A REAL MARSHALL PLAN FOR AFRICA

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Productivity Growth and Living Standards

- The African Experience:
    - In 1960, the average labor productivity of African countries was about the same as Asian countries — 14 percent of that in the United States. African productivity did not improve relative to that of the United States by 1996; Asia improved its position to 34 percent.
    - The most notorious poor African performers are Angola, Central African Republic, and Democratic Republic of the Congo.
- And questions more generally:
    - Why are living standards and labor productivity in sub-Saharan Africa stagnant or falling behind that of the United States?
    - FINANCE/MANAGEMENT ANSWERS (INCLUDING BLOOM and VAN REENEN) — LINK TO BUSINESS INSTITUTIONS AND BUSINESS ENVIRONMENT

A ‘PRO-GROWTH AGENDA’ DISCUSSION OFTEN CENTERS ON ‘POLICY’:

- Remove barriers to competition
- Protect private owners with well defined and well protected property rights
- Corporate governance arrangements must be transparent
- Macroeconomic environment faced by private decision makers must be stable.

GOOD STUFF, BUT DEVELOPMENT ASSISTANCE CAN DO MORE TO CONDITION ‘AID’ ON ‘INSTITUTIONS’

A Real Marshall Plan for Africa

On June 5 of this year, Bill Duggan and I called for a 'Marshall Plan for Africa' in a piece in the *Financial Times*. That day was the sixtieth anniversary of U.S. secretary of State George Marshall's announcement of what became known as the Marshall Plan for Europe. The Marshall Plan has been widely heralded as an example of the triumph for economic revitalization of foreign aid on a grand scale. Indeed, given the high rate of extreme poverty in the sub-Saharan Africa — and that Africa is poorer today than it was a generation ago — some world leaders have called for a Marshall Plan for Africa.

Of course.

But there is much misunderstanding about the original Marshall Plan. It was less a grand aid program than a large-scale effort to restore the power of business and productivity as a growth engine. A true Marshall Plan for Africa could ignite growth and reduce poverty, but only through a different set of institutions than the current aid system.

Marshalling Resources for Africa

And this distinction is an important one and devotees of the current aid system offer a foil: U.K. Prime Minister Gordon Brown proposed in 2005 a grand aid vision, which he, too, termed a Marshall Plan for Africa. Indeed, he argued that Africa's dire situation calls for massive concerted action by the world community.

Brown proposed four main elements. First, rich-country governments and multilateral institutions forgive all their loans to the governments of Africa. Second, rich countries double direct development aid, including an International Finance Facility that borrows on future promises of aid to frontload spending. Third, African governments commit to anti-corruption measures and more spending on health, education, and welfare. Fourth, rich countries end trade barriers that hinder the import of African agricultural products. These elements are very "macro."

Now let's look at the original Marshall Plan. Here, too, there were four main elements. First, a rich country – the United States – made grants to European governments for restoring production through loans to local businesses who repaid them to their own governments. Second, each European government spent the repaid funds on restoring commercial infrastructure to further boost production, such as ports and railroads. Third, each European government made economic policy reforms to support their domestic private sectors. Fourth, a regional coordinating body handled the distribution of funds among countries. Note that these elements are very "micro."

It is plain to see that, on the one hand, Brown's plan has little in common with the original Marshall Plan. Brown's plan fosters government-led development with an emphasis on social services. The Marshall Plan fostered business-sector development with an emphasis on loans and economic infrastructure. The closest Brown comes to business development is cutting trade barriers in donor countries. The Marshall Plan did the opposite: It cut trade barriers in recipient countries. Brown's plan is the same old aid to Africa in a bigger package. The Marshall Plan was something else, that Africa has never seen on a major scale — a business-sector support project.

Of course, there are some important similarities: The need for action is urgent — Africa is in danger of economic and social collapse, wile Europe was under threat of Soviet advance. Speed is critical — the original plan lasted four years, and Brown's version shouts for success in only ten years. And the efforts are financially similar, both spending about $20 billion per year in today's dollars.

Another recent attempt that invokes the Marshall Plan is the U.S. Millennium Challenge Account (MCA) to which I referred earlier. The MCA offers major aid packages to governments of poor countries who put in place economic reforms and improve human rights and democratic institutions. This plan, too, fails to capture completely the spirit of the original Marshall Plan. The only element in common is economic reform. Other than that, the MCA ends up giving major aid to government-led development. It is not a business-sector support project like the Marshall Plan. Human rights and democracy are good things, of course, but they are not the same as business.

Dueling Marshall Plans

We need to ask ourselves some questions. *Charity or Development*? Recurrent droughts, civil wars, and the AIDS crisis have made Africa the world's leading candidate for charitable aid. NGOs and international agencies have grown up to gather and deliver that charity. That's laudable — but it is not the same as economic development.

