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## Sub-Saharan Africa and G20 Responses to the Global Financial Crisis: First, do no harm

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## **Sub-Saharan Africa and G20 Responses to the Global Financial Crisis: First, do no harm**

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### **Abstract:**

These days, plenty of cognoscenti in academia and politics share the common concern that the build-up of global macroeconomic imbalances threatens the international economy. While there is broad disagreement on the essence of what an imbalance exactly is, the term is generally associated with perceived macroeconomic disequilibria in balance of payments, but also fiscal and monetary policy. In the aftermath of the financial crisis the G20 leaders addressed these issues in the 'Seoul Action Plan' adopted in November 2010. The G20 emphasizes the need for domestic policies directed to increase savings in the deficit countries and to increase absorption in the surplus countries. In this paper we assess the G20's desire, mostly on paper, in the light of its implications for sub-Saharan Africa. We first review how sub-Saharan Africa was hit by the crisis and consider prevailing crisis responses. We then assess whether the G20 is on the right track and whether the G20 is the appropriate 'coordination' body to solve the dissonance problem of national economic policies. Subsequently possible implications for sub-Saharan Africa are presented. We conclude that there could be a potential positive impact of the 'Seoul Consensus' on Africa, if the rich countries really abstain from trade protection measures and currency wars.

## I. Introduction

Along with international capital flows come global macroeconomic imbalances, which have for many years raised concern in politics and in academic circles. Recently they are claimed to have destabilised the global economy when they peaked prior to the world-wide economic crisis. Implicitly, the imbalances are traced back to speculative behaviour from private actors and distortive measures from state actors in non-market economies such as China.

This seems to be only half of the truth, since there is good reason to assume that monetary policy in the US in combination with US housing subsidisation schemes encouraged 'clever' banks to securitise loans in order to sell the risks. At the same time, Western governments were not able to balance their budgets, which also contributed to the crisis.

This crisis not only hit the developed world, but also created huge problems and a recession in many developing countries, particularly in sub-Saharan Africa, which reformed their economies over several painful decades and had just started to reap the benefits of these reforms. Although the causes are rooted in the North, sub-Saharan Africa suffers from it. Therefore, it is worthwhile to analyse the attempts of the significant economies in the North but also key developing countries to solve their own problems, and the implications of these policy shifts for African economic development.

Our prism for doing so is the G20 Leaders' Forum. At their recent meeting in Seoul, the Group of 20 (G20) agreed on a 'Seoul Action Plan', which also addresses the problems of the poorest in the 'Seoul Consensus'. Both documents can be judged positively, as they take the right direction: freer trade, lower imbalances, fiscal stability, just to mention the main elements. Much emphasis is given to consensual cooperation and the avoidance of global economic conflict. It is fair to say that the G20 members in theory learned the lessons of history. However, it is also pretty obvious that the documents, as with any former G20, G7 or G8 agreements, lack an enforcement mechanism. It has to be seen to what extent the G20 can deliver.

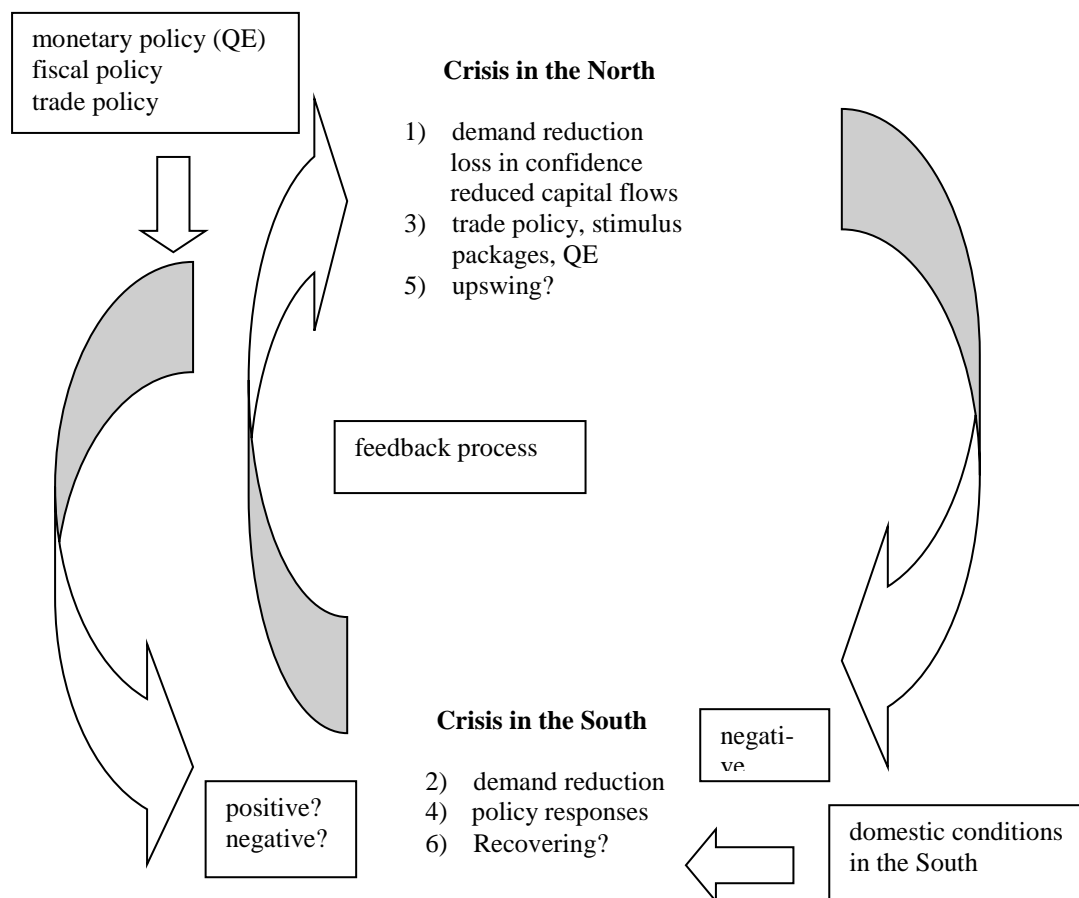
Nonetheless, the paper tries to establish the potential impacts of G20 'delivery' on the Sub-Saharan African economies. First, we discuss the impact of the crisis and the crisis fighting measures of the G20 on the economies of sub-Saharan Africa. One can identify a number of measures that affect the sub-continent negatively, particularly in the trade field. Next, we analyse the Seoul documents with respect to their message for Sub-Saharan Africa, focusing particularly on macroeconomic imbalances and associated responses. We end with some broader recommendations concerning the role of major emerging markets in re-

energising the trading system, and the need for more continuity in the G20's agenda through establishing a small, focused Secretariat.

