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AFRICA AND THE GLOBAL FINANCIAL CRISIS: TOWARDS A "JUST BARGAIN" AT THE G20 SUMMIT

A BACKGROUND PAPER FOR THE APRIL 2, 2009 G20 SUMMIT IN LONDON

March 2009

Introduction

The financial hemorrhage and its rapid spread across the globe, especially in the developed world, have given cause for policymakers in the developing world to assess the magnitude of its impact on their economies. In what started as a localized crisis in the US, the credit/financial contagion has spread to the real economy and there is now a strongly synchronized global economic contraction unfolding. Africa is no exception. Unfortunately, since the crisis first erupted, relatively little attention has been given to its consequences on low-income countries, especially those in Africa. Initially, the conventional wisdom was that African countries were unlikely to be hard hit or at worst have only minimal impact of the effects of the crisis. This reasoning was principally predicated on among others the following:

- That low-income countries are generally less exposed to the financial contagion than emerging markets, as their financial institutions are not strongly integrated into the global financial system, and because the complex structured financial instruments at the heart of the crisis are rarely used in poor countries (Prizzon, 2008).
- That most banks in Sub-Saharan Africa rely on deposits to fund their loan portfolios (which they keep on their books to maturity) and that their inter-bank markets are small (Maimbo, 2008).
- That in recent years better macroeconomic policies, debt relief, and favourable external conditions (high commodity prices combined with low interest rates) have contributed to lower external debt ratios in many low-income countries, thus helping them better withstand the effects of the crisis.
- That investors weary of the markets in developed countries may seek opportunities in African and other emerging market economies.

Thus the transmission mechanisms between the financial systems in Africa and the rest of the world are weak and should minimize the impact on the crisis. Alas, evidence available up to now, suggests that the crisis after all, has grave ramification for Africa, albeit through some what different transmission mechanisms.

The transmission mechanisms

The transmission of the impact of the financial crisis on Africa remains somewhat different from those in the developed and perhaps, the emerging market economies given the structure and level of sophistication. While the direct impact of the crisis is likely to be more limited, Africa will be severely impacted by the effect of the crisis with an exacerbation of the already precarious poverty situation in these countries. This could lead to African countries missing the millennium development growth targets (MDGs). The channels of transmission in Africa may include:

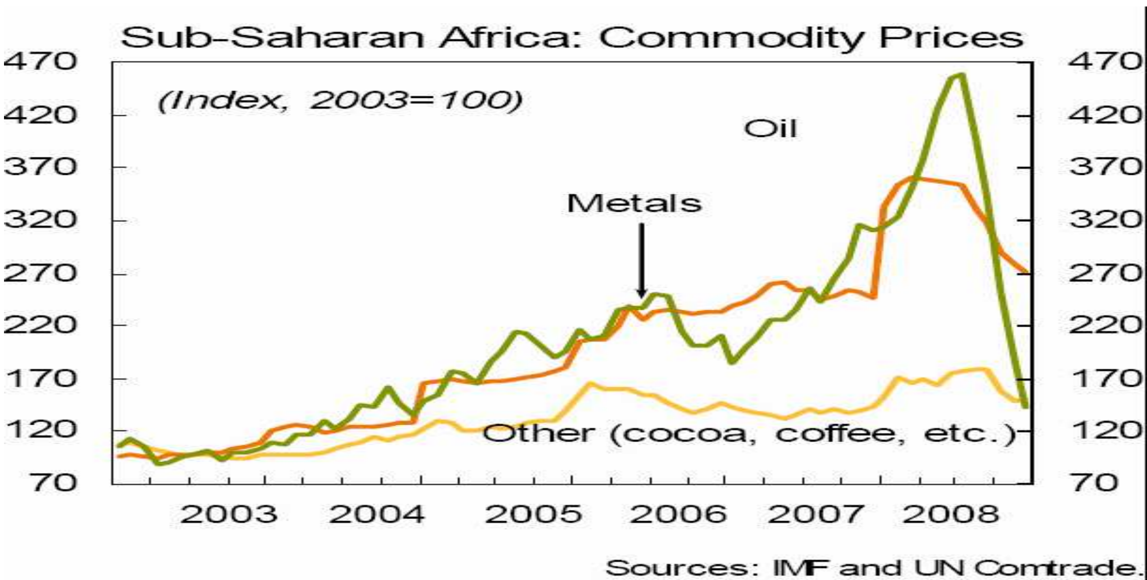
- Slower export growth (global trade is projected to decline in 2009),
- Lower commodity prices (which will reduce incomes in commodity exporters)
- Reduced remittances,
- The potential for reduced aid from donors.
- A reduction in private investment flows, making weak economies even less able to cope with internal vulnerabilities and development needs.
- Losses arising from central bank reserve management practices
- Weakened local investor confidence in equities and bonds on African Stock Exchanges

The IMF notes that *"After hitting first the advanced economies and then the emerging economies, a third wave from the global financial crisis is now hitting the world's poorest and most vulnerable countries,"* in this regard, the FUND suggested that *"Bilateral donors must ensure that aid flows are scaled up, not trimmed back"*. Financial markets in Africa are already feeling the impact of the crisis. Stock markets across Africa which had displayed strong resurgence and an energy that had not been seen for years have started to tumble. As of end-2008, most African country equity markets had given up all or virtually all of their gains since the beginning of 2008 and a number of initial public offerings which had characterized earlier periods had disappeared[1] (see table 1).