The Marshall Plan also faced the question of charity. But as the Plan's historian, Harry Price, tells us: "Welfare needs — in residential housing, schools, and hospitals — through pressing, were widely deferred in favor of more strictly productive investments." Certainly, Africa's welfare needs are greater than Europe's were after World War II, so charity is important. But charity is not a Marshall Plan.

Government or the Private Sector? Current development assistance in Africa goes overwhelmingly through government channels for government projects. The heyday of the African private sector ironically was the 1950s and early 1960s, just before independence. In the present period, starting, funding, and running a business in Africa faces myriad government obstacles — where the Marshall Plan helped European business thrive. In Mozambique, for example, it takes 153 days to start a business. In Canada, it takes two.

And it's not just a matter of corruption — an area of emphasis of the MCA. Anti-corruption measures are good, of course, but they do not by themselves remove economic development from the government's hands. And NGOs are not optimal either. In a 'normal country,' businesses lead development, not NGOs.

Social Services or Economic Activity? Africa's need for social services is clearly significant. Economic development is the sustainable path to social services. The Marshall Plan explicitly aimed for Europe to be self-sustaining at the end of four years. And it was.

But Africa cannot possibly be self-sustaining in four years, like Europe, or even ten years, which is Brown's horizon. (Foreign aid exceeds 10 percent of African GDP.) But a Marshall Plan for the African business sector could make substantial progress over a decade because a thriving economy is self-sustaining. (For example, $10 billion per year over ten years could create a permanent revolving loan fund of $100 billion. The other $100 billion of Brown's plan could be used for social services.)

A Real Marshall Plan

So what *would* a real Marshall Plan for Africa look like today? It would not look exactly like the original, for sure. Africa today is not the same as Europe in 1947. Despite the ravages of World War II, Europe then was in better shape than Africa is now. The Marshall Plan aimed in the first instance to restore the European economy to its prewar prosperity. Sub-Saharan Africa has never had such prosperity to restore. It has always been poor. Yet the essential elements of the original Marshall Plan offer a way forward that any program of development aid must follow.

A Marshall Plan for Africa would first of all stand apart from the current aid system of governments and NGOs. The original Marshall Plan had its own institutions: It created an Economic Cooperation Administration (ECA) to run the entire program, with headquarters in Washington and small missions in every European country. Each country had a special ECA account. Receiving countries formed a regional coordinating body, the Organisation for European Economic Co-operation, which led to both the OECD and the European Union. An African Marshall Plan would have its own institutions to match, along the same international, regional, and national lines.

Second, an African Marshall Plan would concentrate exclusively on *business* development. Social services would remain the domain in governments and NGOs. Africa has tremendous social needs that call for concentrated attention from expert agencies. Let governments and NGOs, who lack a comparative advantage or track record in economic development, specialize in social services. This division of labor rules today in most rich countries. It is a winning formula throughout the world. Let Africa do the same.

A business-only Marshall Plan would set up the equivalent of an ECA to collect and manage the funds on the donor side. An African country would become eligible through specific policies in place to foster business development, and might then have its own revolving fund in a special account. In the original Marshall Plan, governments spent the repaid loans on economic infrastructure projects the ECA approved. An African Marshall Plan can do the same. Given Africa's size and diversity, there might be regional ECAs rather than a single one for the whole continent. The Marshall Plan was competitive among countries: If one did not cooperate, another country was happy to take the money instead. An African Marshall Plan would preserve this key element of the original.

The funds themselves would go for a variety of purposes. Above all, they would not go for government economic development plans, the old system that did not work. Competitive regional funds would support a variety of activities all based on best practice accumulated over the history of aid, from the Marshall Plan to today. Almost every multinational, national, and NGO aid agency has some unit or program that does, indeed, help the private sector. Gordon Brown's own Department for International Development has an excellent Enterprise Development Department with plenty of expertise and experience in the field. An African Marshall Plan would, above all, inventory what already works and do more of it in more and more African countries.

One such unit is Doing Business, a joint program of the World Bank and the International Finance Corporation. This unit compiles an annual report on ten key indicators of a healthy business sector in 155 countries. The indicators are starting a business, dealing with licenses, employing workers, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts, and closing a business. Africa ranks low on all of them. A key use of funds in an African Marshall Plan would be programs of activity to reform these practices throughout Africa. Again, there is plenty of best practice already from which to learn.

An African Marshall Plan would also draw from best practice in other countries. For example, some official aid in Eastern Europe in the 1990s helped foster business development directly. There is plenty to emulate in these good examples. And the booming microfinance sector has plenty to draw on too. But the overall program is not just about microfinance, or even small business. An African Marshall Plan should be an all-business support project. Microfinance can thrive today in some countries because small loans go to individuals, not companies. When an entrepreneur reaches large enough scale to become a small business, the official restrictions kick in and the business cannot grow.