## II. Sub-Saharan Africa and G20 Crisis Responses: A Catalogue

For quite some time, observers were sure that the global financial crisis beginning in late 2007 and culminating in 2008 was a northern phenomenon mainly. But in mid-2009 it turned out that the world economy's periphery was also hurt by the crisis although not as badly as the developed countries in the Organization for Economic Cooperation and Development (OECD). Nevertheless, the negative effects for the whole system exaggerated and developed a feedback process as shown in figure 1. The start of the crisis in the North reduced demand from that part of the world, capital flows also decreased. The consequence was a huge range of stimulus packages.

*Figure 1: Feedback processes of the global crisis.*



Source: own design.

These packages naturally are meant to regain confidence and stabilise expectations at home, thereby leading to rising demand and output again; examples are “cash for clunkers” programmes and huge increases in public investment. As an – often unintended – consequence of the direction, the packages had an explicit or implicit protectionist nature. This hurts the developing world twice. First, the demand reduction in the North diminished overall trade flows in all directions to a substantial degree, and second the subsequent boost to global demand was restricted to OECD countries.

To be fair, this is a global picture which does not necessarily apply across all African nations. The set of domestic policies and institutions are relevant for the degree to which a country suffered from the crisis and some countries were still well connected to the world and growing (see e.g. Figure 2).

## 1. Macroeconomics and Trade

Prior to the global economic crisis sub-Saharan Africa’s economic growth performance and macroeconomic fundamentals, as a whole, improved remarkably from the dark days of the 1980s and 1990s debt crises (IMF, 2010a). This was driven by two broad sets of factors: rapid economic growth propelled by first US, then Chinese demand for commodities; and continued policy reforms resulting in more sustainable macroeconomic profiles in a number of countries.

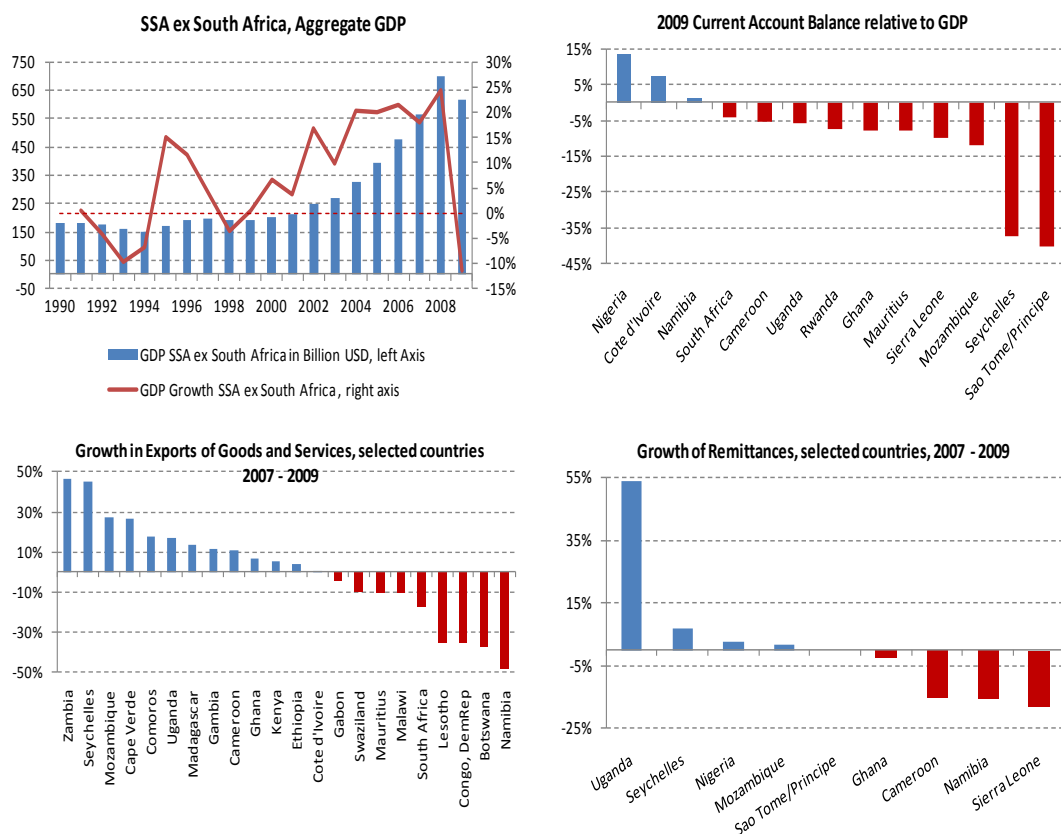
At a general level sub-Saharan Africa’s economic growth is closely linked to developed country, but increasingly emerging market – especially Chinese – economic growth (Reisen, 2010). The key transmission belt for this linkage is African commodity exports which are needed for various manufacturing processes undertaken in advanced countries and China. Consequently, as OECD and Chinese growth and exports took serious hits the initial impact of the crisis in Africa as a whole was felt in declining export volumes and commodities prices, with attendant impacts on current accounts and economic growth. Furthermore, tourism and remittance receipts, linked particularly to EU markets, suffered in many countries (IMF, 2010a; N’Zue, 2010).

