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**A Way Forward**

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**NAVAL  
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**MONTEREY, CALIFORNIA**

**THESIS**

**SUB-SAHARAN AFRICA AND THE MARKET ECONOMY:  
A WAY FORWARD**

by

Babafemi Runsewe

March 2008

Thesis Co-Advisors:

Letitia Lawson  
Jessica Piombo

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| REPORT DOCUMENTATION PAGE   |  |   | Form Approved OMB No. 0704-0188                     |  |
|---|--|---|---|--|
| Public reporting burden for this collection of information is estimated to average 1 hour per response, including the time for reviewing instruction, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to Washington headquarters Services, Directorate for Information Operations and Reports, 1215 Jefferson Davis Highway, Suite 1204, Arlington, VA 22202-4302, and to the Office of Management and Budget, Paperwork Reduction Project (0704-0188) Washington DC 20503.   |  |   |   |  |
| 1. AGENCY USE ONLY (Leave blank)  |  | 2. REPORT DATE<br>March 2008                            | 3. REPORT TYPE AND DATES COVERED<br>Master's Thesis |  |
| 4. TITLE AND SUBTITLE: Sub-Saharan Africa and the Market Economy: A Way Forward   |  |   | 5. FUNDING NUMBERS                                  |  |
| 6. AUTHOR(S) Babafemi Runsewe   |  |   |   |  |
| 7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES)<br>Naval Postgraduate School<br>Monterey, CA 93943-5000  |  |   | 8. PERFORMING ORGANIZATION REPORT NUMBER            |  |
| 9. SPONSORING /MONITORING AGENCY NAME(S) AND ADDRESS(ES)<br>N/A   |  |   | 10. SPONSORING/MONITORING AGENCY REPORT NUMBER      |  |
| 11. SUPPLEMENTARY NOTES The views expressed in this thesis are those of the author and do not reflect the official policy or position of the Department of Defense or the U.S. Government.  |  |   |   |  |
| 12a. DISTRIBUTION / AVAILABILITY STATEMENT<br>Approved for public release; distribution is unlimited  |  |   | 12b. DISTRIBUTION CODE                              |  |
| <p>13. ABSTRACT (maximum 200 words)</p> <p>The thesis examines what economic policies are most suited for African countries in the light of the poor economic performances over the years. Policy prescriptions have varied from the state getting actively involved in the economy by shaping and directing to allowing the economy shape itself. The regional framework, New Partnership for African Development, accords recognition to the efficacy of the market shaping itself. However, differences remain on the involvement of the state and role of the market. This study aims to provide answers to this through a comparative examination of successful and unsuccessful economic cases</p> <p>In the case studies, none of the argument was sufficient alone to improve economic growth and development. While the market facilitated growth in some sectors, it was state involvement that exploited and facilitated growth in others. The growth in instances the state intervened was sustained by market-friendly policies and short-term interventions. It is also obvious that growth is dependent on the nature, competence and independence of a state's bureaucracy.</p> <p>Overall, the paper concludes that a blend of improved planning and opening of the market guarantees economic growth and development.</p> |  |   |   |  |
| 14. SUBJECT TERMS Sub-Sahara Africa, Liberalization, Structural Adjustment,   |  |   | 15. NUMBER OF PAGES<br>105                          |  |
|   |  |   | 16. PRICE CODE                                      |  |
| 17. SECURITY CLASSIFICATION OF REPORT<br>Unclassified   | 18. SECURITY CLASSIFICATION OF THIS PAGE<br>Unclassified | 19. SECURITY CLASSIFICATION OF ABSTRACT<br>Unclassified | 20. LIMITATION OF ABSTRACT<br>UU                    |  |

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**SUB-SAHARAN AFRICA AND THE MARKET ECONOMY: A WAY  
FORWARD**

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Submitted in partial fulfillment of the  
requirements for the degree of

**MASTER OF ARTS IN SECURITY STUDIES  
(STABILIZATION AND RECONSTRUCTION)**

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## **ABSTRACT**

This thesis examines the economic policies most suited for African countries in light of the poor economic performances over the years. Policy prescriptions have varied from the government taking active roles in fashioning and directing the economy to allowing the economy to shape itself through the forces of demand and supply. The regional framework for economic development, New Partnership for African Development, accords some recognition to the efficacy of forces of demand and supply. However, some fundamental differences remain in the involvement of the state and role of the market. This study aims to provide answers to this through a comparative examination of successful and unsuccessful economic cases.

