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Innovative Policy Measures and Practical Steps for Mobilizing Domestic Resources to Achieve
Development Effectiveness in Africa

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Your Excellency, Ato Meles Zenawi, Prime Minister of the Federal Democratic Republic of Ethiopia

Your Excellencies, Heads of State and Government

Your Excellency, Dr. Jean Ping, Chairperson of the African Union Commission

Honourable Ministers

Distinguished Delegates, Ladies and Gentlemen

It is an honour and pleasure to have the opportunity to address this distinguished gathering on the important topic of Innovative Policy Measures and Practical Steps for Mobilizing Domestic Resources to Achieve Development Effectiveness in Africa.

Development finance has been identified since the early post-independence era as a binding constraint on growth and development efforts in Africa. It was therefore fitting that the NEPAD programme put this matter back on the front burner by making resource mobilization one of its three pillars. It is therefore encouraging that the HOSGC is taking a closer look at domestic resource mobilisation which represents the best spirit of self-reliance that NEPAD embodies.

Indeed, you will be pleased to know that this topic has recently received more direct attention including at the AU ECA Conference of Ministers of Finance, Planning and Economic Development in 2009 and the recently concluded Forum on Financing Development held in Addis Ababa in May 2011.

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There are several dimensions to mobilizing domestic resources in an innovative way but before I turn to the four areas on which I will focus my remarks let me first of all answer the question of whether, in view of wide-spread poverty, there are, indeed, any domestic resources available in Africa waiting to be mobilized. The short and direct answer is yes. The extent of pension fund holding in Africa is evidence enough of this just as the huge sales of telecommunications companies and the over-subscription of government bonds floated at home are other pointers to the scale of untapped resources.

Bearing this in mind, I think that there are four key areas that we could focus on, namely mobilizing public finance, managing natural resource revenues, tackling illicit capital flows and exploring domestic options for new and innovative development financing.

Mobilizing public finance—strengthening tax systems and the private sector

In a 50-country study, ECA and its partners found that tax revenues in Africa have been on the rise with average tax revenue as a share of GDP increasing since the early 1990s. However, this positive trend has been mostly driven by resource-related tax revenues that divert attention from more politically demanding approaches like corporate income taxes, personal income taxes, Value Added Taxes (VAT) and excise taxes. Indeed, the evidence shows that countries without large natural resource endowments have been more effective in collecting taxes and in improving the quality and balance of their tax mix.

There are typically three types of challenges that our countries face with respect to further mobilisation of public resources which need to be addressed. These relate to:

- Cross-cutting structural bottlenecks, including high levels of informality, a lack of fiscal legitimacy and huge administrative capacity constraints.**
- Erosion of the already shallow tax-base by excessive granting of tax preferences and inefficient taxation of extractive activities.**
- An unbalanced tax mix that relies excessively on a narrow set of taxes to generate revenues.**

The required policy response would be to undertake tax reforms linked to growth while instituting good governance, transparency and accountability. It would also be essential to deepen the tax base, sequence trade and tax reforms and continue efforts to developing the private sector.

Managing Natural Resource Revenues

As more African countries discover natural resources, including petroleum, there is need to pay closer attention to the management of

these resources for development effectiveness. I wish to highlight four areas for attention in this regard.

- Our countries need to formulate inclusive, balanced and country-owned national development strategies that are aligned to the African Mining Vision with a view to using natural resources as a catalyst for inclusive and sustainable growth and development.
- Proper governance systems must be in place to ensure that Africa's people receive the best deal for their resources over the long term. This would require accountability throughout the value chain starting from the contracting phase, right through revenue collection to spending the proceeds from natural resources.
- The domestic economy should be enabled to benefit from the extractive sector by promoting forward and backward linkages and minimizing negative spillovers from the natural resource sector to the rest of the economy in order to promote diversification and employment.
- Increasing accession to and implementation of the African Peer Review Mechanism and the Extractive Industry Transparency Initiative principles.

Tackling Illicit Capital Flows

It is conservatively estimated that the total illicit financial outflows from Africa between 1970 and 2008 amounted to \$854 billion and may be as high as \$1.8 trillion overall. According to the Global Financial Integrity Report, 60-65% of this is commercial money, which is worrisome because and estimated 60 per cent of world trade now is taking place within, rather than between, multinational corporations.

The implications of this are that African countries are deprived of badly needed resources for undertaking development as annual figures can reach US\$160bn a year, which is a much higher figure than what is required in meet the MDGs.

Policy action will therefore be required to stem the outflow of such resources by tackling mechanisms used such as:

- falsified invoicing; inflating or undervaluing prices to increase costs and diminish tax liability

- **round-tripping whereby businesses operating in a country send their money offshore and bring it back disguised as foreign investment to get preferential tax treatment**
- **transfer (mis)pricing - against “arms-length” open market pricing, parent companies sell to each other at inflated prices; inflating costs in intra-corporate financial transactions (especially prices for “intangibles”)**

Tackling these issues is important and would require tightening legal loopholes and harmonizing tax policy at the regional and continental levels to avoid a ‘race to the bottom’ tax competition. It will also require enhancing transparency in investment contracting and scrutiny of oversight institutions.

The international community must also be called upon to do its part by improving transparency in the business dealings, better regulating tax havens, addressing issues of money laundering and establishing multilateral agreements to expand and deepen tax information exchange.

New and Innovation Forms of Domestic Resource Mobilization

The final topic that I wish to address on this occasion relates to the domestic application of new and innovative forms of finance. In other words, to the extent possible, we need to explore how best to raise additional resources at the domestic level in such areas. While the potential use of pension funds and public-private partnerships are relatively straight forward there are also possibilities to raise domestic resources from taxing speculative financial transactions.

While not appropriate in most cases, we should not lose sight of instruments used in other parts of the world which may be workable in some of our economies. Some of these options are air travel levies, sovereign wealth funds including inter-generational funds based on exhaustible natural resources, carbon taxes dedicated for financing investments in clean energy. While most of our countries cannot rule these forms of financing in, we should certainly keep an eye on them and not rule them out.

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In conclusion, I wish to stress the continued importance of sound fiscal policies, political will, institutional capacity and good governance to underpin on-going efforts to mobilize domestic resources. As we celebrate this 10th anniversary of NEPAD, it is such policy measures and practical steps that will take us closer to our objective of transforming Africa's economies.

I thank you for your kind attention. ECA stands ready as always to work with partners such as the African Union Commission and the NPCA to accompany the efforts member States in the vital task of mobilizing domestic resources for development.

Thank you.