In the way that microfinance spawned new institutions and mechanisms over the past thirty years, an African Marshall Plan must foster creativity on new institutions and mechanisms for Africa's missing mid- and large-size businesses. The whole program needs to be entrepreneurial, to see new opportunities and new combinations as events unfold.

Acknowledging a Role for Business and Business Schools

This leads to the last key element of an African Marshall Plan: *The business sector must lead it*. Business leaders staffed the original Marshall Plan, including its head, Paul Hoffman of Studebaker, a major car maker of the day. An African Marshall Plan should be a creation of the business sector, in flesh as well as spirit.

With a business core, it is likely that it would be less popular than Brown's plan — after all, charity touches the heart, and business does not. The original Marshall Plan started out with only 14 percent of the U.S. public in support. The tide for action was turned by an aggressive information campaign by American business leaders; in this case the Committee for Economic Development. By contrast, business leaders have been conspicuously absent from the growing debate on African poverty.

And business schools can help, as the world's leading institution for the support of the business sector. Business schools would play a key role in supporting the entire enterprise with research, training, and outreach to the business community. The units within aid agencies that do foster business development are simply too small and too beholden to their agency's overall mission to lead the way. In contrast, business schools offer a strong network of established institutions already dedicated to support for the business sector.

Research at business schools would include the perpetual harvesting of best practice in rich and poor countries on successful ways to foster business, as well as best practice for the African businesses themselves to succeed in their sectors. Training would include MBA and executive programs for African professionals to run businesses or to support them in Marshall Plan programs. And outreach includes an ongoing forum for the business sectors in Africa and to make a concerted case to philanthropists that the business path is also worth their interest.

There are strong links among all these activities. For example, an executive education program might bring together a group of African professionals at a time to learn about how a healthy business sector works and to study best practice most relevant to their current situation. Executive education programs often lead participants to work on a "personal case" during the sessions, with help from faculty and each other. This personal case can be the start of a proposal to the regional African Marshall fund. Or participants from the same business, agency or country can work on a joint proposal. The graduates also become advocates for reform in their countries, with specific actions to propose. Such business school programs would offer a way for African professionals who left their countries to find a useful way to return. The best and brightest have left the continent. This kind of program can help them return.

Business schools in rich countries might run such programs in partnership with business schools in Africa (as we do at Columbia Business School). There are many other teaching, research and outreach activities to conduct jointly at first and then wholly in Africa. Business schools would compete to participate, with Marshall Plan funding. This method stands in sharp contract to "African capacity building initiatives," which rank high among the notable failures of the past decades of development aid. That is, aid agencies gave African government institutions multi-year scholarships and exchange visits, operating funds, and technical assistance to build them up. Most African business schools are government institutions, enmeshed in the old aid system. In a Marshall Plan, they must be entrepreneurial — like business schools in rich countries — to develop good proposals for funding.

Business schools can also help educate a new generation of philanthropists on how to redirect some of their charity. Helping business thrive will never have the same direct humanitarian appeal as giving food or medicine to a helpless child. Philanthropists know that business is the source of their own wealth, but they typically do no know how hard it is for business to survive in the current aid system. Warren Buffett, for example, said in an interview after his donation to the Gates Foundation, "A market system has not worked in terms of poor people." This comment reveals a common misunderstanding about most poor countries — that, somehow, the business sector has not delivered the goods. But this observation is not true: The business sector has not had the chance. There are many good ways for philanthropists to help change this. Business schools can show them how.

Does The Marshall Plan Miss The Point?

- Niall Ferguson's question (drawn from a U.S. congressman): What would it cost not to aid Europe? And he argues that Europe would have recovered anyway. Perhaps, but Ferguson himself challenges this notion:

> It helped get the European economies through a balance-of-payments crisis, to be sure. More important, though, it helped European governments balance budgets and reduce inflation. It forced them to shift from wartime controls to free-market mechanisms. And it played an important part in moving Europe from a dysfunctional system of labor relations based on strike action and class conflict to one based on wage restraint and productivity growth. *In all of this, the Marshall Plan resembled the "structural adjustment programs" the International Monetary Fund imposed on borrowers in the developing world during the nineties, but on a larger scale and with much better public relations.*