Figure 2 shows selected details of these developments. On the top left, one can see the sharp decline of GDP growth in 2009. The top right graph illustrates that between 2007 and 2009 many countries in Sub-Saharan Africa, particularly those not exporting oil, ran current account deficits.<sup>1</sup> The growth of remittances (bottom right), an increasingly important source of external finance, has also

<sup>1</sup> This, however, is not a crisis specific feature. Many countries in sub-Saharan Africa had run current account deficits before, which is not surprising, given the scarcity of capital in Africa. Intertemporal capital theory suggests this pattern. See section 3 below.

been negative in some countries. The same holds for the development of goods and services exports (bottom left). Whilst these charts show mixed results, there cannot be any doubt that the sub-continent was hit by the crisis and the subsequent policy response. Although the data cannot disentangle what was caused by the crisis, what was due to the policy responses in developed countries and what was caused by domestic policy responses in these countries, a closer look at global policy conditions – the main focus of this paper – is justified.

*Figure 2: Past Developments of Economic Indicators.*



Source: Worldbank Development Indicators.

Before getting there it is important to note that many observers of African political economy were concerned that the global economic crisis would lead to African governments undoing the hard-won policy reforms of the 1980s and 1990s. Crisis response measures were implemented in a number of countries, along two broad fronts: stimulus packages, and budget revisions and/or targeted sectoral support measures designed to secure revenues. N'Zue (2010) argues that these were all crisis response measures but the list presented doesn't firmly establish whether these measures would have been implemented in the absence of the

crisis.<sup>2</sup> More importantly, the IMF argues that substantial policy reversals did not materialise (IMF, 2010a).

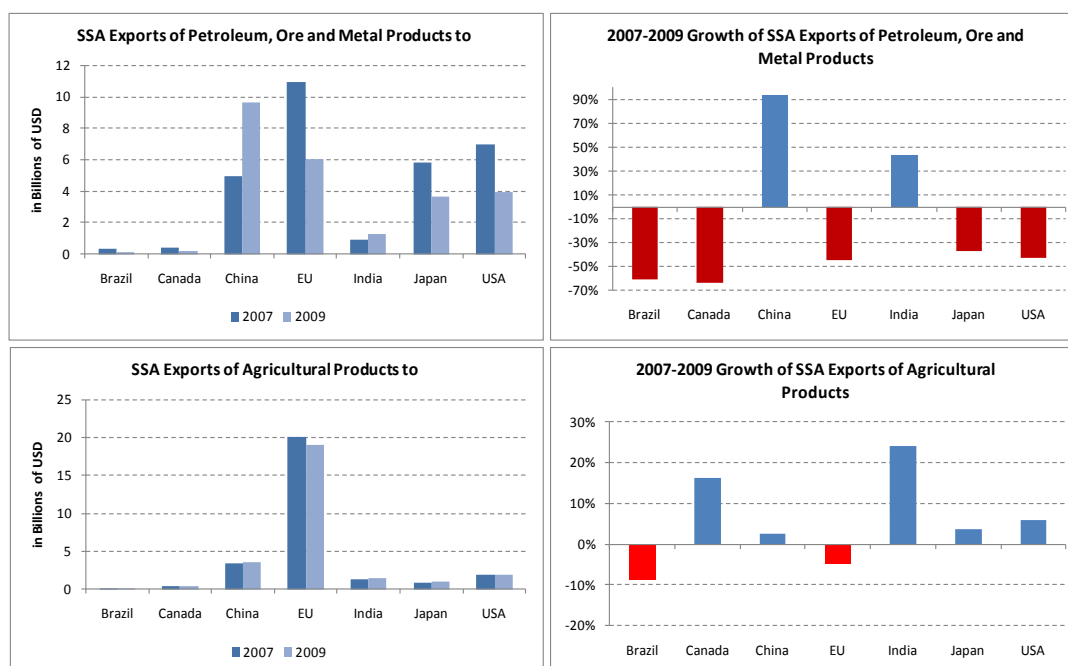
Recently growth rates in sub-Saharan countries have generally recovered, driven by Chinese growth in particular but also the uncertain recovery in the OECD, albeit not yet to pre-crisis levels (N’Zue, 2010). The interesting story is that stagnant growth in the OECD for the foreseeable future implies increasing reliance on emerging economies’ economic growth, especially Chinese but down the line India too. Figure 3 illustrates the development of exports of agricultural products and commodities from the Sub-Saharan region to the rest of the world. The figures impressively demonstrate the rising importance of China and India with respect to trade in commodities and thus future economic partnerships; exports of agricultural products on the other hand remain firmly tied to the EU with its complex agricultural trade policy system and preferential market access for African countries and other former colonies.

Hence the economic crisis has accelerated trends underway prior to it and along with that African hopes for diversifying traditional reliance on the West (UNCTAD, 2010; United Nations, 2010). In the medium term these dynamics are undoubtedly important, but in the short to medium term and for as long as fiscal positions in key OECD donor nations remain impaired and economic growth anaemic, African economic growth is likely to be somewhat diminished.

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<sup>2</sup> For example South Africa’s stimulus package is cited as a crisis response measure, whereas in fact the outlines of stimulus measures – almost entirely infrastructure expenditures – were in place at least a year prior to the crisis.

*Figure 3: Exports of Commodities and Agricultural Products.*



Source: Worldbank WITS Database, based on UN Comtrade figures.