In the case studies, none of the approaches was sufficient alone to improve economic growth and development. While the market exploited and facilitated growth in some sectors, it was state involvement that facilitated growth in others. The growth in instances the state intervened was sustained by market-friendly policies and short term involvement. It was also obvious that success is dependent on the nature, competence and independence of a state's bureaucracy.

Overall, this paper concludes that a blend of improved planning and management and opening of the market guarantees economic growth and development.

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## **ACKNOWLEDGMENTS**

I express my profound gratitude to Professors Letitia Lawson and Jessica Piombo for their guidance and mentoring during the preparation of this thesis and my studies in California. The thesis is dedicated to my children, Damilola and Temitope, for their understanding during my study.

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## I. INTRODUCTION

### A. PURPOSE

Between 1960 and 1973, the economies of countries making up the Third World were almost on par with one another. During this period, the average annual growth rate in sub-Saharan Africa (SSA) was 2.9% and peaked at 11%.<sup>1</sup> This performance was comparable to that in South East Asia and Latin America and was largely driven by agriculture and manufacturing. However, by the mid 1970s, while the economies of South East Asian countries continued to grow, those of SSA and Latin America began to decline. This was most pronounced in Africa where the gross domestic product (GDP) growth fell from 2.08% in 1975 to 1.36% in 1990.<sup>2</sup> This was unlike the countries in South East Asia, whose total GDP growth rose from 1.7% in 1975 to 2.09% in 1990.<sup>3</sup> However, in spite of the general decline in economic performance, a few African countries continued to experience economic growth. These included Mauritius, Botswana, Kenya and Zimbabwe.

Owing to poor economic performance, the Bretton Woods institutions began advising and encouraging poorly performing developing countries to embark on neo-liberal economic reforms in the early 1980s. These reforms included liberalization of the market, devaluation of currency and reduction of government budget deficit amongst other things. The aim was to open up the local market for competition and encourage an export drive which, it was believed would stimulate the local economy. While the reforms were successful in a few countries, including Ghana, Mozambique and Uganda, the reverse was the case for most of SSA.<sup>4</sup> Some assessments attributed this general

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<sup>1</sup> Michael Chege, "Sub-Sahara Africa: Under-development's Last Stand," in *Global Change, Regional Response: The New International Context of Development*, ed. Barbara Stallings (NY: Cambridge University Press, 1995), 318.

<sup>2</sup> Ibid, Also, Morten Jerven, "Regression in Africa Growth- A Review of the Method and the Evidence" (paper for the EH 590, London School of Economics, April 2007), 4.

<sup>3</sup> Ibid.

<sup>4</sup> Chege, "Sub-Sahara Africa," 309.

failure to the reforms themselves, while others argued that internal factors (the inability or unwillingness of governments to create an enabling environment, corruption, poor infrastructure, etc.) were the chief cause.<sup>5</sup>

At the same time, the advent of the 'Internet' and the quickening of globalization after the triumph of capitalism over socialism with the fall of the USSR were to increase trade and development among the developed and newly industrialized countries. Some developing countries explored the opportunities created by this diffusion of information, technology and the growing inter-dependence to improve their contributions to global trade. Unlike other regions, Africa's contribution in these areas remained insignificant, leading to the further marginalization of the region.<sup>6</sup> Its only contribution has been the supply of raw materials, while much of Asia and Latin America now contribute manufactured goods and services to the globalized economy. The purpose of this research, therefore, is to examine why some economies were successful in the region, and then to explore the options available for the rest of SSA in light of these experiences and the differing prescriptions offered by the Bretton Woods institutions and African regional experts.

## **B. IMPORTANCE**

The continuous marginalization of SSA from the global market owing to her inability to contribute meaningfully is a source of concern not only to the continent, but to the world at large. For instance, while the standard of living in much of the rest of the world has improved, the reverse is the case in Africa, threatening human security and thus regional and international security. The experience of the successful economies such as Botswana, Mauritius and Cape Verde is a lesson for the rest of sub-Sahara Africa. Recent events elsewhere have no doubt revealed that economic growth and development

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<sup>5</sup> Thomas Callaghy, "Between Scylla and Charybdis: The Foreign Economic Relations of Sub-Saharan African States," in *Africa: Dilemmas of Development and Change*, ed. Peter Lewis (Boulder, CO: Westview Press, 1998), 382.