- Local elites won't buy it — the political economy of acceptance.
    - Rajan-Zingales: Development trap = an initial allocation of endowments such that the constituencies created by those endowments successfully support bad policies that reproduce those initial constituencies over time.
    - Ironically, formerly Communist countries have seen the relatively rapid rise of market institutions following the collapse of the *ancien regime.* One of the virtues of communism is a very strong emphasis on education, and this creates the broad constituencies that can press for "micro" market reforms once the stranglehold of the Communist elite is broken.
    - But, in Africa (and sometimes in Latin America), a relatively small, educated urban middle class has often sided with a small ruling clique in opposing wider, deeper market reforms (in the spirit of Anne Krueger's original description of a *rent-seeking society*).
    - In such a situation, efforts at education and teaching business skills may be needed before market reforms — hence the need for 'business school' involvement. (Indeed, with pro-market reforms coming first, the poor may well have been made worse off in some countries, making them turn against reforms. In addition, once the opportunities for the middle class were liberalized, they too may have withdrawn their support for further reform of endowments.)
    - And there is empirical evidence (Rajan and Zingales) to support the hypothesis that, *ceteris paribus*, attitudes toward competition are affected by characteristics that represent the ability to take advantage of opportunities — education, status, and income.
    - *Implications for sequencing reform*: Education and business skill development can be externally supported. Then external support can encourage reforms that produce growth: Economic growth can create greater opportunities, which in turn reduce the incentives of the privileged to defend their turf, and instead make them focus on reforms that remove impediments to taking advantage of opportunities.
    - Note the difference with respect to both Sachs and Easterly.

Realizing It's Time for a Change

The great French historian Marc Bloch, said this about the transition from feudalism to capitalism in the middle ages: "The older agrarian regimes worked as interlocking systems. It was difficult to take an axe to one part without destroying the whole." Development aid is now an "old system" in Bloch's terms, despite existing for less than half a century. It has its own institutions, rules, norms, career ladders, and funding sources. Thousands of skilled professionals have excellent training in exactly what they are doing, but not in what they should be doing. It's a huge interlocking system that cannot change quickly. But can it change at all?

Gordon Brown, Jeffrey Sachs, and many prominent philanthropists personify a growing spirit that 'we must do something' for Africa. A true business-like Marshall Plan is the 'something' we should do. There are many details to work out, but the original offers hope: The ECA became law on April 3, 1948, and by June 30, it had set itself up and disbursed $788 million in aid. With a clear economic mandate, an African Marshall Plan could bypass government bureaucracy to work with the greater flexibility of the private sector.

A new Marshall Plan would work — it would require no leap of faith. Despite its scale and rapid implementation, the original Marshall Plan was an *incremental* program. It built on what came before — it made existing European businesses stronger. An African Marshall Plan would do the same: It would take different kinds of African businesses a step further in their development. The large overall effect would be the sum of many small ripples. That's how a market system works.

For an African Marshall Plan to work, the aid system must cooperate, too. Governments and NGOs must disentangle themselves from economic development, and concentrate all their efforts on social services. This requires a huge shift in many bureaucracies large and small. Above all, it requires leadership. In the 1980s, Deng Xiaoping dragged China's bureaucracies toward the business world. The head of every aid institution, government, and NGO must now do the same. Again, business schools can help. Business sectors are constantly reforming — they must, or they die — and business schools play a key role. For example, American industry in the 1980s faced stronger Japanese companies with much better business methods. Business schools helped them catch up. Today, business schools face enormous demand in China and India, where the new business sectors know full well the value of business education. They can do the same for aid.

In the first round of an African Marshall Plan, aid experts must go back to school. Business schools can give them the training they need to get up to speed on the business sector overall and in the countries where they work. Many aid experts simply do not know much about business. It will take tremendous humility to admit that — and to re-tool for what is really needed. But we have no choice.

In his speech, George Marshall was very clear that the "breakdown of the business structure of Europe during the war" was the problem that aid most needed to solve:

> It is logical that the United States should do whatever it is able to do to assist in the return of normal economic health in the world, without which there can be no political stability and no assured peace. Our policy is directed not against any country or doctrine but against hunger, poverty, desperation, and chaos. Its purpose should be the revival of a working economy in the world so as to permit the emergence of political and social conditions in which free institutions can exist. Such assistance, I am convinced, must not be on a piecemeal basis as various crises develop.

Marshall's logic applies just as much to Africa today: a thriving business sector is the key to improving political and social conditions.

He was right. Today Africa needs business. And aid must help, not hinder, and reform itself on the same scale as China, India, and Eastern Europe have done. If not, Africa will fail to seize the promise.

- Interesting global productivity facts:
    - *There is substantial dispersion in labor productivity across countries*: In 1960, an average worker in the richest 5 percent of countries in the world produces about 35 times more output than an average worker in the poorest 5 percent of countries in the world.
    - *Disparity in labor productivity has increased over time*. By 1996, the labor productivity ratio between the richest and poorest countries increased to approximately 46. And this increase in disparity is explained by a substantial deterioration in labor productivity in the poorest countries relative to that of the United States.
    - There is substantial mobility of individual countries in the distribution of labor productivity over time. Labor productivity in Hong Kong relative to that in the United States rose from 19 percent in 1960 to 94 percent in 1996 — an almost fivefold increase during the period — while relative labor productivity in Venezuela declined from 94 percent in 1968 to 36 percent in 1996 — a more than twofold drop in relative productivity.