Performance of Selected Sub-saharan stock market indices

	Index 18 Dec 08	% change between Dec 07 - Dec 08: One Day	% change between Dec 07 - Dec 08: in local currency	% change between Dec 07 - Dec 08: in $ terms	% change between Dec 08 - 16 Feb 09: in local currency	% change between Dec 08 - 16 Feb 09: in $ terms
Kenya (NASI)	71.2	+8	-28.8	-41.1	-17.1	-19.7
Malawi (Domestic)	4,319.4	+1	+26.4	+27.7	-10.2	-10.0
Mauritius (SEMDEX)	4,704.9	-2.8	-36.6	-44.1	-15.1	-18.7
Tanzania (DSE Index)	26,423.6	0.0	+21.3	+7.5	-0.2	-0.9
Uganda (All share)	4,324.3	+2.9	-21.1	-31.8	-16.3	-18.6
Zambia (All share)	547.1	+1.1	-28.6	-49.2	-7.1	-19.4
GSE (All share)	10,431.6	0.0	+58.1	+25.9	-4.7	-11.4

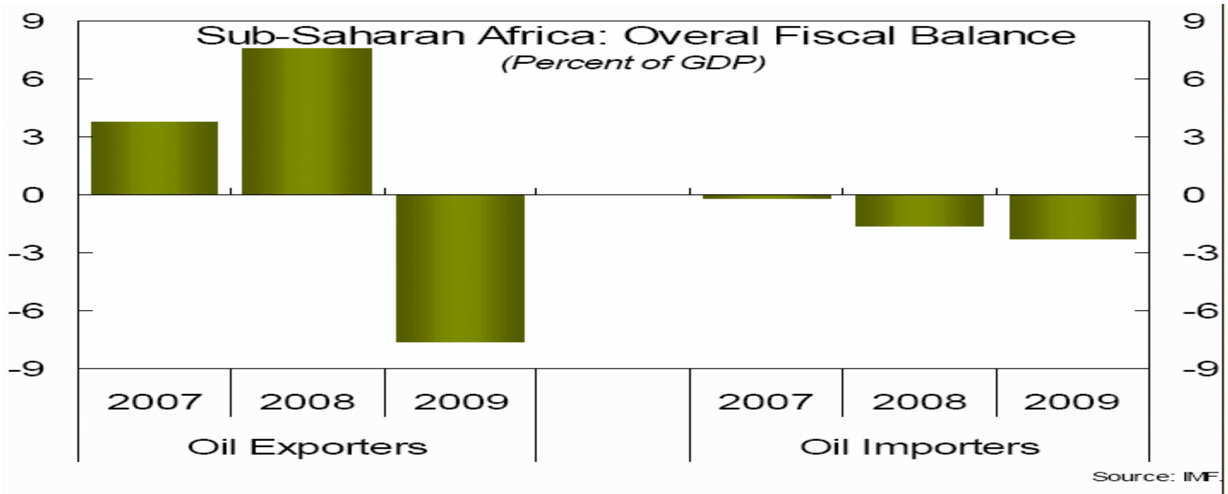
Source: African Morning monitor, page 7. GSE data from the Ghana Stock Exchange and author computations



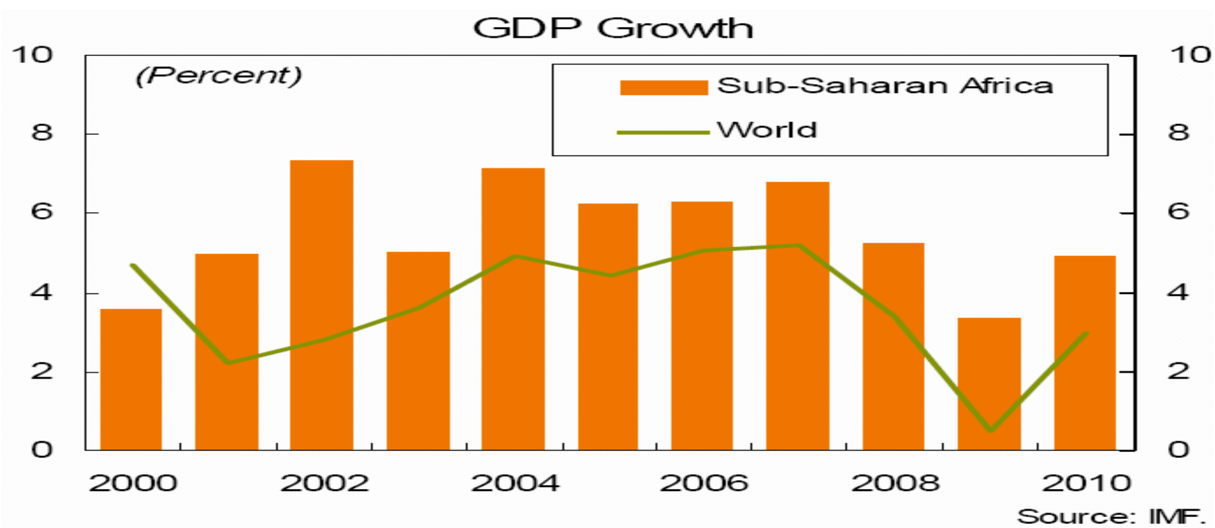
Similarly, many African countries could move into a new danger zone, with heightened risk to exports, investment, credit, banking systems, budgets, and the balance of payments, and remain most vulnerable. Fiscal deficits for instance are expected to worsen not only because of the plunge in export revenues but also because of the need

