Ghana, Senegal, and Uganda Adopt Bold Reforms

For the past decade, sub-Saharan Africa has been struggling to improve its economic performance. A new *Occasional Paper* by the IMF's African Department, *Adjustment for Growth: The African Experience*, looks at the experiences of Ghana, Senegal, and Uganda, and concludes that implementation of far-reaching adjustment and reform programs can boost economic performance. The main requirement for success is an appropriate mix of comprehensive adjustment and reforms that increases private saving and investment. To achieve this end, all three countries—and indeed all African countries—need to implement sustained and consistent policies to keep inflation low, step up fiscal consolidation, and promote financial reform.

Four themes dominate the IMF study:

• *Saving and Investment.* The adjustment experience in sub-Saharan Africa underlines the importance of expanding private saving and investment as a prerequisite for growth. For example, the ratios of total saving and investment to GDP in sub-Saharan Africa during 1986–92 amounted to 11.8 percent and 18.6 percent, respectively, compared with 24.5 percent and 25.7 percent for developing countries generally. An investment-to-GDP ratio of about 25 percent is needed by sub-Saharan African countries to maintain a sustainable annual growth rate of about 6 percent.

• *Tight Financial Resources.* Given growing demands for limited foreign assistance funds, African countries will need to develop their domestic financial resources and attract more foreign investment.

• *National Differences.* While sub-Saharan African countries have many points in common, there are significant differences among them. In particular, some have made sustained adjustment efforts over a period of time and some have not been able to do so, owing to civil strife or other reasons. While the countries in the first group are already reaping the fruits of their efforts, they will need to continue to pursue sound policies—adapted to the specific contingencies facing each country.

• *Policies Matter.* In many African countries, the expansion of private investment has traditionally been impeded by such political factors as structural and institutional constraints and governmental intervention in the setting of prices, wages, and exchange rates. While public policies are not the only determinant of private saving and investment in Africa, the recent success of stabilization and reform programs in Ghana, Senegal, and Uganda confirms the importance of policies explicitly designed to foster an environment of low inflation, reduced economic uncertainty, higher private saving and investment, and a stronger human capital base.

The experiences of Ghana, Senegal, and Uganda also demonstrate that effective implementation of medium-term adjustment and reform programs can generate positive economic results rather quickly. The divergence in performance among various groups of sub-Saharan African countries reflects differences in their policy responses to deteriorating terms of trade and disappointing progress in fostering macroeconomic stability, improving external competitiveness, and alleviating structural and institutional impediments to private sector activity.

Notwithstanding their differences, the IMF study highlights important commonalities uniting the three African countries under review. In general, each has suffered from a legacy of governmental intervention in the economy, low savings rates, lagging productivity, and marked vulnerability to external shocks. More narrowly, the three case studies highlight the costs associated with changing and uncertain economic policies.

Ghana (1983–91)

At independence in 1957, Ghana was the world's largest cocoa producer. It enjoyed the highest per capita income in sub-Saharan Africa, with external reserves equivalent to three years of imports. Over the next two decades, however, economic performance weakened in response to interventionist policies, including controls on foreign exchange, prices, and credit, and quantitative restrictions on imports. These policy choices in turn triggered large public sector deficits, surging inflation, and a negative balance of payments position. Ghana's economic difficulties were further exacerbated by a severe drought in 1983 and falling cocoa prices. By 1982–83, Ghana's economy had virtually collapsed.

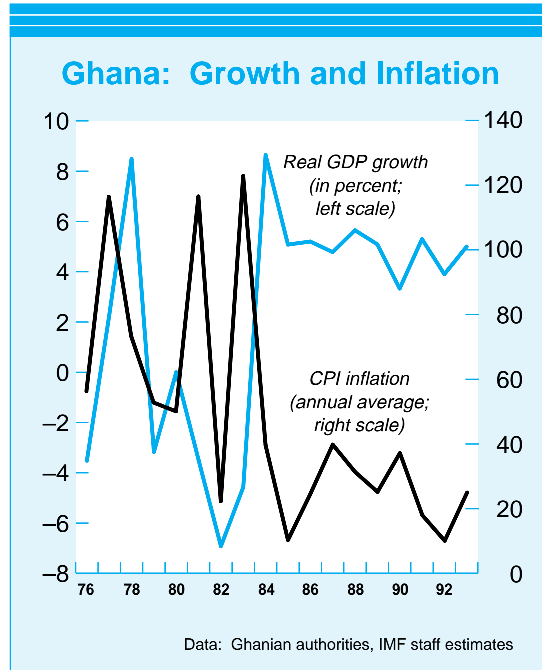
In the aftermath of these shocks, Ghana launched an ambitious economic recovery program in 1983. Key elements of the reform strategy included a realignment of relative prices to encourage more productive activity, the promotion of exports, and strengthened economic incentives; a progressive shift away from direct controls and intervention and toward

greater reliance on market mechanisms; early restoration of fiscal discipline; measures to increase public saving and reduced recourse to bank financing of the government; rehabilitation of the economic and social infrastructure; and implementation of structural and institutional reforms to enhance economic efficiency and encourage private saving and investment.

