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African Poverty and Western Aid: Paper 1

Beyond *The End of Poverty* Building Structures and Policies for Long-term Economic Growth

Introduction

Jeffrey Sachs, the brilliant economist who for the last few years has been director of the *Earth Institute* at Columbia University, argues passionately in *The End of Poverty* for more development aid from the rich world in order to overcome a seemingly intractable poverty trap of subsistence living. He explains that with key investments on the part of the donor countries – in health, infrastructure, and education – poor countries can accumulate enough capital to get out of the vicious cycle onto the ladder of modern economic growth. While his suggestions are appealing, Professor Sachs seems to overlook the importance of the context in which this aid is dispersed, the governmental structure, policy environment, and trade relations that determine how an economy will function over the long-term; in doing so, whatever incremental gains the aid program might achieve will be fragile, because new hospitals, schools, and roads, while necessary, cannot counteract the destabilizing forces of inadequate political representation and are not a panacea for bad international trade policies. Sachs' improvements, while in and of themselves meaningful, might be fleeting instead of the stable base on which to build future prosperity.

Professor Sachs does, however, understand the transformative power of the industrial revolution, what he terms the *ladder of modern economic growth*. Building on the work of Jared Diamond and his *Guns, Germs, and Steel*, he explains that due to

variable geography, societal conditions, and trade relationships, the modern industrial revolution was destined to begin in Great Britain, with its enviable combination of fertile geography, access to European markets, and relatively open society (33-34). After this initial spark of creativity, the power of these new technologies combined with the incentives of capitalism soon propelled Western Europe and the United States onto a path of self-sustaining economic growth. Over the course of the twentieth century, these processes spread around the globe.

However, not all countries had the right mix of natural endowments and societal factors to benefit from these technological advances, and the ones that missed out the most were the African countries south of the Sahara. According to Professor Sachs, there is a way out of the poverty trap that plagues these societies, but only if the rich world is willing to invest huge amounts in new investments. While noble, it is unclear if these massive new investments, without associated reforms in trade policy and domestic governance, would allow poor countries to really get on the ladder of self-sustaining economic development.

1. Delivery Difficulties & The Problems of Scaling Up Across the Board

Sauri, Kenya, a Millennium Village that is starting to participate in these interventions as described by Sachs, is indeed a hopeful vision of bettering the quality of life for a specific group of people. However, it is still a test model, and the Millennium Promise in total only covers about 350,000 people across ten model clusters (Millennium Promise). While substantial, it does not suggest the capability of scaling up to cover the hundreds of millions of people living in extreme poverty across Africa.

There is a large disconnect from implementing the full scope of interventions in these few villages with the massive plan that would roll them out on a scale 100 times greater. The 449 interventions that comprise Sachs' "investments needed to end world poverty" are all worthy investments that probably would improve the living standards of the very poor. Sachs convincingly points out that packaging these projects together is necessary, because public health impacts ability to work impacts household savings impacts education and vice versa. However, even though he states that all of these things are needed, he is less than convincing when talking about the ability of the United Nations and governments to cooperate on these initiatives. In the words of William Easterly, this aid "goes astray because we keep trying to train the aid agency cow to win the Kentucky Derby" (2006, p. 12). In other words, it might be too much work to do all of these things at once, and at the end of the day, trying to would just get more people discouraged at the prospect of aid ever working.

Professor Sachs, however, explains the delivery plan will only give money to governments that have a viable *Poverty Reduction Strategy* and where the "collective will is present to be responsible partners in the endeavor" (269). In saying so, he states the limits of his "end of poverty;" that is, only for countries with governments that still want to work within the UN/World Bank/IMF system. To add even more complexity, the distribution of aid dollars will be determined by another series of complex calculations to determine each country's "financing gap" with regard to implementation of their PRS. Although he says this explicitly, it seems that Sachs is suggesting that a new level of bureaucracy will overlay the existing aid organizations to organize all these calculations, but be agile enough to adjust implementation dynamically across different countries'

environments (the clinical economics that Sachs endorses, see Chapter 4). Since the examples he lists for scaling up (see pages 259-265) are much, much smaller than the breadth of changes he proposes, it is unclear whether the various aid agencies will be up to the task.

2. The Broken Ladder: Stagnation and the Necessity of Structural Changes

If we assume that the government does indeed successfully distribute the influx of new funds along the guidelines in their *Poverty Reduction Strategy*, then what happens next? After a “Big Push” of billions of dollars of investment in new schools, roads, health systems, and agricultural technology, does society simply step onto the ladder of modern economic growth and be on its way? Historically, the cases have been more complex than this simple notion. As William Easterly points out in *The White Man’s Burden*, “poverty is a complicated tangle of political, social, historical, institutional, and technological factors,” (6) and so someone should be wary of an all-encompassing solution.