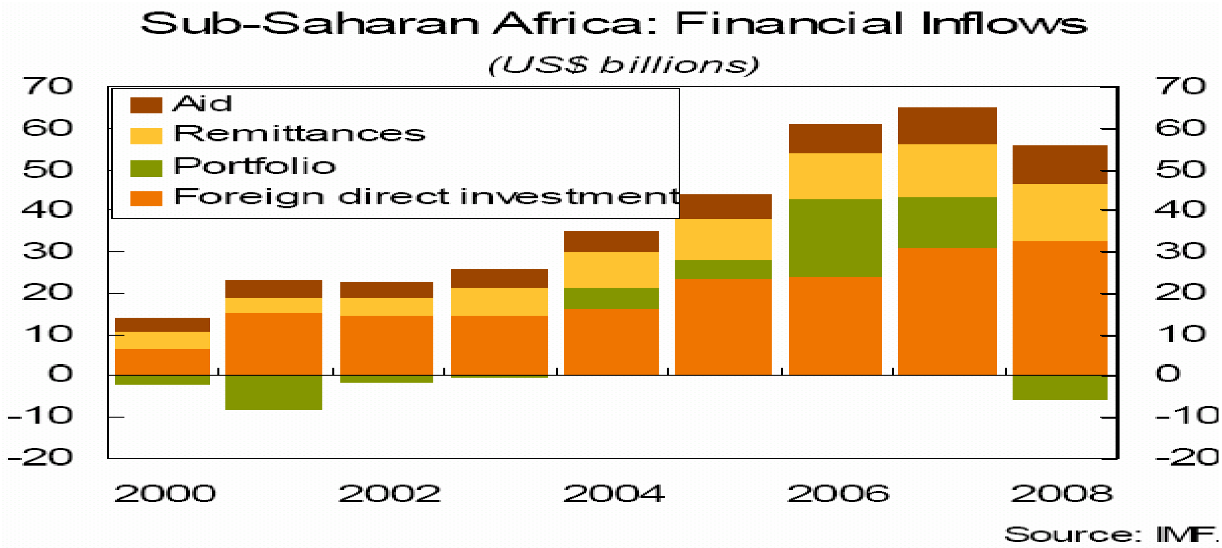
[1] In some instances, there were failed IPOs, for instance the IPO of Ecobank in Ghana.

to increase social spending and safety nets and to provide the fiscal stimulus required to mitigate the worst consequences of the financial crisis.



The plunge in exports demand from the developed countries and an absence of new capital sources (e.g. from sovereign bond issues) will impinge on growth in Africa like the other regions. At the same time, sharply tighter credit conditions and weaker growth are likely to cut into government revenues and governments' ability to invest to meet education, health and gender goals, which are necessary for attaining the MDGs.





In recent years, many African countries as a group have benefited from increasing private flows (particularly FDI and remittances). However, a lot of these countries still heavily dependent on external official aid and debt flows. Besides, debt relief and favourable external conditions (high commodity prices combined with low interest rates) have led to significantly reduced external debt ratios in many low-income countries, though most of these countries remain vulnerable to external shocks.

According to the IMF and World Bank classification, only nine Heavily Indebted Poor Countries (HIPC) are rated as enjoying a low risk of debt distress (IDA and IMF, 2008). The IMF notes in particular that 26 low-income countries "appear particularly vulnerable to the unfolding crisis," including Nigeria, Ghana, Zambia, Albania and Armenia. The entire group will need at least $25 billion in financial aid, and perhaps as much as $140 billion in a "bad-case" scenario. Thus financial crisis will further compromise external debt sustainability for many developing countries, as growth rates and export earnings fall. Moreover, foreign debt is denominated in hard currencies, making repayment ability highly sensitive to shifts in exchange rates. And with the collapse in commodity prices and the recent appreciation of the dollar, exchange rates in many low-income countries have already been falling. For instance, the Zambian kwacha fell 24 per cent against the dollar between August and October. Such depreciations make it obviously much harder to service foreign debt (Prizzon, 2008).

In the last eight years, African countries have made significant progress in the areas of economic performance and good governance. There is a determination to sustain economic reforms, better manage its economies, show and be committed to transparency, accountability and comprehensiveness in the conduct of government business as well as a determined effort to fight corruption. The boom in commodity prices provided the needed revenue to sustain reforms and enhance the growth process. Africa has been able to, among others,

- Improve on macroeconomic management exemplified by robust monetary and fiscal policy; most of the economic fundamentals are moving in the right direction hence the existence of macroeconomic stability
- Liberalize markets and trade
- Widen the space for private sector activity
- Increased FDI in most countries
- Emergence of stock markets
- Investing in people in order to accelerate poverty reduction
- Utilizing aid to reduce poverty
- Improving governance

The remarkable success recorded in several African countries particularly as regards better macroeconomic management, united efforts at self-criticism and evaluation and development agenda (NEPAD, APRM etc) prompted scholars to argue that perhaps Africa may claim the 21st century. The global financial and economic crisis threatens to reverse the trend of satisfactory economic performance in the African continent. African countries can expect to experience weaker export revenues; further pressures on the current accounts and balance of payment; lower investment and growth rates; increased poverty; unemployment; more crime; weaker health systems and more difficulties in meeting the MDGs.

