

## **Financing Africa's Development**

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What emerged from this morning's discussions is that we need to take a comprehensive, long-term view if we are to support development and reform. The conviction that aid is not the only answer was reinforced. Permanent solutions can only come from within African countries themselves; with help from outside, yes, but based upon their own resources and their own initiative.

OECD countries, when looking at developing countries and at African ones in particular, have a tendency to neglect the private sector. This is strange for economies that are all committed to the market economy. When they do consider the private sector, it is often in terms of the large companies, many of which have their roots in the OECD zone and invest in Africa.

Yet, in our own OECD-country histories, we have seen that growth and redistribution, job creation and household wealth, have come from smaller, indigenous enterprises, a climate favouring entrepreneurship and a vibrant private sector. The whole point of the market economy is to provide space for private and individual initiative.

Small enterprises are the seeds of the private sector, itself the source of innovation and diversification. They supply larger companies and develop their own activities and product lines. When they grow, they provide employment and tax revenues. Small and medium-sized enterprises can be the motors of economic growth. In most African countries, however, the business environment is not conducive to enterprise development.

Initiatives in the past to support smaller enterprises in developing countries have largely failed. Why? Often, they were unsuccessful because they sought to replace existing structures and institutions, or to compete with them, rather than reforming and building upon what had already existed. Entrepreneurs do know their environments; what they need is to be able to operate within them.

As the AEO stipulates, this requires long-lasting commitment and a true partnership between African governments, financial institutions, the private sector and the international development community.

What can be done?

- African countries should develop their own country-owned strategies for private sector development with a special emphasis on SMEs servicing the local and export markets. The tone should be given at the top emphasizing the commitment of leaders through pro-active policies to engage the private sector in their national development strategies for growth and poverty reduction.
- Governments should engage private sector participants in an ongoing dialogue so as to build the necessary trust and domestic partnerships between all development stakeholders leading to tangible and mutually beneficial policy outcomes. In designing their comprehensive strategies for private sector development, domestic leaders should create the necessary mechanisms and institutional platforms for mobilising the informal rural sector, the local SMEs, the export-import firms and the larger multinational actors.

- Strategies for private-sector development should be comprehensive and country-focused. The central objective should be to facilitate wealth creation and productive restructuring through the provision of appropriate incentives for enterprises to move from the informal to the formal sector, the development of clusters of productive activities and the creation of sustainable and competitive value chains. Agricultural development and export diversification should be given top priority.
- African institutions – the courts, the regulatory environment, private property rights – need to be reformed. African businesses need better access to training and information; they need to be better able to enter the formal sphere.
- The time needed to establish a business, or to dissolve one, added to the complexity of the process and the bureaucracy represent so many obstacles to local initiative and entry to the formal sector. So daunting is the task, indeed, that many small entrepreneurs simply decide to stay outside the formal system. The result: lack of protection for employees and owners; lack of collateral for financing in the formal sector; general insecurity; and loss of tax revenue for the government. Outside the formal system, small firms may also be more likely to indulge in corruption in order to overcome obstacles linked to their informal status.
- Special attention should be given to strengthening SME activities through the development of a selective set of competitive clusters. Cluster formation involves building horizontal and vertical linkages among entrepreneurial units either in the same or complementary economic activities so as to reduce operating costs, create economies of scale and increase competitiveness. Cluster formation could be underpinned by complementary investments in infrastructure, training, skill formation, capacity building and networking as well as appropriate regulatory reforms (reduction of administrative burden for business start-ups, quality standardization, etc) and suitable and cost-effective financing schemes and incentives.
- To assist SME development, priority should be given to financial reforms and appropriate financing. *Effective financing of SMEs* – this year’s focus theme - should include regulatory reform, the creation of a friendly business environment for doing business, the extension of guarantees to local banks to entice them to lend in local currency (e.g. USAID Development Credit Program), tax incentives for rewarding companies that agree to have their financial statements audited, the creation of equity funds suitable for SMEs, financial incentives for partnerships, etc.
- The banking systems in Africa, with some exceptions, are not adapted to lending to small enterprises. Making financing more flexible would help. The non-banking financial sector also has a job to do here. The state can help; donors as well.
- *Capacity building* in both the public and private sectors can be promoted through development assistance to enhance administrative capacities, skill formation and the extension of business services. Country-needs programmes should be resurrected to provide a diagnosis and assessment of national priorities.

Much has been said and written about the NEPAD and its private-sector friendly infrastructure projects. It is clear that the continent requires Africa-wide schemes to improve transport and communications generally, as well as provision of energy supplies. At the same time, however, the local situation is what directly affects small businesses and limits their growth. Large infrastructure projects on a regional or continental basis take time to be completed, but private businesses need services now. This is where national policies can complement NEPAD programmes.

This might well be an appropriate moment, with growth figures on the rise, to take a new look at what can be done to create a business-friendly environment in African countries.

The African Economic Outlook has attempted to tackle some of these issues in its 2005 edition and, simply by raising the dilemma of the “missing middle” - the virtual absence of

SMEs between the informal sector and the multinationals or state enterprises - has opened the way at least to part of the solution for obtaining sustained growth in Africa.

Pierre Ewencyk, the coordinator of this year's African Economic Outlook, will tell us more about this in a few moments in his introduction.

Let me conclude by saying how fortunate we are to have with us some outstanding guests with extensive experience of confronting these challenges, and with some very complementary points of view:

- Aicha Ennaifa, Tunisia's Director of Industrial Strategies, will talk of his country's successful experience of promoting the development of SMEs;
- Pierre Jacquet, Executive Director of AFD, the French development agency, that lends support to enterprises development in Africa and beyond;
- Paul Derreumaux, President of a successful, independent, African private banking group operating throughout the continent;
- Elizabeth Littlefield, CEO of a consortium of donors aiming to supply high quality microfinance services to the poor; and
- Martin Abega, who represents a professional group of dynamic entrepreneurs in Cameroon.

On behalf of the Development Centre and the African Development Bank, I welcome them and you all to this session. I would also like to remind you that we will have the honour during the closing session to hear from OECD Secretary General Donald Johnston and from Brigitte Girardin, Minister for Co-operation, Development and the French-speaking Community.