

**A STATEMENT BY MR. FUDZAI PAMACHECHE OF THE AFRICAN UNION
COMMISSION DELIVERED AT THE MEETING ON CAPITAL FLOWS AND
DEVELOPMENT OF AFRICAN ECONOMIES: TOWARDS AN ACTION PLAN
FOR INVESTMENT IN AFRICA**

ZANZIBAR, UNITED REPUBLIC OF TANZANIA

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Chairperson,
Colleagues,
Ladies and Gentlemen,

I wish thank the ECA for organizing this important workshop and for giving me the opportunity to say a few words on behalf of the Commission of the African Union.

Despite improvements in macroeconomic stability in many African countries, they continue to face a perennial shortage of public and private investment, which constrains their ability to accelerate growth. The New Partnership for Africa's Development (NEPAD) programmes recognizes the critical importance of filling the resources gap that exists in Africa. This resource gap could be filled by enhancing domestic resource mobilization, through improved public revenue collection and increases in domestic savings with the bulk coming from external flows, in particular debt relief, overseas development assistance (ODA), increase in trade or market access and private direct foreign investments (FDI). The market access component emphasizes the diversification of production, the promotion of the role of the private sector, export led growth and removal of trade barriers to intra-Africa and international trade. The NEPAD document 2001-10 identified the resource gap required annually to stimulate sustained growth that would have a positive impact on poverty reduction to be about 12% of GDP or US\$ 64 billion while the World Bank estimate in 2005 put this requirement at \$76 billion.

In looking at capital flows, one is more concerned with the movement of capital within and without the economy. Capital flows within an economy refer to domestic resource mobilization through savings and channeling those savings into investment. The level of savings determines the level of domestic investment. Domestic resource mobilization and in particular high levels of long-term investment is key to achieving sustained economic growth that has the capacity to have a positive impact on poverty reduction. The other side of capital flows

relates to capital flowing into an economy from outside. The key components of capital flows from outside include development assistance or aid, foreign direct investment (FDI) and workers' remittances.

According to the ECA Report on Capital Flows and Development financing in Africa, the trends indicate that since 2000 capital flows in the form of aid, workers' remittances and FDI have increased considerably by about 54% between 2000 and 2003. Aid is the main inflow into Africa and has for long been targeted for social services such as health and education. In 2003 aid was the largest component accounting for 46% of total inflows, followed by workers' remittances at 30% and FDI at 24%.

The continent has also experienced substantial resource outflows in the form of debt service payment, profit remittances by FDI and capital flight. Debt service remains the main source of capital outflows from Africa. For example in 1986 the debt service payments were higher than ODA, workers remittances and FDI combined. While this scenario has changed for the rest of Africa, for a number of countries this is still a major obstacle to development. Debt reduction efforts have to ensure that the resources freed are used to boost productive activities to make debt levels sustainable.

Capital inflows in Africa particularly FDI has tended to concentrate on extractive industry which is highly capital intensive and does not generate many jobs. There has been substantial investment in the oil, petroleum and gas as well as mining industries. Due to lack investment into higher value products, Africa continues to export unprocessed commodities whose prices are determined at the whims of the developed markets. The impact of this is evident in African countries where crude oil is exported to foreign markets and refined oils exported to those same countries thus exposing them to the same problems as encountered by non-oil producing countries. The same is true of countries exporting raw materials such

as cocoa or coffee beans. Concerted efforts at investing in higher value chain are required to address this anomaly.

The aid component of inflows has largely benefited the social sectors, which should be supported by a strong productive sector. Unfortunately very little investment goes into the productive sector. In as much as this strategy is contributing to the alleviation of poverty on the continent, greater emphasis should be put on developing the productive sector that will yield even better results given its impact on job creation, sustained growth and subsequently poverty reduction.

Africa is not getting a fair share of foreign investment and this inevitably keeps the continent in a vicious circle of low growth and increasing poverty. To break this and move into a virtuous circle, there is need for a big push in investment both domestic and foreign so that they reinforce each other. Attracting the latter, in particular requires efforts at both national and continental level to rid Africa of its image of a “high cost” place for doing business. In recent years we have seen countries making efforts to deal with this problem or perception by improving macroeconomic management, simplifying business registration procedures, providing aftercare services and introducing incentives.

At the level of the AU, efforts are underway to reinforce continental resource mobilization through the establishment of an investment bank to compliment the ADB. The AU Commission is also in the process of commissioning studies on the development of common investment strategy for Africa and the promotion of the development of micro finance as a major tool for mobilizing domestic resources for investment by the vulnerable groups. It is hoped that this will identify bottlenecks to investment and resource mobilization with a view to adequately address them and improve investment flows.

Well- developed markets and institutions facilitate the exchange of goods and services, the mobilization of resources, and their efficient allocation to profitable investment projects, and diversification of risk. The development of the financial sector has direct bearing on the growth of the economy in any country as the ability of the financial sector to provide investment finance as well as working capital is a prerequisite to enhancing the capability of the productive sectors to produce and create wealth. Export led growth policies coupled with emphasis on diversification of production, increase in productive capacities and aiming for higher value added exports would enhance economic growth and development.

It is also critical that capital markets are developed, integrated and deepened to make them more sustainable and competitive and support investment growth in Africa. It goes without saying that there is need for improved economic management in particular debt management, exchange rate and price stability and better investment incentives applying to both domestic and foreign investors.

While we are able to talk about capital flows in generalities, it is vitally important that there is adequate data that is readily available. So far the data that we have on debt for example is not from the countries themselves but from the World Bank or the lenders. This lack of accurate information compromises our negotiating power for further debt relief. The key challenge is what can we do to reverse the net outflow of capital from Africa? What incentives can we give to FDI so that more of the profits remittances are retained as investment capital?

When one talks of workers remittances, that data is overly understated due to many factors including remittances not going through official channels and this is prevalent in countries where the exchange rate is not properly aligned. The area of data may need to be examined to see what can be done to improve the situation. The meeting may want to look at the need for building capacities both human and institutional in order to monitor capital flows. There is also need to discuss the question of legal and regulatory framework as well as monitoring

and surveillance systems for capital flight, which can be devastating in an economy.

I look forward to fruitful discussions and recommendations on how Africa can best mobilize resources to finance its development.

I thank you for your kind attention.