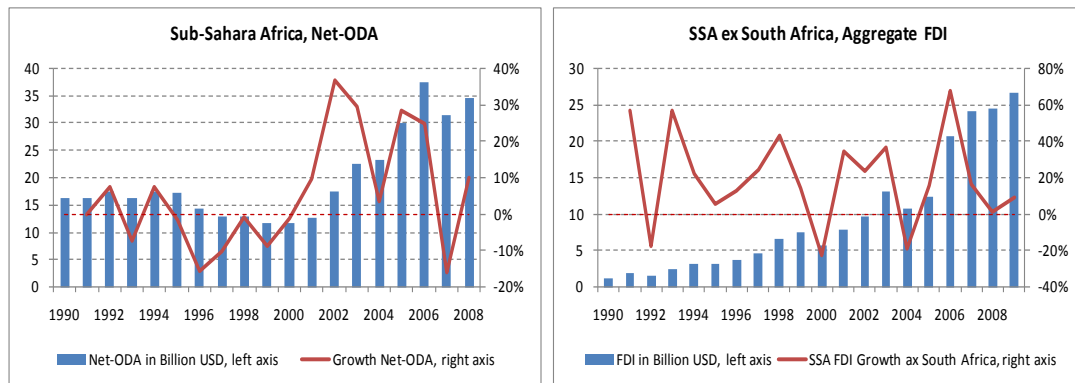
In the past sub-Saharan African countries have relied on official development assistance (ODA) to supplement meagre domestic fiscal resources and fund chronic current account deficits, but particularly in the years before the crisis, this reliance has diminished substantially in favour of sustained foreign domestic investment (FDI)<sup>3</sup> and remittance inflows. As can be seen from Figure 4, net ODA and aggregate FDI for Sub-Saharan Africa were still on record levels.<sup>4</sup>

<sup>3</sup> These are still concentrated in a relatively small group of countries, mostly oil exporters but including the most diversified economies: South Africa, Kenya, and Ghana.

<sup>4</sup> Unfortunately remittances are not reported by a large number of countries. An aggregation for Sub-Saharan Africa is therefore not possible. See also the selected countries and the chart inserted in figure 2.



Figure 4: Official Development Assistance and Foreign Direct Investments.



Source: Worldbank Development Indicators.

The challenge the sub-continent faces is that such inflows from the OECD countries are likely to be substantially curtailed for the foreseeable future. Therefore, raising domestic resources to fund huge development needs will remain challenging for many African countries. Hence the manner in which global macroeconomic imbalances are unwound, if at all, has major implications for many sub-Saharan African countries. We return to this in section 3.

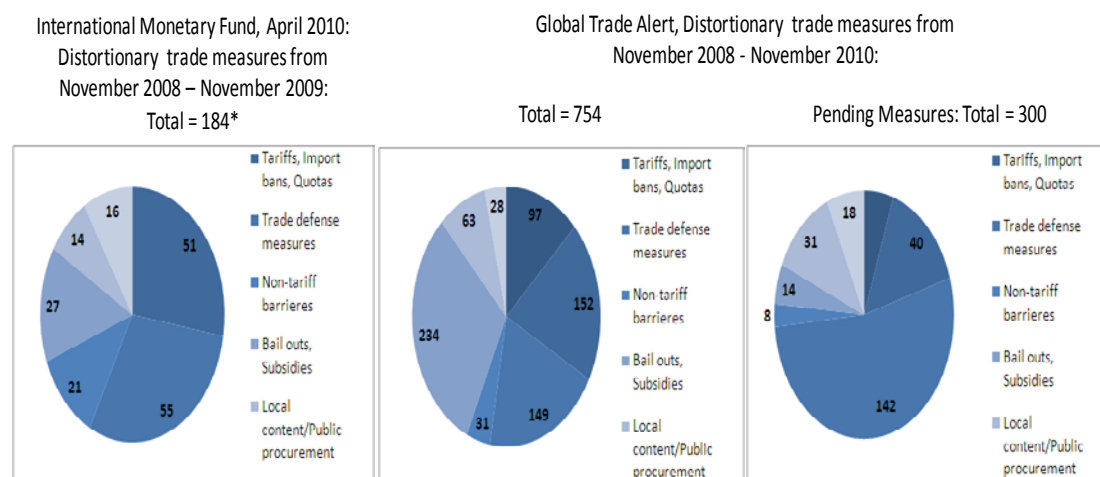
## 2. Trade Policy Issues

At the onset of the global financial crisis many observers were concerned that protectionist trade policy responses could result in a global trade war. Clearly the worst predictions have not come to pass, albeit there has been a substantial escalation in 'murky protectionism' (Baldwin and Evenett, 2009). Whilst the incidence of protectionist policy responses is contested, the direction and broad patterns are not. By and large developed countries have resorted to fiscal (subsidies; bail outs) and regulatory measures, whereas developing countries with their shallower pockets have resorted to tariff, including contingency (anti-dumping, countervailing, safeguard) measures (Evenett, 2010, 19).

Figure 5 gives an overview of distortionary trade measures. First, it illustrates the high number of trade related measures taken since the peak of the crisis. Evenett (2010, 19) states that the Global Trade Alert (GTA) Database now contains information on 1339 state measures that have been announced or implemented since 1 November 2008. These amount to an average of 30 measures per month. After the Canada G20 summit in June 2010, approximately 5 months ago, the GTA database added 288 new entries, an average of 55 measures per month. Secondly, the figure shows that there are differences with respect to the source of reported data. The official figures collected by the IMF are much

smaller than those collected by GTA. At the very least this points to the importance of reconciling measurement of the incidence of trade protection.

*Figure 5: Distortionary Trade Measures.*



Source: IMF 2010b, CEPR, 2010.

Ogunleye (2010) documents the contours of impact of African trading partners' protection measures on African trade and finds substantial incidence of harm (80 percent of total measures versus 20 percent that were liberalising). Not surprisingly these mostly affected the more diversified economies, particularly South Africa (80 measures) followed by Egypt, Tunisia, Morocco, and Kenya (56, 40, 33, 31 measures respectively). Ogunleye (2010, 40) also notes that a substantial portion of these measures are concentrated in the agricultural sector in which many African countries have a comparative advantage, and that the World Trade Organization's (WTO) rules specifically allow for developed countries to increase payments to their farmers in times of declining global prices, including export support payments. This points to the urgency of concluding the Doha round in order to further discipline the use of agricultural subsidies.

Yet the gaps in the WTO's regulatory regimes go much further than this, as evidenced by the wide array of crisis responses (Evenett and Hoekman, 2009). Specific problem areas from the standpoint of African countries include:

- Subsidies disciplines on finance, in light of huge bailouts to the financial sector. Whilst these were obviously necessary in order to prevent the wholesale collapse of the Western financial system, their continued implementation does raise questions about whether the recipients might use them to build market share in relatively rapidly growing emerging mar-

kets whilst restricting lending at home, thereby constituting unfair competition.