<sup>6</sup> Charles Soludo and Osita Ogbu, "A Synthesis of Major Themes in the Political Economy of Trade and Industrialization in Africa," in *The Politics of Trade and Industrial Policy in Africa- Forced Consensus?*, ed. Charles Soludo, Ha-Joon Chang and Micheal Ogbu (Trenton, NJ: Africa World Press, 2004), 1; and Kidane Mengisteab, *Globalization and Autocentricity in Africa's Development in the 21<sup>st</sup> Century* (Trenton: Africa World Press, 1996), 17.

thrive as countries adopt democratic and liberal economic values with good planning amongst others. This is further enhanced through globalization for the ultimate benefit of the country and its people.

The need to develop the region becomes imperative considering the fact that the region has experienced most of the world's conflicts in recent years. These conflicts are largely attributed to economic causes, including: low economic growth and opportunities, reliance on the export of primary commodities, etc.<sup>7</sup> This is further compounded by the fact that the probability of conflicts is higher in countries that have been embroiled in one in the past.<sup>8</sup> Thus, it is imperative that the region develop to grow the economy and reduce the probability of more conflict.

### **C. LITERATURE REVIEW**

#### **1. Major Debates on Development in Africa**

The debates on development in SSA center on the policies adopted by governments over the years. These debates revolve around neo-liberal and state interventionist policies. The neo-liberals attribute the failures of most African economies to the state interventionist policies adopted at independence. In particular, they note that the policies, rather than boost agricultural and industrial growth which were essential to economic performance, undermined the potentials therein.<sup>9</sup> On agriculture, they assert that marketing boards and price control mechanisms rather than encouraging rural farmers to increase production, resulted in low earnings for the farmers, and a drift from rural to urban areas.<sup>10</sup> This is attributed to the practice of under pricing agricultural produce for the urban consumers while utilizing surpluses from agricultural produce to finance the industrial sector to the detriment of the agricultural sector.<sup>11</sup> In addition, they

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<sup>7</sup> Paul Collier, "Africa Growth: Why a 'Big Push?'" *Journal of African Economics* 15, Supplement 2 (2006): 191-192.

<sup>8</sup> Ibid.

<sup>9</sup> Adebayo Olukoshi, "Democratization, Globalization and Effective Policy Making in Africa," in *The Politics of Trade and Industrial Policy in Africa- Forced Consensus?* ed. Charles Soludo, Ha-Joon Chang and Michael Ogbu (Trenton, NJ: Africa World Press, 2004), 4.

<sup>10</sup> Ibid.

<sup>11</sup> John Rapley, *Understanding Development: Theory and Practice in the Third World* (Boulder, CO: Lynne Rienner, 1996), 43; and Francis Nyamnjoh and Ignasio Jimu, "Success or Failure of Developmental State in Africa: Exploration of the Development Experiences in a Global Context," in *The Potentiality of 'Developmental States' in Africa, Botswana and Uganda Compared*, ed. Pamela Mbabazi and Ian Taylor (Dakar: Senegal, CODESRIA, 2005), 21.

note that the design of an import-substitution-industrialization (ISI) strategy was responsible for poor industrial growth. They claim the strategy relied on foreign capital and, instead of driving exports, resulted in the alteration of the economic output of countries in ways that ultimately did not improve the economy.<sup>12</sup> One of the shortcomings observed in the strategy was the use of locally generated foreign exchange to finance the importation of inputs and spare parts for industries, which had amongst other things, led to the stifling of the development of a local capitalist class.<sup>13</sup> In addition, they note that in instances where ISI propelled exports, it was to neighboring countries and not to the developed economies. Kenya's trade with its neighbors is cited as an example in this regard.