It is against this background that the G20 summit is taking place in London. The issues of concern to Africa at this summit can be discussed under three broad headings:

1. What new policies or reforms can help Africa deal with the financial crisis?
2. What changes in the International Financial System are necessary to avoid a similar financial crisis in future and give African countries the necessary policy space?
3. Exiting from dependence on Aid

DEALING WITH THE FINANCIAL CRISIS AND GLOBAL RECESSION

The present financial crisis which commenced in the United States of America, and spread to Europe is now global. African economies which relatively managed their economies well, resisted bad lending practices, held high levels of foreign exchange reserves, did not buy toxic mortgages (most countries do not even have a mortgage sub-sector), regulated their banks well and minimize excessive risk taking through derivatives, and not in a recession are now beginning to suffer from the crisis.

It is thus compelling that short-term measures to stabilize the situation be put in place in order to restore global economic stability. This would ensure that economic growth and poverty reduction in Africa are not threatened.

Fiscal Stimulus

The financial crisis has resulted in a fall in aggregate demand with indications that this fall could be larger than in any period since the Great Depression. The fall in aggregate demand is due to a large decrease in real financial wealth, an increase in precautionary saving on the part of consumers, a wait and see attitude on the part of both consumers and firms in the face of uncertainty, and increasing difficulties in obtaining credit.

The Governments of the developed countries (the United States, United Kingdom and other European countries for example) have responded to the slowdown in their economies by resorting to fiscal stimulus to increase aggregate demand. Monetary policy has reached its limits with interest rates close to zero in many countries. Indeed many advanced countries find themselves in a situation akin to the Keynesian liquidity trap, leaving room only for fiscal stimulus to boost demand. The developed countries like the United States are more easily able to finance the fiscal stimulus from government borrowing and the Congress has just passed President Obama's $787 billion stimulus package to jump start US recovery.

The international dimension of the crisis requires a global coordinated approach to providing fiscal stimulus however. Olivier Blanchard et al (2008), note that there are several important spillovers that could limit the effectiveness of actions taken by individual countries:

- Countries with a high degree of openness may be discouraged from fiscal stimulus as more fiscal expansion results in a deterioration of the trade balance. If all countries act however, the amount of stimulus needed by each country is reduced.
- Some interventions such as subsidies to troubled industries may be perceived as unfair industrial policy by trading partners
- The history of the Great Depression shows that as the crisis deepens, there is increasing pressure to raise trade barriers.

All these factors point to the need for a concerted approach by the international community. How does Africa feature in the discussion on the global increase in aggregate demand? The answer is that Africa has not featured in this discussion except in asides that refer to the limited ability of emerging and developing countries to undertake fiscal stimulus programs. Rodrik (2008) notes that developing countries are severely limited in what they can do in this respect because they have little room for domestic borrowing. Serious fiscal stimulus requires that they have to resort to external resources, of which there is a severe shortage at the moment. However, the developed countries' fiscal stimulus will be a lot less effective if not accompanied by similar fiscal stimulus in the developing world. Without this, global imbalances and inequalities will intensify.

Aid modality and Infrastructure Finance

The international community has recognized the need to increase external resources to Africa to enable the region weather the global slowdown. However, given the difficulties donors are facing in meeting existing aid commitments to Africa, there is a need for African countries and donors to agree on a more flexible method of aid delivery. For example, although there is a move towards budget support, both recipients and donors could agree on a framework that allows resources from domestic stimulus packages in developed countries to be tied to infrastructure projects in Africa, with firms in donor countries playing a role in execution. This linking of financing and execution of projects will release resources for development in Africa while contributing to employment and growth in donor countries. This idea is similar to the recent proposal of the Senior World Bank Vice President (see Lin 2008). He argued that the fiscal stimulus in developing countries could focus on two areas.

- First, developing counties have pressing needs that can be met through public investments, especially infrastructure investment and projects related to agricultural transformation. There are also international spillovers given that work on infrastructure (using innovative public-private partnerships) will involve the use of materials and expertise from firms in many developed countries. The President of the World Bank, Richard Zoellick has proposed the setting up of a " Vulnerability Fund" whereby the advanced economies contribute 0.7% of their respective stimulus packages (about $15 billion) which can then be made available to the poorest countries as ODA.

- Second, developing countries should invest in social protection and human development to avoid the financial crisis being converted into a humanitarian crisis with permanent declines in the welfare of poorer households. However, not all developing country governments would have the fiscal space, healthy reserves, current account surpluses, or access to capital markets to be able to undertake such fiscal stimulus. Many African countries in particular are challenged in this regard and therefore present a case for donor support. There is therefore the need for Africa to be fully integrated into the coordinated effort to increase global aggregate demand. This would require swift action by the international community to provide the necessary concessional financing to preserve hard-won gains in growth, governance, protection of the socially vulnerable, poverty reduction, and macroeconomic stability.

