes violently. In public life government bureaucracies and private corporations are often seen as the property of the privileged – and indeed they generally are. When children are malnourished and disease stalks the shanty towns, why is it a priority to pay lawyers and law enforcers and so give more to those that already have?

In fact, this issue replicates a more familiar problem on a wider scale. How much should a poor society pay a policeman? Precisely because the police have the power to extort bribes, they must be paid enough that they are not too easily tempted. When everyone else is desperate, it is important that the police are not desperate too, even if the result is unfair.

What difference can good policies make in this direction? Institutions cannot change quickly. A society's institutions are rooted in the daily lives, actions, beliefs, and expectations of all its citizens. Attempts to change them will encounter resistance. There is reason to think that large, abrupt changes in a society's legal regime can promote law-breaking. If gift exchange is customary when meeting government officials, for example, it is probably reflected in lower government salaries. Faced with a refusal to offer gifts, the official might retaliate in some other direction: for example, if law-breaking was previously widespread, by threatening to expose some other illegal behaviour by the reluctant giver.[29] Either the law is ignored or everyone is threatened by exposure. This is the case for gradualism.

A case for gradualism is not a case for doing nothing. Policy matters. While history, geography, and institutions provide a legacy that cannot be changed, good policies can still make a measurable difference.[30] If change is slow and if repeated failure is also possible, all the more reason to start now.

Good political leadership can also load the dice in favour of change. This is because many of the events that disrupt growth are political acts. The decision to rig an election, or contest a fair election result, can trigger violence. Thus, by their behaviour leaders influence the behaviour of others through their expectations and the incentives they perceive. Good leadership enabled a peaceful transition from apartheid in South Africa, just as good leadership gave most European countries a peaceful transition from communism. It was easy to envisage much worse outcomes. Thus, good leaders made a clear difference.

IMPLICATIONS FOR POLICY MAKERS

Africa's growth performance in the first decade of the twenty-first century has led to speculation that the continent is entering a new century of sustained economic growth. Such a view, however, raises a number of question marks when the current boom is put into historical context. As was the case in previous boom periods, high external demand for natural resources — particularly oil, but also land and cash crops — is at the heart of this rapid growth. Without institutional change, therefore, further growth reversals can be expected. Indeed, the multi-party democracies established in the 1990s are already showing considerable strain in several countries across the continent, with military coups and ethnic violence hindering what is already a fragile electoral process.

Our research on European economic history highlights the fact that the pattern of rapid economic growth followed by reversals can be repeated over a very long period of time – in Europe's case, half a millennium. With average incomes in many African countries today comparable to Europe in the Middle Ages, such a comparison suggests that it will be difficult for Africa to break free from this historical pattern without significant institutional change. The main reason is that institutions in many African countries still have many of the features of a 'limited-access' social order. In this context, policy should focus on:

- Good policy will foster a robust civil society that can thrive outside of state control. This must include nongovernment organisations that have permanent legal status and do not depend on strong leaders and patronage, or on informal ties to power.
- While such organisations have many varieties, one is particularly important: the sphere of corporate enterprise. Thus fostering the private sector is part of good policy. We will see in chapter 2 that sustainable

economic development and job creation are inconceivable without larger firms. Incorporated private business is an ultimate expression of a society's willingness to allow its members to invest in the future and wait patiently for productive returns. Fostering the private sector does not mean treating rich people favourably. It begins with making it easy to start and register a business and protecting business property against theft and confiscation.

- Good policy will invest in the legal framework of the economy, and also in the apparatus of the law and impartial law enforcement. This means courts that are open to the press, non-political appointment of court officers, security of tenure for judges, decent salaries for police officers, and a social consensus that it is normal to punish senior political and business leaders if they break the law.
- Finally, good policy will foster the government's fiscal capacity. This means paying tax officers a decent salary, encouraging a diverse tax base, easing the conditions for starting and registering a business, setting taxes that are simple and transparent with few loopholes and concessions, and taxing many activities and many people lightly.

Reading these recommendations, anyone might be forgiven for thinking that here is a recipe for apple pie. But there is more. These items are not randomly chosen from a longer list of desirables: they really deserve priority. Attempting them does not guarantee that apple pie will be the result. Most societies that have succeeded at them have done so only after repeated attempts. There is only a chance of success. But there can never be success if we do not try. Good leadership is also vital. In other words, these are not just lessons for specialists and technocrats. They are lessons for all who hold or aspire to office, including the highest offices of all: presidents, prime ministers, and their political advisers.

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ENDNOTES TO CHAPTER 1

This chapter sums up research listed in the references under Broadberry, and van Leeuwen (2011), Broadberry, Campbell, Klein, Overton, and van Leeuwen (2011), Broadberry, Campbell, van Leeuwen, and van Zanden (2012), and Broadberry and Gardner (2014). Two of the researchers, Stephen Broadberry and Leigh Gardner, are also authors of this policy report. We also draw extensively on the conceptual framework of North, Wallis, and Weingast (2009). The authors thank John Wallis personally for advice.