Liberalization of the exchange and trade system was another important element of Ghana's reform program. Before 1983, the system suffered from foreign exchange controls, restrictive export regulations, pervasive quantitative restrictions on imports, and high trade taxes. Beginning in 1983, average effective export and import tariff rates were significantly reduced. By the latter part of the decade, Ghana had removed nearly all quantitative restrictions on imports.

The policy response to these changes has been impressive, according to the IMF study. By the late 1980s, severe fiscal imbalances were brought under control, and a distorted exchange and trade system was liberalized; by the end of 1991, inflation was lowered to 10 percent, from 123 percent in 1983. Strong recovery in real growth also triggered a tangible increase in real per capita incomes, reversing a long decline. And Ghana's growth performance responded well to the liberalization of the exchange and trade regime and the elimination of price controls.

Important challenges remain. Amidst a high rate of inflation and lagging efforts to achieve structural reform, the private sector's role remains limited, owing, in part, to the continued large role played by the public sector in economic decision making. Apart from the need to reduce government intervention in the economy, other reform priorities include parastatals, the regulatory framework governing investment and tax policy, and primary education and literacy.



Senegal (1978–93)

From 1960 through the early 1970s, Senegal followed inward-looking policies and the economy grew at a low rate compared with neighboring countries. A series of droughts during 1978–84, combined with deteriorating terms of trade and inappropriate financial and structural policies, further weakened Senegal's economic performance. Average yearly growth declined to 2 percent during 1978–84 from nearly 5 percent for the 1974–77 period.

In the early 1980s, Senegal undertook a series of macroeconomic stabilization and reform measures that helped reduce macroeconomic imbalances and inflation. Senegal also registered some progress in implementing structural reforms to increase production, exports, and job creation. To eliminate barriers to private sector activity, it took steps to liberalize labor legislation, prices, and external trade. And it achieved visible breakthroughs in privatization and restructuring public enterprises.

According to the IMF study, Senegal's weak and deteriorating competitive position may have worsened some of its economic difficulties during the reform period. Of special concern was the substantial appreciation of the CFA franc between 1986 and 1993 relative to the U.S. dollar—a situation that contributed to, if it did not cause, the poor performance of Senegal's exports. Similarly, the large increase in real interest rates in Senegal in the late 1980s may have helped dampen domestic investment.

Two obstacles hindered Senegal's reform efforts throughout 1978–93, according to the IMF study:

• *External shocks* undermined growth, especially during 1989–93. Senegal's narrow production and export base, and its dependence on energy imports, made the economy particularly vulnerable to terms-of-trade shocks and adverse weather, with negative consequences for output, saving, and investment.

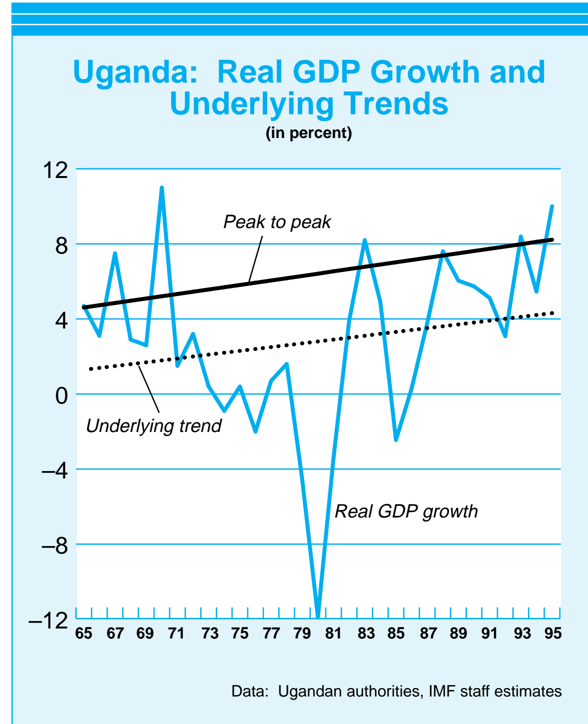
• *Structural rigidities* persisted. Private sector companies held onto their monopolies in such sectors as sugar, cement, and petroleum importing and refining, while state enterprises retained their monopoly over rice imports, groundnuts, and the groundnut oil sectors. And deficiencies in the regulatory and legal environment failed to provide a healthy climate for private sector activity; notably lacking were strong incentives for higher investment and exports. If accompanied by adequate macroeconomic and structural policies, the 50 percent devaluation of the CFA franc in January

1994 (see *Special Supplement, IMF Survey*, March 21, 1994) could prove salutary in strengthening Senegal's external competitiveness and its ability to attract larger volumes of private investment.