Underpinning these economic choices, the school asserts that the array of subsidies, governments' part-ownership of ISIs, tariffs, high exchange rates and protective measures created avenues for rent-seeking, patronage and corruption which bedeviled the political class, regulatory bodies, bureaucracy and society at large.<sup>14</sup> Further, they opine that a lack of political empowerment and development of the populace allowed the self-serving African elite to continue the colonial practice of using the state to extract wealth for personal gain. The net effect of which was a downturn in the fortune of state-owned industries, non-competitiveness of the industrial sector, inefficiency in the bureaucracy and a decline in public goods and services.<sup>15</sup> In addition, lack of accountability and the authoritarian and paternalistic nature of most African states are seen as both causes and effects of the policies adopted.<sup>16</sup>

After a decade of neo-liberal Structural Adjustment Programs (SAPs), the state interventionist school took up the position of critic. The criticism of neo-liberalism included the failure of SAP policies to take cognizance of the role of external factors in their design, the abandonment of the concept of nation-building, which was paramount in

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<sup>12</sup> Rapley, *Understanding Development*, 39.

<sup>13</sup> Ibid., 32-33; and Mengisteab, *Globalization and Autocentricity*, 137.

<sup>14</sup> Thandika Mkandawire and Charles Soludo, *An African Perspective on Structural Adjustment: Our Continent Our Future* (Trenton, NJ: Africa World Press, 1999), 25.

<sup>15</sup> Rapley, *Understanding Development*, 44.

<sup>16</sup> Mengisteab, *Globalization and Autocentricity*, 134-135; and Mbabazi and Taylor, *The Potentiality*, 22.

the design of the intervention strategy adopted at independence, and the “elevation of rent-seeking and neo-patrimonialism to the status of a conceptual *deus ex machina* which explained everything that went wrong.”<sup>17</sup> Another criticism of the neo-liberal policy was its assumption that any active state role was detrimental or hostile to the private sector, and the discrediting of the state has a player in the development of a state. The school notes that external constraints such as unfavorable terms of trade and large external debt burdens were important contributors to the failure of development in countries of the region. Furthermore, they assert that some of the rents that neo-liberal policy frowned upon were integral to the development of capital accumulation and thus a distinction ought to have been made between productive and unproductive rents.<sup>18</sup> In this regard they argue that rent-seeking ought not to have been conflated with corruption, patron-client relationship and the extended family system.<sup>19</sup> In addition, they opine that the protective barriers such as tariffs, licenses, and import restrictions that the neo-liberals sought to remove served multiple objectives which were necessary considering states’ low revenue bases and late entry into the global economy.

The most criticized aspect of the Structural Adjustment policy was the relegation to the background of local politicians, bureaucrats and policy makers in the search for solutions by the BWI and the implementation of the policy. The school argues that the imposition of the policy through conditionalities and the discrediting of local politicians, policy makers and bureaucrats doomed the policy from its inception, largely because there was no domestic consensus to guarantee local ownership and sustainability.<sup>20</sup> Furthermore, they argue that some of the policies condemned in Africa were successfully utilized in Asia, the difference being the means of financing industrialization.<sup>21</sup> The group gives credence to their arguments with the tacit admittance by the BWI of the inadequacies of the policies.<sup>22</sup> This, they claim, was buttressed by the poor performance of the economies of most SSA by the end of the decade.

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<sup>17</sup> Olukoshi, “Democratization,” 7; and Mkandawire and Soludo, *An African Perspective*, 27.

<sup>18</sup> Ibid.

<sup>19</sup> Ibid.

<sup>20</sup> Mkandawire and Soludo, *An African Perspective*, 26; and Olukoshi, “Democratization,” 9.

<sup>21</sup> Ibid., 32, 34.

<sup>22</sup> Rapley, *Understanding Development*, 119.

Each school supports its claim largely with quantitative analysis of economic indicators for the continent as a whole. This approach masks the significant variation within the continent, in policy, performance and local ownership. Therefore, this thesis will adopt a comparative case study approach in order to bring new evidence to bear on this long standing debate.

## **2. A Major Question**

The tacit acceptance by African leaders of the neo-liberal agenda in the New Partnership for African Development (NEPAD) and the World Bank's ostensible acceptance of the importance of local ownership have created something of a consensus on the development policy for the first time in three decades. However, differences remain. While the AU and Africa specialists are now more favorably disposed to improving public planning and management based upon their readings of the East Asian success stories,<sup>23</sup> the BWI remain focused on economic openness of the economy based on different readings of successes in the new industrializing countries of Asia. In particular, the AU and regional specialists are of the position that while the economy is driven by the market, the state should play a significant role in guiding and developing the economy.<sup>24</sup> The BWI, however, remain committed to the economy being driven by the market with minimal government involvement.