Meeting existing aid commitments

In an examination of the impact of the financial crisis on aid flows to developing countries, Development Initiatives (2009) note that the financial crisis is a potential "quadruple whammy" for financing for developing countries

First, The value of the existing aid commitments has fallen. The value to developing countries of the EU target of 0.56% GNI in 2010 has fallen by nearly $12bn a year since 2007 as a result in downward revisions to estimates of national income following the financial crisis.

Second, donors may be less likely to meet their commitments. Analysis by the Center for Global Development in Washington DC shows that after each previous financial crisis in a donor country since 1970, the country's aid has declined. For example, Japanese aid fell by 44% in the six years after the financial bubble burst in 1990; and Japan's aid has never returned to its pre-crisis level.

Third, the financing needs of developing countries have increased as a result of rising food and oil prices as well as slower growth in exports, investment and employment. The food and fuel price increases alone are expected to push an additional 100 million people into deeper poverty and this means additional donor financing will be required.

Fourth, there may be substantial declines in non-aid flows to developing countries such as foreign direct investment, remittances, and equity investment. According to an analysis by the Overseas Development Institute, financial flows to developing countries may fall by as much as $300 billion a year, a fall of 25%.

In industrialised countries the fiscal "automatic stabilisers" tend to increase spending in recession, which both dampens the macroeconomic effects of the downturn and channels additional funding to services that face additional costs. By contrast the institutional arrangements for providing finance to developing countries tend to mean that finance is reduced just as needs are increasing, which amplifies the economic downturn, increases economic instability and jeopardises poverty reduction and service delivery.

In 2005, members of the G7 and of the European Union made commitments to increase aid spending by 2010 and by 2015. In addition, donors made specific commitments to double aid to Africa by 2010. Half way to the 2010 target, G8 aid to Africa has increased by only $3.3 billion since 2004, less than a sixth of the increase that they have pledged to deliver by 2010 (Development Initiatives, 2009).

Although the commitments made in 2005 have been consistently reaffirmed (most recently, by G20 finance ministers) it is becoming clear that a number of donors will not reach their 2010 targets, nor will the EU collectively. The EU agreed to reach 0.7 per cent ODA/GNI by 2015 with an interim target of 0.56 per cent ODA/GNI by 2010.

Germany, Italy and France undertook to reach 0.51% ODA/GNI in 2010, and the UK undertook to reach 0.56% ODA/GNI.

The World Bank notes that "aid-dependent countries are particularly vulnerable to disbursement shortfalls and perhaps changing donor priorities". Despite recent commitments to improve aid predictability and to scale up official development assistance, progress has been slow and challenges to sustaining these commitments in the current environment are expected to increase. IDA should assume an increased role in assisting countries deal with the impact of the global financial crisis. IDA15 replenishment (of US$ 25.1 billion for the World Bank to help overcome poverty in the world's poorest countries) should significantly boost IDA's ability in this regard.

Africa should therefore insist at the G20 summit that rich countries meet their existing commitments on aid and debt reduction.

Accelerating Disbursements and Improving Access to existing Facilities

The nature of the financial crisis is such that countries may face a situation that demands a quick and sizeable response to address a temporary balance of payments problem. The IMF's Short-Term Liquidity Facility is one example of such a facility for which outright puchases of up to 500% of Quota is allowed. Africa should also advocate the expansion of access limits for the Compensatory Finance Facility (CFF) that would provide upfront unconditional lending to countries experiencing a temporary shortfall in export earnings. Regional Development Banks like the African Development Bank should also provide Emergency Facilities to assist member countries with the liquidity required in times of crisis.

G20 should urge and support the IMF to put in place a new facility to support African economies during this crisis; this should be a special facility with relaxed conditions to be based on outcomes.

Khoras (2009) argues that accelerating disbursements –the flow of money to already approved projects- is the surest way of helping poor countries. Apparently about $60 billion is already in the pipeline but procedural requirements have stalled delivery. It is suggested that some of these funds be reprogrammed as budget support because of the emergency nature of the crisis.

In addition, aid agencies can relax the amount of counterpart or matching funds that poor countries are supposed to provide. Furthermore, emergency procedures can be used for some countries that have sound policies and programs in place- as in the case of the response of aid agencies to major calamities.

Leveraging Multilateral Banks Capital

The capital of multilateral banks such as the World Bank, Asian Development Bank, and African Development Bank, could be leveraged to the extent that their outstanding loans do not exceed their paid or callable capital. *In this regard an early general capital increase for the African Development Bank is needed to enable it further scale up its interventions in support of countries in Africa.*

Sale of IMF Gold reserves.

At its founding, the IMF acquired gold under its Articles of Agreement as the basis for reserves for the Fund. The world operated on the 'gold standard" where currencies of member countries were tied to the value of gold under a regime of fixed exchange rates (The Bretton Woods System). With the collapse of the "gold standard" in 1971, the IMF kept the gold as a "rainy day fund" (Birdsall and Williamson, 2005). The IMF's gold reserves are the third largest in the World after the United States and Germany and are valued at $9 billion dollars on its balance sheet but with a market value of some $86.2 billion as at August 31, 2008.