- Government procurement policies. As the 'Buy America' package and its various clones in other countries such as China demonstrated, this area is not well-regulated by WTO disciplines. Currently it is only covered under a plurilateral code mostly subscribed to by developed countries; non-signatories – which of course have chosen to exclude themselves from this code – can therefore find themselves shut out of lucrative procurement markets in the developed world in particular.
- Policies affecting movement of workers. Oguleye (2010, 44-45) notes that a number of European countries in particular tightened their immigration procedures, which in turn impacts on African skilled migrants with attendant consequences for remittances back home.
- Investment conditionalities, such as the French government prevailing on Total not to shut down its refinery at Dunkirk which in turn meant rationalization in another national jurisdiction, potentially Nigeria.

Consequently, even if the Doha round were to be (perhaps miraculously) completed, there is a large agenda arising from, and transcending, the economic crisis which could and should keep the WTO busy for years to come. Unfortunately the same geopolitical dynamics affecting the G20 have also been evident in the Doha round for some time, so the prospects for these issues being addressed are not high. At the very least this suggests a more focused agenda for the WTO in the future, together with reform of its decision-making dynamics (World Economic Forum, 2010; Draper, 2010b).

Turning to the continent itself, N'Zue (2010) argues that African crisis response measures often impacted directly on trade, particularly intra-regional trade. He notes further that the regional economic communities (RECs), with the exception of the East African Community (EAC) failed to develop intra-bloc responses or to coordinate the unilateral actions of their members. He is surely right to suggest that the RECs need to up their game, but this finding also proves that those RECs are often poorly designed in the first place and not rooted in regional political and economic realities (Draper, 2010a).

### 3. Financial Regulation

Gathering in Cape Town in June 2009, the cognoscenti of the World Economic Forum were much exercised with how the global economic crisis would impact on Africa. Their key finding: '...on average, most African countries were less

affected by the global recession than most countries in other regions due to the continent's isolated position in the world financial system' (World Economic Forum, 2009, 6). However, this didn't prevent the transmission of some serious macroeconomic consequences, particularly via the trade channel, as discussed above.

On the regulatory front, tightening capital requirements as required under the Basle 3 amendments and the extra steps likely to be required of those banks deemed 'too big to fail', could result in restricted flows of capital to emerging markets and Africa especially. Since these regulations will be phased in over a number of years they are best considered medium-term in their impact. They may also restrict the supply of capital within African countries as they will be obliged to impose stricter prudential requirements on their own financial sectors (Thomas, forthcoming).

Offsetting this potential negative trend is the fact that such prudential tightening would reinforce the good governance trend seen in substantial parts of the sub-continent, particularly concerning the financial sector. Thus potential declines in capital inflows via ODA, remittances, and FDI from OECD countries will oblige African countries to develop their own financial sectors and revenue mobilisation through taxation, through domestic efforts but also regionally. This will pressure those governments to enhance their domestic political legitimacy, thereby boosting democracy and reinforcing the good governance cycle (OECD, 2010). Furthermore, for the handful of African countries that are developing liquid capital markets<sup>5</sup> the OECD countries' increasing risk-appetite for emerging market assets could strengthen their financial sectors.

On the flip-side if there is a sustained and substantial increase in capital inflows into these economies that could have deleterious consequences in terms of currency appreciation and potential Dutch disease effects. However, these effects can be mitigated with appropriate structural reforms and supply side measures that channel investments into job creating and output increasing projects, thereby contributing to increasing and sustainable growth on the sub-continent. On balance, better global financial regulation that improves governance can be seen as advantageous for Sub-Saharan Africa.

#### 4. The 'Seoul Consensus' on Development

Finally, it is worth noting that the G20 is now attempting to address African problems through its working group on development, co-chaired by South Korea and South Africa. At the Seoul Summit this resulted in several commitments

<sup>5</sup> South Africa, Nigeria, Ghana, Kenya, Senegal, Gabon are all active in foreign bond markets for example (Rand Merchant Bank, 2010, 2).

to avoid further tensions (G20, 2010), among them the pledge to coordinate macroeconomic policies as well as a strong commitment to open markets and the acknowledgement that the Doha Round faces a small window of opportunity in 2011. They also developed the 'Seoul Consensus' on development. This consensus is based on six principles supporting an open market economy. These core underlying principles are useful and appropriate for Africa: economic growth is regarded as the foundation of development; one-size fits all policies are to be avoided; and the private sector is regarded as central to achieving the objectives. The 'Consensus' fills these principles with nine pillars, eight of which are being pursued in the Sherpa track whereas financial inclusion has been allocated to Finance Ministers. Under each pillar multi-year action plans are supposed to be elaborated. This agenda is clearly large, and some winnowing is required. Nonetheless, it seems to address the needs of African economies.

What does the 'Seoul Consensus' have to say about trade and macroeconomic policies? On the trade front it essentially rehearses well-known WTO debates on duty-free-quota-free market access for the least developed countries (LDCs) without recommending decisive action; recommits G20 countries to providing Aid for Trade finance; and pledges G20 support for regional economic integration efforts in Africa. On the macroeconomic front it advocates 'growth with resilience' through provision of social protection schemes; and ramping up domestic resource mobilisation and the facilitation of tax revenues in order to reduce reliance on ODA inflows. The pillars also acknowledge important microeconomic aspects, e.g. the necessity of access to capital markets for SMEs, the virtues of investment promotion and the need for knowledge building and transfer. On balance, the text is aware of the basic problems both in economics and policy.

However, as usual with 'G-something' declarations, the commitment is rather loose. It is worth mentioning that again there is no single pledge about a withdrawal from agricultural protection in the G20. There is only a commitment to food security. This may even have perverse incentives: in order to preserve food security, the rich Northern countries may feel the need to maintain overproduction so that they still can run food aid programmes. Such programs destroy incentives and market opportunities for domestic producers in developing countries, so that this pledge might prolong a vicious circle. Interestingly though, many African economies are hugely invested in the European system of agricultural protection by virtue of enjoying preferential access to the EU market at levels better than those enjoyed by other non least-developed countries (LDCs). Since the sub-continent contains 33 LDCs it is not surprising that the Africa group's positions on agriculture in the Doha round tend to favour retaining elements of the EU agricultural system.