This thesis seeks to address this debate about whether improved planning and management, a further opening of the economy or a nuanced combination of the two is most likely to contribute to economic growth and development in Africa. Accordingly, the effect of the public sector, its roles and policies on the development of the agricultural and industrial sectors will be examined.

## **D. METHODOLOGY**

To address the objective of the study, this thesis will examine the cases of Botswana, Nigeria and Malaysia. A comparison between the successful and unsuccessful cases will be made to ascertain what went right and what went wrong. Botswana was chosen because it is one of the few successes in Africa with an estimated 2006 GDP per

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<sup>23</sup> New Partnership for African Development Framework Document, <http://www.nepad.org/2005/files/homes.php> (accessed March 12, 2008; Olukoshi, "Democratization," 25; Mengisteab, *Globalization and Autocentricity*, 185; and Mkandawire and Soludo, *An African Perspective*, 96-100.

<sup>24</sup> Ibid.

capita of about \$10,900.<sup>25</sup> Among other things, it presents a fairly good representation of most African countries in terms of colonial legacies. Furthermore, it started as a primary product exporter (of cattle and later diamonds), with a low GDP at independence. Malaysia was chosen largely because it is one of the relatively successful cases in South East Asia, having a GDP per capita of about \$12,900.<sup>26</sup> Furthermore, like most African societies, it is multi-ethnic, started as a mono-crop economy and has diversified its economy, thus substantially improving the economy. Nigeria was chosen because the outcomes of their development efforts have not been successful, with an estimated GDP per capita of \$1,500 in 2006.<sup>27</sup> Each case study will conclude with an assessment of whether its experience is best explained by the neo-liberal argument of the BWI or the developmental state argument of African regional specialists. The BWI are right if ISI and state intervention mechanisms hampered economic growth and development in the three cases. On the other hand, the developmental state school is right if the implementation of neo-liberal policies hampered or did not impact positively on economic growth and development. This thesis concludes with the comparative analysis and conclusions with respect to the implications of its findings for economic policy options for SSA as a whole. Secondary sources will be used for the research.

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<sup>25</sup> Central Intelligence Agency, *The World Fact Book*, <http://www.cia.gov/library/publications/the-world-factbook/print/bc.html> (accessed September 2, 2007).

<sup>26</sup> Ibid.

<sup>27</sup> Ibid.

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## **II. NIGERIA**

### **A. INTRODUCTION**

This chapter examines the role of the public sector and the effects of its policies on the agricultural and industrial sectors of Nigeria between 1970 and 2005. In particular, it focuses on whether the role and policies of the state and the resultant outcome support the arguments of the neo-liberals or developmental state advocates. The period from 1960-70 is not examined because the effects of the Civil War will obscure the effects of economic policies significantly. Similarly, the period from 1990 to 1999 is not examined because of political instability due to the annulment of elections and military interventions.

The policies of the state are best understood by an examination of three distinct periods: 1970-85, 1986-99 and 1999-2005. The state intervened actively through legal and institutional mechanisms, and active participation in direct production between 1970-85 and this resulted in a decline in industrial and agricultural performance. A mix of IMF imposed neo-liberal policies and state-led development formed the basis of the period 1986-1999. During that period, agricultural output increased tremendously while industrial performance was uneven. The most significant improvements in the manufacturing sector were in agro-allied industries. The period 1999-2005 heralded the adoption of home-grown neo-liberal policies, a reduction of the state's active role and improved governance and management. The contribution of the non-oil sector to GDP increased significantly, but with minimal growth in the industrial sector. Nevertheless, the petroleum sector remained the dominant contributor to the GDP. The most important change in this period was the pronounced reduction in the government's role due to divestment in some sectors of the economy, strengthening of the bureaucracy and rationalization of the work force. Overall, this chapter shows that none of the two arguments satisfactorily result in economic growth and development. It is, however, obvious that liberalism is ultimately beneficial to growth, while state-led development facilitated the market in some sectors.