1. Optimists: Radelet (2010); McMillan and Harttgen (2014). More pessimistic views: Kalema (2011); Arbache and Page (2009). See also Devarajan and Fengler (2013).
2. A longer view of Africa's economic history: Jerven (2010).
3. This is not the first attempt to compare African economic development in the recent past and European development during the medieval and early modern periods. However, previous studies (Bates, 2010; Fenoaltea, 1999) have been limited to a qualitative approach.
4. Inspired by the economist Robert Barro: Barro (1991).
5. See for example Jerven (2010) and Ndulu and O'Connell (2008).
6. Trans-Saharan trade: Lydon (2009). Gains at some times, lost in others: Jerven (2010). The boom of the late nineteenth century: Havinden and Meredith (1996); Hopkins (1973). Prados de la Escosura (2012) gives growth estimates for eight African countries (Sierra Leone, Ghana, Nigeria, the Gambia, Kenya, Uganda, Tanzania, and Mauritius) from around 1880 to 1960.
7. In our four case studies we draw on the work of others as follows: on Sierra Leone, Clapham (1976), Herbst (2000), and Reno (1998, 2000); on Kenya, Mwega and Ndung'u (2008) and Elischer (2010); on Nigeria, World Bank (1958), Iyoha and Orioaki (2008), Collier and Gunning (2008), and OECD (2012); on South Africa, Feinstein (2005), Fedderke and Simkins (2012), and OECD (2012).
8. One of Africa's deadliest civil wars: UNODC (2013: 85).
9. Shadow state: Reno (2000).
10. Real politics: North et al. (2009: 42).
11. Privileges granted to elites: Epstein (2000).
12. Nigeria's private sector: OECD (2012).
13. New estimates: Broadberry, and van Leeuwen (2011), Broadberry, Campbell, Klein, Overton, and van Leeuwen (2011), Broadberry, Campbell, van Leeuwen, and van Zanden (2012), and Broadberry and Gardner (2014). We also draw on related research by Malanima (2011); Álvarez-Nogal and Prados de la Escosura (2012); Leandro Prados de la Escosura is also a CAGE associate.
14. Hardly any time: Pinker (2011: 224-229).
15. The nature of this balancing act has been fiercely debated. The temperature of debate has been raised in part because some scholars have emphasised one side of the balance over another. Our view draws on the work of a wide range of contributors, especially North and Weingast (1989), Epstein (2000), Açemoglu et al. (2005), and O'Brien (2011). As already mentioned, our interpretation owes much to the most recent stage of this debate, represented by North et al. (2009), Cuberes and Jerzmanowski (2009) and Kishtainy (2011).
16. Access to power is either 'open' or 'limited': North et al. (2009).

17. Following the collapse of the Roman Empire: Wickham (2006).
18. Recent research: Kishtainy (2011).
19. Jerven (2010) identifies two generations of literature on African economic growth since the 1960s. In the first generation, there was a focus on 'too much power': Africa's disappointing economic performance was explained largely by the policies pursued by African governments after independence. For this first generation a major source of growth failures was African rulers' interference in their countries' economies for largely political purposes, in order to seize rents and use them to reward supporters. The result of this analysis was a series of 'structural adjustment' reform programmes in the 1980s and 1990s, which aimed to set limits on the capacity of African rulers and ruling parties to interfere in their economies. The second generation emphasised other factors besides policy failure, and looked further into history to understand the origins of Africa's failed institutions. Among the factors that emerged was deficient state capacity, or 'too little power'. The second generation therefore sought to explain why African states have relied on political structures dependent on rent-seeking and patron-client networks. The problem is that these structures do not amount to a 'capable' state. Explanations have included geographical endowments, such as low labour-land ratios and the legacies of colonial rule.
20. Baskaran and Bigsten (2013: 92).
21. Açemoglu and James Robinson (2011).
22. The 'gatekeeper' state in Africa: Cooper (2002); in post-colonial African states: Lynch and Crawford (2011).
23. Homicide rates in Northwestern Europe: Eisner (2003).
24. On one estimate: Hoeffler (2006).
25. Legacies of colonial rule: Gardner (2012); Mkandawire (2005); Olsson (2009). Post-independence political imperatives: Block (2002); Kasara (2007)
26. South Africa: Ajam and Aron (2007). Settler states: Mkandawire (2010).
27. Frye (2010) describes this process in relation to Eastern European transition economies.
28. The rule of law: nearly all economists would see the rule of law and trust in the key institutions of the state and their proper functioning as critical factors enabling people to cooperate (in groups) and compete (in markets) to achieve mutually productive outcomes. Kenneth Arrow, Friedrich von Hayek, Douglas North, and Elinor Ostrom are four Nobel prize winners who would agree on this, even though they would disagree on many other things. See for example Hayek (1960), Arrow (1972), North (1990), and Ostrom (1998).
29. There is reason to think: Acemoglu and Jackson (2014).
30. Good policies can still make a measurable difference: Delgado et al. (2012).