### III. Macroeconomic and Trade Policies: Is the G20 on the Right Track?

The ‘Seoul Consensus’ is part of the ‘Leaders’ Declaration’ from November 11-12, 2010 (G 20, 2010). The latter’s fundament is the ‘Seoul Action Plan’, which advocates monetary and fiscal stability, trade openness, development, financial regulation and structural reforms. As mentioned earlier, the document is written in a very general form, so that everyone can agree; thus critical issues are avoided, albeit the general pledge seems in line with good economic and diplomatic reasoning. We focus next on the issue of global macroeconomic imbalances.

#### 1. Perceived Macroeconomic Imbalances

In economic terms imbalances are often used as a synonym for disequilibria in the balance of payments, particularly pertaining to the current account, but also domestic fiscal and monetary policy problems. In political debates the focus is particularly on current account deficits and associated currency alignments, with the emphasis often defaulting to the latter. These debates become quite emotional when a domestic trade balance is in deficit. They are generally driven by a strong mercantilist bias: trade surpluses are seen as a benefit to the country; policymakers and commentators usually praise the domestic economy and its international competitiveness. Trade deficits are seen as either a sign of weakness and thus characterized as economic disequilibria, or determined by foreign countries’ unfair practices. This leads logically to calls for appropriate political tools to manage such a ‘perceived imbalance’. Therefore, ‘deficit countries’ view exchange rate policy and protectionist measures as appropriate tools for combating trade deficits.

In order to avoid these protectionist policies coordination of macroeconomic policy is certainly justified. However, following the inter-temporal approach mentioned below, it is not justified to combat a perceived imbalance without an assessment of its causes, nature and how to cope with it.

With this in mind, a crucial passage of the ‘Seoul Action Plan’ is the following:

“...12. We have a shared responsibility. Members with sustained, significant external deficits pledge to undertake policies to support private savings and where appropriate undertake fiscal consolidation while maintaining open markets and strengthening export sectors. Members with sustained, significant external surpluses pledge to strengthen domestic sources of growth.” (G20, 2010, p.3)



To judge the document with respect to its potential success both within the G20 and in relation to sub-Saharan Africa, it is important to ascertain whether or not the G20 members interpret this paragraph equally in terms of modern intertemporal allocation theory (Obstfeld and Rogoff 1994). Such an interpretation does not express a prior normative judgement on a trade deficit or a trade surplus. It rather analyses the current account simultaneously with the capital account. Both balances are linked together as the difference between domestic savings and investment is equal to the difference of exports and imports (corrected for the change of foreign reserves and transfers). This identity always holds, but is important when it comes to analysis. According to this approach, the intertemporal decisions about saving and investment lead to capital flows, which then change the nominal and/or the real exchange rate causing trade flows to adjust. As a result, the current account changes. The normative judgement of the resulting imbalances depends on the sustainability of the capital flow. Economic agents from surplus countries that are investing in (deficit) countries accumulate debt contracts and carry out portfolio and foreign direct investments. Thus surplus countries generate returns through interest payments and claims on future profits. As a general rule, the following has gained general acceptance: if capital flows are invested properly, the imbalance seems unproblematic *ex ante*, if it is consumed the judgement is much more critical.<sup>6</sup>

Despite some impressive counter-examples, this theory is backed by much empirical evidence over the last centuries. As long as capital inflows are used in a sustainable way, i.e. for investment rather than consumption, the markets do not challenge macroeconomic policy. South Africa can be seen as one example: the growing trade deficit from 2003 was driven by rising investment. The investment climate in the country was and still is judged positively (Draper and Freytag 2008). Consequently, South Africa – although hit by the crisis – did not suffer a large reversal, rather the opposite could be observed: Net capital inflows were maintained even during the crisis. Even small countries can maintain imbalances for a while. For large countries this may hold even longer, in particular if they can borrow in their own currency, as the US example shows. One has to consider that the US trade deficit is driven by consumption to a much higher extent than South Africa's. This highlights the need for the US to continue reducing its current account deficit.

In this light the statement in the 'Seoul Action Plan' is remarkable as it seems to interpret imbalances not as disequilibria *per se*, rather it acknowledges that the saving-investment decisions taken individually and aggregated in countries may well lead to imbalances in equilibrium. In this interpretation, the global economy has moved away from equilibrium; a new equilibrium will be reached by different saving-investment decisions in several key countries. Deficit countries

<sup>6</sup> See Draper and Freytag (2008) for a short literature review as well as Corden (2007).

must increase their savings while surplus countries raise their investment and consumption. Looking at the current cases (US as deficit country, China and Germany as surplus countries), this is reasonable. Even after the adjustment, imbalances may well exist. In addition, trade protection is not an accepted tool in this context, as acknowledged by the plan.

The issue of imbalances is crucial for the success of the 'Seoul Action Plan' and consequently for the 'Seoul Consensus'. The main question here is whether the very ambitious document is really mirrored by both the commitment and ability of governments to deliver a global coordination of policies, or whether the implicit prisoners' dilemma of democratic governments in the sphere of vested domestic interests is overwhelming. This raises the very real problem of policy dissonance, or a large gap (an imbalance if you will) between official statements and real intentions and actions.

## 2. Policy Dissonance

Judging from the G20 members recent rhetoric regarding imbalances, it seems that at least the big G20 members still take a pure mercantilist perspective which regards trade surpluses as good and trade deficits as bad. The political reactions are according to this logic, as the following three examples show.