## **B. POLITICAL HISTORY**

The history of Nigeria is traceable to the amalgamation of the Northern and Southern Protectorates of 1914. This action set the stage for full British administration. Prior British relations were limited to trade.<sup>28</sup> The amalgamation opened new economic and social orders in the country, and was based on financial and economic concerns.<sup>29</sup> The increased agitation for independence by the elite and a few educated Nigerians after World War II led to a series of constitutional negotiations culminating in the 1954 Richard Constitution. The Constitution led to the formation of a federal state consisting of three regional governments and a weak central government. This structure led to a further deepening of the ethnic divisions in the polity. British administration formally ended in October 1960 with the hand-over of power to the Nigerians. The post-independence democratic regime was ended by the military coup of January 1966 following civil disturbances in the regional elections in the western region.<sup>30</sup> The high point of instability during the period was the Civil War of 1967-70. Military administrations ended in 1979 after thirteen years of military rule, only to return in December 1983. This second period of military regimes ended in May 1999, and the country has since been under democratic rule.

## **C. POLITICAL ECONOMY**

Nigeria was an agrarian economy with a significant level of extractive industry activity until the early 1970s. Trade between European companies and the marketing boards established by the colonial administration facilitated the growth of cash-crop export to supplement the preexisting food crop-based agrarian economy.<sup>31</sup> The boards regulated purchase prices and controlled exports. Minerals such as tin and coal were mined beginning in the early twentieth century, but the capital intensity of these sectors prevented Nigerians from participating in its exploration and extraction. Foreign investors earned most of the profit while the colonial government earned little.<sup>32</sup> The

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<sup>28</sup> Michael Crowder, *A Short History of Nigeria* (NY: Frederick A Praeger, 1962), 205.

<sup>29</sup> Ibid, 213; and W B Hamilton, "The Evolution of British Policy Towards Nigeria" in *The Nigeria Political Scene*, ed. Robert O Tillman and Taylor Cole (NC: Duke University Press, 1962), 32.

<sup>30</sup> Richard Sklar, "Crisis and Transition in the Political History of Independent Nigeria," in *Dilemmas of Democracy in Nigeria*, ed. Paul Beckett and Crawford Young (NY: University of Rochester Press, 1997), 20.

<sup>31</sup> Ibid., 83.

<sup>32</sup> Ibid., 91.

accumulated surpluses of the marketing boards and the earnings from the extractive industries financed economic development projects of the era.

The establishment of rail links, the introduction of portable currency, taxation, elimination of community tolls and improved security boosted trade. The discovery and exploration of crude oil in 1957 did not alter economic policy in the immediate years after independence. Instead, the economic base shifted from agriculture to oil-based commodity export in response to market forces. At independence, the country adopted an Import Substitution Industrialization (ISI) strategy like most developing countries.

#### **D. ECONOMIC AND DEVELOPMENT POLICIES**

Nigeria was administered by two development plans prior to independence. While the British administration designed the first in 1945, the second was based on recommendations from the World Bank in 1955. The first plan was premised on promoting economic development by investing in social advancement,<sup>33</sup> while the second focused on stimulating the economy through industrialization in line with the ISI strategy.<sup>34</sup> Both plans relied upon foreign capital investment to drive the economy. In the 1955 development plan, the World Bank recommended that agriculture, industrial production and development corporations play more positive and useful roles in economic development. Consequently, emphasis shifted from provision of social services to industrial stimulation through public investment in infrastructure. This resulted in the establishment of development corporations by the central and regional governments. Statutory corporations providing loans and equity finance to Nigerians and investing in foreign sponsored projects were also established in compliance with the recommendations. A lack of coordinated planning among the regional governments (and regional rivalry) resulted in the duplication of projects and waste in the system, though foreign capital investment increased. The first plan was deemed to have failed due to a lack of definitive objectives and local ownership, while the second plan was seen to have failed because of inter-regional competition over the allocation of resources.<sup>35</sup>

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<sup>33</sup> R. O. Ekundare, "Nigeria's Second National Development Plan as a Weapon of Social Change," *African Affairs* 70, no. 279 (April 1971): 146-158.

<sup>34</sup> *Ibid.*, 148.

<sup>35</sup> *Ibid.*, 147.