The idea of using IMF gold reserves as development finance is not new. Between 1976-1980 $3.3 billion of IMF gold sales was used to finance concessional loans to low income countries. In 1999 the IMF Board also approved gold sales to finance IMF participation in the Highly Indebted Poor Country (HIPC) Initiative.

There has been considerable discussion in recent years about the sale of IMF gold reserves in the context of providing debt relief and more recently to shore up the administrative budget of the Fund itself. The Fund needs near universal support (85 percent majority voting power) from the IMF Executive Board to engage in the use of its gold reserves. The US holds 17 percent of the votes so its agreement is necessary. The IMF is also required under U.S. Law to gain support from Congress before selling any IMF gold. Gold producing countries have also historically been wary about the potential impact of gold sales on world gold prices.

What is different now and why would we expect any agreement at the G20 summit on gold sales as a development finance instrument?

- Emergency situation
- Gold prices have risen dramatically in recent years
- No budgetary cost to advanced countries
- Selling IMF gold constitutes a transformation of a sterile stockpile into a productive resource

Africa can ask that some $13 billion be raised through the sale of some 15% of IMFgold reserves to help developing countries deal with the financial crisis.

Issuance of new Special Drawing Rights (SDRs).

Nancy Birdsall, Joe Stiglitz, Dani Rodrik, George Soros, Montek Ahluwalia, have all called for a new issue of SDRs by the IMF. This can be done almost immediately and does not require the IMF to negotiate a program for every country that needs a loan. Rodrik (2009) notes that the main objection to the creation of SDRs has always been that this would be inflationary. This argument is however supportive of the issue of SDRs in this global recession and deflation. Africa should propose a proposed $250 billion new

SDR issue. Birdsall (2009) notes that this amount can be allocated following a 90-day period of prior consultation with the US Congress by the US Treasury.

CHANGES IN THE INTERNATIONAL FINANCIAL SYSTEM

The international financial system, at the core of which are the Bretton Woods institutions (the IMF and World Bank established in 1945) has proven totally inadequate in anticipating as well as dealing with the financial crisis. It is against this background that the forthcoming G20 meeting is taking place in London on April 2, 2009.

The G20 agenda is expected to address a number of issues including:

- Sound regulation and strengthening transparency
- International cooperation and strengthening financial market integrity
- Reform of the IMF and
- Reform of the World Bank and multilateral development banks.

The British Prime Minister, Gordon Brown has spoken of a " Grand Bargain" to be struck between advanced economies and emerging market economies where emerging market economies would get expanded access to IMF resources with less conditionality, governance reforms that would see the voting shares of developing countries increased significantly, as well as an increase in the representation of the emerging economies in the governance of Fund, World Bank, Financial Stability Forum and Basel Committee on Banking Supervision.

How does Africa fit in this "Grand Bargain" to be struck at the G20 summit? The issues of concern to Africa relate to inter alia Aid Delivery Modalities, the Debt Sustainability Framework, Trade, Voice and participation, Financial Inclusion, and Regional Cooperative Arrangements.

African and other developing countries have voiced their reservations and criticisms of the existing international financial architecture over the years. These criticisms notwithstanding, the financial architecture has fundamentally remained the same since the Second World War. There are a number of key areas that African countries would like to see reformed in the context of the redesign of the global financial architecture.

Increasing policy space

Approaches to aid flows have evolved since the 1950s from project based aid in the post-war era to aid-induced policy reforms, ex-ante conditionality in the context of structural adjustment programmes of the 1980s and mid 1990s, and the present situation of aid based on economic and political benchmarks with a focus on governance and institutional issues (Oya, 2006). In this mode, aid is delivered on the basis of "good policy choices" of the recipient country. Who determines what are "good policy choices" and what is the basis for that determination?

Critical to the determination of good policies has been the World Bank's Country Policy and Institutional Assessment (CPIA) scorecard, which is used by the World Bank in the determination of aid allocation, allowable debt ceiling, and conditionality. Under this methodology countries are ranked according to the quality of their policies and institutional arrangements. This focus on performance represents a significant problem for African countries. For example, under this system a country considered to be doing well in terms of policy performance will receive more aid while a country with poor performance because it is a fragile state will receive less even though its resource needs are high. Furthermore, the current system of aid delivery denies African countries policy space in making a range of different types of policy choices in several areas, including agricultural policy, fiscal policy, monetary policy, exchange rate policy, privatization of state-owned enterprises (SOEs) and trade and industrial policy inter alia.

In the context of the current global financial crisis, Alexander (2008) has posed the question what kind of CPIA rating the United States and EU would receive if they were subject to a CPIA review, in light of their current fiscal policies, bailouts, subsidies, nationalizations, etc. The very policies adjudged as "bad" when implemented by countries in the developing world.

Kanbur (2005) notes that any logic for allocating development assistance resources to a poor country must have two components—how much the assistance can be translated into improvements in outcomes that the donor cares about ("aid productivity" or "performance"), and how much the donor values these improvements in outcomes ("need").