Importantly, as Easterly argued in his 2001 *The Elusive Quest for Growth*, income derived from capital is just one factor that determines GDP, accounting for one-third of total production (51). Two-thirds accrues from the wages to workers. An important corollary to this idea is that the only way to increase GDP per capita over the long term (*labor productivity*) is through the process of technological innovation, in that “technical change avoids diminishing returns if it saves on the ingredient in fixed supply” (Easterly 2001, p. 53). Easterly compares growth in human capital, i.e. the kind of capital that would accumulate from Sachs’ proposed interventions in health care and education, to GDP growth, and again finds little correlation (76). He instead emphasizes that the policy

environment must be correct to sustain economic growth, an environment that rewards these newly educated graduates with the proper incentives to grow the economy, not one that incentivizes them to manipulate government interventions (82).

Although it seems that Easterly overlooks many of the benefits of increasing investment, his ideas about capital do remind us that a wave of investment (even on the scale that *The End of Poverty* proposes) is not enough to get an economy to grow over the long-term. Thus, necessary policy and structural changes need to be implemented that take advantage of increased capital to sustain economic expansion. These will be especially important if, as could be feared in *Section 1*, the only increase in government's technical capacity is a new framework to spend aid dollars, and not new abilities within the permanent bureaucracy. To use aid correctly – that is, as a footing for sustainable economic growth – reforms must be enacted that adjust the incentives: encourage people to grow business, not play politics.

A useful analogy could be provided by Mexico and the introduction of NAFTA. A recent article in *The New York Times* entitled “Nafta’s Promise, Unfulfilled” described a country with immense opportunities and access that did not keep advancing. In the words of Kevin Gallagher, a Boston University professor, “Nafta was a great opportunity, but you had to build on it” (Malkin 2). Economists argued that the Mexican government refused to enact real reforms, and as a result the economy “atrophied” (*ibid.*, p. 1). If the Sachs investment plan is implemented, the key is to avoid what happened last time a “Big Push” was all the rage, which was in the 1960s (Easterly 2006 p. 10): financing what essentially were state-run economies and enriching the corrupt ruling class.

3. Other Ways of Attracting Capital and Investment: The Case of China

As Professor Sachs obviously knows, there are other ways to increase capital and investment and raise living standards than a massive aid package, because this process has been happening organically since the start of the industrial revolution, with the dispersion of technology and knowledge. He describes these events himself, and uses them as a hopeful signal that indeed all countries can achieve this economic possibility. However, and this is his central reason behind vastly increased aid, Africa is still too underdeveloped, with abysmal infrastructure and geographic conditions that cannot possibly facilitate foreign investment. Sachs contradicts himself, though, when talking about India, saying that their market reforms were clearly behind recent growth, now that “businesses that could find profitable opportunities were suddenly allowed to pursue them” (178). Later, though, he acknowledges that basic infrastructure is still lacking, but that *India itself can invest in these services*, now that income has risen to adequate levels. Sachs seems to say that by first opening themselves up to trade and investment, India could raise its income, which would then allow increased investments in social services, but that in Africa, the infrastructure must come first, in the form of public aid, to have any hope at attracting trade and investment. Given the fact that African infrastructure is probably marginally worse than India’s was, this might indeed be true, if not for the actions of the profit-motivated investment of one country: China.

In recent years, China has dramatically altered the development landscape of Africa by deepening economic ties between them. China has become the “mover and shaker” in many countries, from oil-exporting countries like Chad, Sudan, and Nigeria to mineral-rich countries like Zambia even to agricultural countries like Cote d’Ivoire.

Moreover, unlike the World Bank/IMF with their tight restrictions on lending, the Chinese “have stepped into this picture, coming to struggling countries like Chad with deep pockets, fewer demands on how African governments should behave and an avowed faith in everyone’s ability to prosper” (French and Polgreen 2007A 1). In many countries, Chinese companies are building new roads, irrigation systems, and mobile phone networks, with the expectation of being paid back in natural resources. Many governments are more than willing, and the Chinese too seem determined to stick it out over the long haul, with the foreign minister to Chad explicitly saying, “if they don’t produce things today, they will.” (*ibid.*, 1)

In addition to contracts for natural resources with big state firms, increasing numbers of Chinese emigrants have come to Africa after pioneers told them of “abundant opportunities in a part of the world where many economies lie undeveloped or in ruins, and where even in the richer countries many things taken for granted in the developed world await builders and investors” (French and Polgreen 2007B, p. 1). However, others worry about a return to colonialism, where China hunts for and extracts resource wealth from the continent, sending boatloads of cheap manufactured back in exchange.