Uganda (1987–95)

Uganda faced a difficult situation in the mid-1980s and throughout much of its adjustment period that began in 1986. The civil war had devastated transportation, power, and water facilities. In 1986, per capita GDP was 60 percent below its level of 1970, inflation had risen to 240 percent, and external debt service was more than 50 percent of exports. A fixed exchange rate had eroded the country's competitiveness, leading to an acute shortage of foreign exchange, the emergence of parallel markets, and growing external payments arrears. By 1987, exports other than coffee had all but ceased and Uganda suffered annual declines in its terms of trade every year from 1986 to 1992. Largely as a result, Uganda's ratio of scheduled debt service to exports increased sharply.

Uganda's reform and stabilization program has been a major success. Economic growth averaged about 6.4 percent during 1987–94, while annual inflation fell to 3.4 percent in 1994–95. The ratio of gross domestic investment to GDP also increased markedly, to an average of 14.3 percent, the highest level since the mid-1960s. At the same time, the external current account deficit (excluding grants) declined markedly, to 5.9 percent of GDP in 1994–95 from 16.9 percent in 1988–89. Exports became more diversified, with noncoffee exports representing about 30 percent of the total. All of these changes helped foster a more market-oriented environment, with liberalized pricing and interest rates generating positive incentives for saving and investment.



Over the medium term, the IMF study suggests additional steps that Uganda might take to further raise living standards and stimulate economic growth—beginning with structural reform in the banking and financial sectors. It also emphasizes the need to strengthen the banking system and eliminate distortions in the allocation of financial resources. Finally, efforts should be undertaken to accelerate the transition away from a cash-based economy.

Effective management of its substantial external debt represents another major policy challenge confronting Uganda. Uganda's adjustment efforts have relied to a great extent on disbursements by multilateral institutions. As a consequence, the country's external debt rose to $3.4 billion at the end of June 1995 from $1.3 billion in June 1987, but since the added debt was highly concessional, the average interest rate and maturity on the debt stock improved substantially. Nevertheless, the debt-service ratio was high over the adjustment period, hitting a peak of 128 percent in 1991–92, before falling to a more manageable level of 28 percent in 1994–95. This level of debt, according to the study, demonstrates the need for substantial increases in export volumes and diversification and substantial debt relief.

The Road Ahead

While Africa confronts major economic challenges, the overall message conveyed from the reform and stabilization experiences in Ghana, Senegal, and Uganda remains positive. All three countries have shown progress in enhancing the efficient use of resources. At the same time, the uneven success in mobilizing domestic political support for reform and stabilization should be seen as a call for more sustained and consistent policies.

Drawing on the recent experiences of Ghana, Senegal, and Uganda, the IMF study endorses three broad policy initiatives to assist economic reform and stabilization in sub-Saharan Africa:

• Public policies aimed at keeping the rate of inflation low, reducing macroeconomic uncertainty, and promoting financial deepening can have significant and immediate positive effects on private saving and investment.

• Measures should also be taken to lower budget deficits—without, however, reducing public investment in socioeconomic infrastructure (such as schools and hospitals). Instead, greater attention should be given to increasing revenues through a broadened, and more equitable, tax base and improvements in revenue collection.

• Finally, confronted with increasing competition for international private direct investment, more of the resources for attaining satisfactory and sustainable growth in sub-Saharan Africa will have to be generated domestically. In this context, the indigenous business sector will need to play a major role. Accordingly, public policies should be aimed at fostering an environment conducive to private sector development.

Adjustment for Growth: The African Experience, by Michael T. Hadjimichael, Michael Nowak, Robert Sharer, Amor Tahari, and a staff team from the IMF's African Department, is No. 143 in the IMF's *Occasional Paper* series. Copies are available for $15.00 from Publication Services, Box XS 600, International Monetary Fund, Washington, DC 20431, U.S.A. Telephone: (202) 623-7430; fax: (202) 623-7201; Internet: publications@imf.org