The CPIA formula essentially captures need through the income criterion, and does not go directly to the other components of performance. Nor does the CPIA contain any final outcome variables like poverty, extreme poverty, girls' enrollment, maternal mortality rates, infant mortality rates etc. What it has instead is a series of intermediate variables like trade policy, regulatory policy, property rights, corruption, etc, which it is hoped will eventually influence the outcomes stakeholders are truly interested in.

Kanbur (2005) therefore proposes that while leaving the current IDA allocation methodology essentially intact, IDA should introduce one new category of scoring in the CPIA. This category should evaluate the evolution of an actual development outcome variable up to the present.

The choice of variable is open. It will depend on international consensus and on data availability considerations, but surely the elements of the MDGs are likely candidates. One of the major criticisms against the CPIA methodology is its one fits all application to countries. For any meaningful assessment of country performance, it would be important that the "Outcome" used for assessment of country performance be negotiated on a country by country basis and reflect a country's development priorities.

On the issue of governance and institutions, African governments themselves are concerned about issues of corruption, transparency and accountability. The African Peer Review Mechanism conceptualized and implemented by African governments contains a heavy dose of public sector management and institutions. This shows Africa considers the issue of proper governance as fundamental to growth and development and therefore this aspect in the CPIA may become overburdened as a criterion for assessing access to ODA or any other financial resources.

A World Bank report *Economic Growth in the 1990s: Learning from a Decade of Reform*, concludes that "Perhaps the lesson of the lessons of the 1990s is that we need to get away from formulae and realize that economic policies and institutional reforms need to address whatever is the binding constraint on growth, at the right time, in the right manner, in the right sequence, instead of addressing any constraint at any time…." (World Bank, 2004, pp vi-vii).

Africa should therefore demand a redesign of the CPIA to include a category significantly weighted towards country specific outcomes and to use APRM governance indicators as the measures for progress on governance for African countries.

Debt Sustainability Framework

Linked to the CPIA is the joint IMF-World bank Debt Sustainability Framework (DSF). Under the DSF, debt sustainability analyses are conducted regularly. They consist of an analysis of a country's projected debt burden over the next 20 years and its vulnerability to external and policy shocks. An assessment of the risk of debt distress is based on indicative debt burden thresholds that depend on the **"quality of a country's policies and institutions"** . The DSF is important for the IMF's assessment of macroeconomic stability, long term sustainability of fiscal policy, and overall debt sustainability. Furthermore, debt sustainability assessments are taken into account to determine access to IMF financing. IDA uses the assessment of risk of external debt distress from the DSF to determine the share of grants and loans in its assistance to each low income country.

The DSF can also be subject to the same criticism as the CPIA given that the DSA methodology is very judgmental as to what constitutes good quality policies and institutions. In addition, the framework suffers from a number of shortcomings enunciated by Gray et al (2008) in an IMF Working Paper. Their critique is as follows:

• First, a rising debt to GDP ratio does not necessarily imply unsustainable debt dynamics. Countries may have to run large deficits to smooth consumption, or increase expenditure in investment activities and structural reforms to enhance future growth prospects. This may lead to an increase in the debt ratio, but should not, in and of itself, imply that countries are pursuing fiscal policies that are unsustainable. In fact, the theory underpinning debt sustainability does not require a bounded debt ratio; it only requires that future primary surpluses are sufficient to satisfy the government's intertemporal budget constraint.

• Second, the main focus of the approach is on stabilizing the debt ratio, with very little attention paid to whether the level at which the debt stabilizes might be too "high" (unsustainable) or sufficiently "low" (sustainable). Most studies have attempted to fill this gap by mapping the debt ratios to a "safe" threshold, derived by examining the level of external debt at which defaults occur. Not surprisingly, the studies produced estimates that are quite far apart, ranging from as low as 15-20 percent of GDP to 50-60 percent of GDP for emerging market countries.

• Third, since the debt ratio is highly aggregated—short-term, long-term, foreign and local currency debt are usually lumped together—and released on low frequency, it does not properly account for the impact of changes in the maturity structure or currency composition of debt on debt sustainability.

• Fourth, the approach does not fully take into account the level and changes in the assets and liabilities of the public sector which affect debt sustainability. It frequently fails to incorporate some important public sector assets which are relevant to the ability to pay debt, such as natural resources, foreign currency reserves of the monetary authorities and seignorage revenues.

Africa at the G20 summit should argue for a redesign of the DSA framework to take into account the shortcomings of the methodology and remove eliminate the judgmental element of what constitutes good policies and institutions.

Regulatory Reforms and Financial Inclusion

The G20 has a number of items to be addressed as part of the effort to create a more effective and coherent system of global financial regulation. Bradlow (2008) argues that Africa should insist that the groups working on regulatory reform should look at the creative efforts of countries like South Africa and Ghana and microfinance institutions around the world to expand poor people's access to banking and financial services. At a minimum the new regulatory reforms should encourage efforts to provide financial services to the poor that comply with international best practices.

Voice and Participation

An increase in the share of basic votes for African countries in the governance of the IFIs is desirable to allow meaningful representation for smaller economies as was established at Bretton Woods. Once increased, the share of basic votes should be maintained in future quota increases, to prevent a similar future erosion. With the nearly 37 fold increase in quotas over the past 60 years, the share of basic votes in the IMF fell from 11.3% to 2.1%, whilst IMF membership quadrupled. This has shifted the balance in favor of large quota countries.