Although the side effects of unrestricted Chinese investment are not ideal (funding corrupt or oppressive regimes, such as that in Sudan), this method of increasing capital is definitely another avenue to increase investment in Africa. Additionally, when combined with institutional reform and safeguards to prevent a neocolonial-type relationship, the Chinese investments might be leveraged for higher economic growth over the long term.

4. Reforming International Trade Policy to Ensure Export Markets

In his chapter, *Why Some Countries Fail to Grow*, Professor Sachs does briefly mention trade, but only insofar as it relates to the division of labor within the country and access to local agricultural markets. It is possible that these are the only factors that need to be considered if the goal is lifting the populace barely beyond subsistence. However, any idea of longer-term economic expansion is rendered impossible without access to the benefits of the world market; indeed, the machine of prosperity that Sachs identifies as the ultimate way out of poverty.

What perhaps is the best hope for new trading opportunities is the Doha Round of World Trade Organization negotiations. As Sachs describes, “[in the fall of 2001] it seemed that the Bush administration would pursue more than a military approach. In November 2001, it promoted the launch of a new global trade round, in Doha, Qatar. The resulting Doha Declaration placed emphasis on reform of the trading system in order to meet the needs of the poorest countries. An even more important event followed...”

(217). Compared to these few sentences describing opportunities to change trade policy, he spends the next twelve pages describing the Monterrey Consensus to increase official development assistance (ODA) to 0.7% of rich country GDP. It seems that Sachs is eager to ignore what might be more important (that is, a more equitable international trading system) to turn attention solely on pledging more money, which is indeed his central theme. That is unfortunate.

The Doha Negotiations in the WTO are perhaps one of the most crucial long-term changes that can lift living standards for Africans. The initial declaration agreed to work for the hundreds of millions of African farmers by expanding opportunity for their

agricultural exports to be competitive on international markets. Although African goods are given duty and quota free access to their main markets (ODI 3), they are not competitive globally due mainly to price distortions caused by massive agricultural subsidies for farmers in the rich world. Changing these policies have been the main sticking point of the Doha negotiations (Dougherty 1), because the developed countries see their farmers as an essential constituency and part of their heritage that cannot be lost. However, this reluctance to give up these handouts has caused these trade talks to fall apart on multiple occasions; they are only limping along now.

In addition to agricultural trade, the Doha round aims to expand the market for manufactured goods from Africa by assisting firms through technological upgrades and training on how to meet EU and US health and safety requirements (ODI 4). With minimal financial assistance, foreign aid could be redirected toward these goals and crucial foreign exchange could be earned in the process.

The most important achievement for Doha, however, would be real opportunity for African firms and individuals to sell their products and services on the world market. This access is essential to participate (like Sachs illustrates in Bangladesh) in the ladder of modern economic growth, sustaining short-term gains in well being, and progressively building on top of them. By using the proposed increase in aid dollars to instead lessen rich world agricultural subsidies and help build technical expertise at African manufacturing firms, there is a clearer path toward self-sustaining economic growth at costs much lower than in Sachs' aid-dependent approach. It is also a way of escaping poverty that gives more flexibility to the African private sector to organically create wealth. When combined with efforts toward providing free-trade zones and blocs within

Africa itself, these new trade policies can achieve a large open market that Paul Collier says is a good precondition for a turnaround (Collier 72), and one that can provide a more stable base for long-term economic growth.

Conclusion

The End of Poverty is both an alluring goal and a nearly plausible action plan to get there. Professor Sachs, drawing on decades of development experience, outlines the main factors driving modern economic development and the missing pieces that African countries don't have. He argues that due to factors of geography and the disease burden, these least developed countries have not achieved modern economic growth over the past 150 years like the rich world has, but have stagnated in a poverty trap of subsistence living. Sachs proposes massive new investment in public health, education, agricultural technology, and infrastructure to give these countries a boost onto the ladder of development. However, as shown above, there are three main problems with this strategy: *the difficulty of implementation, the unclear next steps, and the presence of alternatives to acquire capital*. Without a clear path ahead from the interventions he proposes (comprehensive domestic policy and international trade reform), Sachs' plan might not put countries on the path to long-term prosperity that he promises.

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