- The United States' (US) government accuses the Chinese government of fostering a trade surplus with the help of an undervalued currency, totally neglecting the problems a country buys when pursuing a competitive devaluation (Freytag, 2008): inflation increases in the long run and relevant imports become increasingly expensive. At the same time, the economy sells its value added for too low a price. Apart from that, the degree of undervaluation is still subject to discussion; some observers even question its existence whereas others dispute the size.
- The Chinese government accompanied by Western governments and a number of emerging powers in the G20 such as Brazil and South Africa accused the US of too loose monetary policy and consequent competitive devaluation when the Federal Reserve announced its latest USD 600 billion quantitative easing plan (QE2). Growing concerns over potential deflation in the US were ignored in these public statements.
- The French government accuses the Germans of under-pricing their exports with low wages. This shows an interesting neglect of theory and facts: first the wage level in Germany is not low, but productivity growth was relatively high in the past (reducing unit labour cost). This is an im-



portant measure to combat mass unemployment. Second, being strong in exports does not automatically mean importing less. The trade balance follows inter-temporal logic, i.e. it is driven by savings and investment decisions. In this regard, the Germans save more than they invest at home, which is indeed a problem for Germany, particularly the Eastern part, in the presence of mass unemployment.

Read such, the controversies follow an old pattern and don't allow a solution as suggested in the quote from the 'Seoul Action Plan'. It seems, however, that too much pessimism is also exaggerated. The problem of course is not one of intellectual capabilities (as the quote clearly shows). The inter-temporal logic is not very difficult to grasp and probably well-known to the policymakers (and at least to their advisors) involved. The question of interest is of political economy nature. Can the governments draw benefits from applying the inter-temporal logic to their problems, or is it politically easier to choose other options, at least rhetorically? In the current state of the debate, it is reasonable to assume the latter. The crisis has brought to light domestic – distributional – conflicts and also encouraged nationalistic impulses, both of which increase the need for scapegoats. In democratic societies, the tendency to give in to short-term needs and solve distributional conflicts at the expense of later generations rather than considering the longer run is notorious. The belligerent undertones may also reflect the (perceived) need of governments to build up a position for the negotiations. There is a different calculus at work in China, where huge political capital is invested in that country's export-driven growth model and policy calculations are much longer-term in nature. This political time dissonance is also a critical element in the broader recourse to protectionist rhetoric.

### 3. Can the G20 Solve the Dissonance Problem?

Next we discuss the question of how likely success of the 'Seoul Action Plan' is. To be sure, the suggestions made in the plan are sensible, as our three examples show: there can be no doubt that it would serve the long-term interest of the United States to increase savings and reduce the fiscal deficit. Similarly, the Chinese economy and population would surely benefit from higher domestic consumption. Consequently savings could be lower and the domestic capital market could develop further. Finally, more domestic investment and consumption would help Germany to further reduce unemployment. Similarly, measures along these lines also would positively affect the global economic and political climate. Thereby the G20 members would facilitate development in sub-Saharan Africa and other underdeveloped regions.

So, one wonders about the difficulties of the respective governments to solve their domestic macroeconomic problems unilaterally. At the same time, the fi-

financial regulation issue is a multilateral one and requires coordination and more efforts to understand the problems. It also requires that countries give up their egoistic and – again – short-term oriented attitudes to avoid strict regulation in order to attract business. So it can only be speculated and has to be awaited how binding the ‘Seoul Action Plan’ will be for the G20 members and what the realised detailed outcomes will be.

However, policy dissonance will occur as long national policymakers are not aware of the potential gains from cooperation. The IMF’s Mutual Assessment Process (MAP)<sup>7</sup> can help to answer the question of potential welfare gains. The technical expertise the IMF offers might thus be a necessary tool to push individual countries to cooperate. To impose sanctions on non-contributors is not the best idea as one could have learned from the recent European Monetary Union (EMU) debt crisis.<sup>8</sup> Therefore, peer review is needed to create the economic incentives to cooperate. To achieve international acceptance of policy recommendations it is also necessary for the IMF to be inclusive for all G20 members, a fact the G20 leaders have acknowledged as reflected in ongoing efforts to reform the IMF.

We would recommend following the general thrust of the plan with respect to unilateral macroeconomic policy actions fitting within the sensible framework proffered. Furthermore, the G20 must really start energising the Doha round; take fiscal stabilisation seriously; ensure that exchange rates float rather than being subject to political deals or conflicts; and ensure that quantitative easing stops eventually (with central banks’ attempts to reduce liquidity).

#### 4. Implications for Sub-Saharan Africa

There are essentially two scenarios for sub-Saharan Africa arising from the policy dissonance problem amongst the G20’s major players. First, the latter could pursue a mercantilist course. This would lead to a series of negative consequences including, *inter alia*:

<sup>7</sup> The IMF provides the technical analysis needed to evaluate how members’ policies fit together and whether, collectively, they can achieve the G-20’s goals. See IMF, 2010c for the recent IMF staff assessment of G20 policies.

<sup>8</sup> In the EMU 22 excessive deficit procedures have been initiated by the EU Commission so far. None of these treatments ended in an imposition of sanctions on EMU member states that had consistent excessive budgetary deficits. The mute acceptance of individual violations of the Stability and Growth Pact (SGP) by all other EMU member states and the limited institutional power of the EU Commission caused this kind of non-cooperation to arise. At the end of September 2010, the EU Commission presented new proposals for a more rules-based SGP, dealing with sanctions, fiscal monitoring and reporting, and broader economic surveillance (view, for example, European Commission (2010) and Featherstone (2010). However, as Wyplosz (2010) argues, the SGP can only work when institutional reforms are implemented – if possible at the European level (i.e. a new treaty), or at the national level (i.e. changes in national fiscal policy institutions).

- The US intensifies ‘competitive devaluation’ via QE2, leading to an associated exit of capital flooding into emerging markets, creating new bubbles which might pop at some point in the future. Since economic growth in the OECD countries is likely to remain depressed for some time, the potential coincidence of emerging market recessions with OECD stagnation should alarm policy makers.
- China continues with its current growth model, including an undervalued currency. Whilst Chinese growth is good for African exports and growth (Reisen, 2010), the currency undervaluation constrains African diversification opportunities at the same time as it impels African countries to embrace the structural reforms needed to attract manufacturing FDI in particular.
- Germany’s role within the EU may, according to some influential commentators, lead ultimately to the demise of the common monetary area (Wolff, 2010), or at the least deflation in peripheral economies in the Eurozone with attendant implications for economic growth in Europe. Since African economies are still firmly locked into the European growth orbit, they have a strong stake in how this drama unfolds.