The World Bank Board has just added one seat for Africa and there is need for the IMF Board to do likewise. This would reduce the enormous work burden of the two African constituencies, that represent jointly 45 countries, and would allow African Executive Directors to play a more active and effective role in broader policy discussions.

The Financial Stability Forum (FSF) should also be reformed by expanding its membership to include developing countries. Africa should be represented on the Financial Stability Forum as it is on the World Bank and IMF boards. There is also the need for Africa to have permanent representation in the G20. In addition, Africa should call on the G20 to create formal channels through which they can submit position papers and voice their concerns to the participants in the G20. The G20 should be asked to establish a "notice and comment" period prior to all actions and decisions that are likely to have a substantial impact on the poor. Furthermore, decentralization of IFI decision making through country offices would enhance efficiency.

Regional Cooperative Arrangements

Africa may wish to consider drawing from the Chiang Mai initiative (CMI) in Asia for the pooling of reserves on a regional basis to deal with the present crisis as well as provide shock absorbers to future external shocks.

AID for TRADE

Several countries are highly dependent on aid, dependence as a per cent of Gross National Income range from 70 per cent for Sao Tome and Principe to 25 per cent for

Malawi. Countries with low aid dependence include mineral rich countries like Nigeria, Gabon and South Africa.

There is often the old debate as to whether trade or aid is more important. Both sides of the argument have convincing points. However, the reality of today and the current crisis in particular suggest that the answer is not one or the other. Africa needs to trade and has been trading with the rest of the world. Whether she has maximized the benefits of trade is another matter. In fact, most African countries have liberalized trade. Africa accounts for about 2 per cent of world trade and its share of world manufactured exports is almost zero. Africa for the most part depends on its traditional primary goods. The challenge for Africa is to manufacture for exports and the G20 countries have to relax certain conditions to enable African exporters penetrate their markets.

As the United Nations seeks increased financial assistance from donor countries to help meet the flagging Millennium Development Goals (MDGs), the inadequacy of international aid and fairer trade agreements has never been so clear. In 2007 alone, aid to developing countries fell by 8.4%, leaving huge challenges ahead to meet the Gleneagles G-8 target of doubling aid to Africa by 2010. In July 2008, the Doha round of trade talks collapsed again for the third time.

The current global economic crisis should not result in the reduction of aid; rather increased aid should be focused on investment in infrastructure as part of the stimulus menu available to countries in Africa. Africa should demand that developed countries live up to their promises on making the Doha Round the "Development Round".

CONCLUSION

Following the Global financial crisis and accompanying global recession, G20 leaders are meeting in London to find answers to these problems. It is important that Africa take the opportunity presented by the crisis to make its voice heard and have its concerns addressed at the G20 Summit.

As noted earlier, in the last eight years, Africa has made significant strides in the areas of economic and political governance. Africa has been able to inter alia, improve on macroeconomic management, liberalize markets and trade, widen the space for private sector activity, increased democratic governance, and investing in people in order to accelerate poverty reduction. However, the global financial and economic crisis threatens to reverse the trend of satisfactory economic performance in the African continent. Given the enormity of the problem facing Africa, The "Bargain" to be struck in London should not only be "Grand" but should also be "Just". For Africa this means that:

- As the developed countries implement various fiscal stimulus packages, there is the need for Africa to be fully integrated into the coordinated effort to increase global aggregate demand. The developed countries' fiscal stimulus will be a lot less effective if not accompanied by similar fiscal stimulus in the developing world.
- Africa should insist at the G20 summit that rich countries meet their existing commitments on aid and debt reduction.

- G20 should urge and support the IMF to put in place a new facility to support African economies during this crisis; this should be a special facility with relaxed conditions to be based on outcomes.

- Accelerating disbursements is the surest way of helping poor countries. There is the need for donors and international financial institutions to accelerate disbursement of funds to Africa to maximize the impact of these resources. Some of these funds should be reprogrammed as budget support because of the emergency nature of the crisis.

- In addition, aid agencies can relax the amount of counterpart or matching funds that poor countries are supposed to provide.

- *A*n early general capital increase for the African Development Bank is needed to enable it further scale up its interventions in support of countries in Africa.

- Some $13 billion should be raised through the sale of some 15% of IMF gold reserves to help developing countries deal with the financial crisis.

- Africa should propose a new $250 billion new SDR issue by the IMF.

- Africa should demand a redesign of the modality of Country Policy and Institutional Assessment (CPIA) to include a category significantly weighted towards country specific outcomes and to use APRM governance indicators as the measures for progress on governance for African countries.

- Africa should argue for a redesign of the DSA framework to take into account the shortcomings of the methodology and eliminate the judgmental element of what constitutes good policies and institutions.

- At a minimum the new regulatory reforms in the financial sector should encourage efforts to provide financial services to the poor in developing countries who are excluded from access to banking and financial services.

- Africa should ask for representation in the Financial Stability Forum and increased representation on the IMF and World Bank Boards. Also, the G20 should create formal channels through which they can submit position papers and voice their concerns to the participants in the G20.

- Africa should demand that developed countries open up their markets for trade and live up to their promise to make the Doha Round the "Development Round".

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