Second, if the actions implied by the Seoul Action Plan were actually taken then whilst the short-term problems would remain in place, in the medium term pressure on the trade front should diminish as the global economy. Furthermore, if this was combined with a serious and successful push to conclude the Doha Round, and expand the purview of the WTO into those areas of interest to African economies not covered by current disciplines (see 2.2) then the G20 would make a very important contribution to leading the world out of the very choppy waters it finds itself in, and by extension would do African economies a great service.

Third, Africa can do something itself. The Chinese demand for commodities have stimulated a European reaction. Africa longer is no Europe’s backyard, but has increased its importance as partner for Europe and other continents. It should play this card consciously. An offensive initiative to complete the Doha Round can help to serve its interest much better than demanding special treatment and more ODA (Draper and Dube, 2011). A process of new thinking would not only help Africa, but also other countries.

Finally, is a general concern that African policymakers do not anticipate how international policy reforms may affect their economies. Naumann (2010), for

instance, states that some African countries do not appear to be actively following international policy debates and thus do not understand how international policy changes affect local producers and exporters. Consequently African policymakers are for the most part not actively engaged in recording their concerns. For sub-Saharan African countries technical knowledge and policy ownership is an essential precondition for successful negotiations at the international level.

#### IV. Broader Issues

Even more important than the normative policy recommendations, which are well-known and widely accepted, the political dimension is relevant. In many countries and regions, the crisis has become a political issue; this holds definitely for the Euro-crisis in Fall 2010. So – being aware of the political economy of the crisis – the G20 should rather take measures to avoid international conflicts, which have their basis in domestic or regional conflicts. It seems obvious that not all members are equally well prepared to be forerunners.

Our main argument here is that as things currently stand the Western – old – industrialised economies are not in a position to take the lead in initiatives to strengthen economic policy rationality on a global scale. Imagine the US administration offering agricultural market opening (which the US needs as urgently as the EU) in a global trade round – it seems impossible currently. The same logic applies to the European Union: who in France would dare to suggest a cut in subsidies for French farmers? Unlikely in normal times, political suicide in crisis times! So what is needed is a credible initiative by new players. The G20 is indeed a platform where the economically and politically (e.g. in the IMF) strengthened emerging markets should take more responsibility.

Therefore, it seems reasonable that the emerging economies start a new initiative for the conclusion of the Doha Round (Freytag and Voll, 2009). This initiative could be based on the ‘Seoul Action Plan’. Thus, it would not even be a surprise, as the ‘Plan’ indeed proposes the conclusion of the Doha Round in 2011. Of course, such an initiative requires political stamina and coordination within the group of emerging economies. The challenge remains that these countries still face significant domestic developmental challenges, and are probably not yet ready to step up to the plate with the kinds of ‘sacrifices’ that such international leadership requires. Nevertheless, the political signal of a balanced proposal from the organised ‘South’ would surely be strong. As noted in sections 2.1 and 2.2 there is much African could gain from a successful conclusion to the Doha round, not least in agriculture (see also Draper and Dube, 2011). Despite their attachment to the European Union, the African nations would benefit from

general reduction of trade barriers: in particular, the potential productivity growth due to increasing import competition must not be underestimated.

Such an approach needs to be supplemented with a concerted effort to establish the true incidence of protectionism given the divergences between the official figures collected by multilateral bodies and those put forward by the respected GTA. This would reinforce the obvious point that the multilateral trading rules exhibit major gaps. Consequently, when the Doha round is completed, the G20 should develop a more focused future agenda for the WTO including reform of its decision-making dynamics.

Finally, it may be useful to consider a renewed organisational form for the G20 – maybe a small secretariat is better to push a constant agenda. It may also provide a solid support structure for the host country, which can draw upon an institutional memory and providing expert advice. Against it stands the fear that it creates a new bureaucracy. One can imagine a middle road (Rhee, 2010, 8): a small secretariat works closely with the current and future host country. Such a regime would support continuity, relieve the host country from defining an over-ambitious agenda, and increase institutional knowledge. Since the major emerging markets are still learning the G20 ropes and suffer from capacity constraints, this would support our proposal for their greater involvement in initiating policies rather than simply reacting to northern proposals. The French government has proposed such a change (Rhee, 2010, 7), however, the chances to realise it can be regarded as negligible. The history of the GATT-secretariat shows that small steps well lead to success. Although we do not think that the proposal is very likely to be realised soon it may well be worth considering it seriously.

## V. Concluding Remarks

There is wide agreement that the extent of current global imbalances is not healthy for the global economy. However, it is even clearer that neither trade protection nor conflict over exchange rates will solve the problems. In this regard the G20 has clearly pointed to the right direction to bring the world economy back on track. Domestic policy measures directed to increase savings in the deficit countries and to increase absorption in the surplus countries respectively, coordinated to the extent it is politically possible, implemented in combination with maintaining open markets are best suited to do the job. The recommendation to conclude the Doha Round can only be emphasized.

Whilst these measures would be beneficial for the industrialised countries themselves, they would also help African economies. Further integration of Africa

into the world economy, continued international inflow of capital into the continent and the absence of international currency conflicts are essential for the continent to proceed on its healthy reform path of the last two decades. The paper has shown the potential positive impact of the 'Seoul Consensus' on Africa, if the rich countries really abstain from trade protection measures and currency wars.

With the US being weakened, Europe being fully concentrated on solving its fiscal problems, and China neither willing nor able to lead the world into better times on its own, Africa can play a role in the recovery process. Given its enormous interest in a healthy and thriving global economy and its high stakes in international trade, it should take a bold initiative to enhance division of labour on the global scale, for example by suggesting detailed steps to conclude the Doha Round. It is in the interest of developed countries to react positively to initiatives from the South; after all they are scarcely in a position to provide global leadership at this critical juncture in the evolution of the global political economy.

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