The First National Development Plan was formulated in 1962. The plan focused on strengthening the government's role in shaping economic development while encouraging Nigerian participation in the private sector.<sup>36</sup> However, political turmoil surrounding the 1963 elections and the 1967-70 Civil War hampered implementation of the plan. In spite of this, the economy showed significant diversification and development. Between 1962-3 and 1966-7, the industrial sector grew from 5.3% of the overall economy to 7%, and mining grew from 1.9% to 3.4%,<sup>37</sup> while agricultural production declined from 62.9% in 1960 to 48.8% in 1970.<sup>38</sup> Furthermore, the private sector drove these developments with the government's contributions limited to the provision of infrastructure. However, the enactment of Banking and Petroleum Decrees in 1969 and increased revenue from oil increased the government's role in the economy through its equity holding in foreign capital investments in the sectors.

After the Civil War, the state formulated three five-year development plans: the Second National Development Plan of 1970-1974, the Third National Development Plan of 1975-1980 and the Fourth National Development Plan of 1980-1984. These plans formed the basis of centralized development planning until 1986 when a neo-liberal structural adjustment program (SAP) was adopted as the economic development framework. SAP was implemented until 1993 when the government formally withdrew from the program. In spite of its withdrawal, it continued to implement some of the policies of the program until 2003 when the National Economic Empowerment Strategy (NEEDS) was adopted as the policy framework.

#### **E. THE 1970–1985 ERA**

The Second National Development Plan was designed as a tool for social change and broadening of the productive base to improve the lot of the citizenry.<sup>39</sup> The government's intention to acquire and control the majority of the productive assets of the

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<sup>36</sup> Ekundare, "Nigeria's Second National," 148; and Adeoye Akinsanya, "State Strategies Towards Nigerian and Foreign Business," in *The Political Economy of Nigeria*, ed. William Zartman (NY: Praeger Publishers, 1983), 159.

<sup>37</sup> Ekundare, "Nigeria's Second National," 150.

<sup>38</sup> Fidel Ezeala-Harrison, "Structural Re-Adjustment in Nigeria: Diagnosis of a Severe Dutch Disease Syndrome," *American Journal of Economics and Sociology* 52, no. 2 (April 1993): 195.

<sup>39</sup> Ekundare, "Nigeria's Second National," 151.

country was explicit in the plan.<sup>40</sup> This revealed the state's perception that it should be a primary driver of the economy. This was not just a purely economic policy, but rather a response to causes of the Civil War, e.g., social disparities among regions and the need for greater national integration. This policy reversal resulted from the perceived adverse effects of a lack of centralized planning in the preceding era, the increased availability of state capital as a result of oil revenue, the emergence of technocrats committed to national planning, and an emerging local bourgeoisie interested in control of the economy.<sup>41</sup> The growth of the oil sector's share of GDP from 0.2% in 1960 to 31% in 1974 gave the government unprecedented leeway to acquire a major stake in the national economy and embark upon numerous projects across the country. This was due to revenues accorded the state by virtue of the Petroleum Decree 1969 and the Nigerian National Oil Corporation Decree 1971, which institutionalized the state's part ownership of foreign enterprises in the oil sector. Highlights of the plan include the allocation of about 8.4% of public sector expenditure to industry against 2.9% in the 1955-61 Plan.<sup>42</sup> The significant increase in public investment in industry was consistent with the ISI strategy. This policy shift was backed by additional laws meant to enhance Nigerian participation in a redistributive and sectorally balanced economy. These new laws sought to enhance the state and the citizen's participation in the economy as a means of reducing foreign domination.

### **1. Private Sector Promotion**

While the policies of the preceding era resulted in increased foreign capital investments, the Nigerian Enterprise Promotion (NEP) Decree of 1972 and 1977 increased Nigerian capital investments. The objective of the policy was to increase Nigerian participation in the economy by establishing a ceiling on foreign capital equity in enterprises and broadening of the productive base. In other words, the legal framework facilitated the Nigerians' entry into commercial and less capital and technical intensive manufacturing sectors such as stationery and consumer goods, while encouraging foreign investments in high capital and technical intensive manufacturing.

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<sup>40</sup> Akinsanya, "State Strategies," 159.

<sup>41</sup> Ibid.

<sup>42</sup> Ekundare, "Nigeria's Second National," 151.

The decree eliminated, restricted and reserved some sectors for foreign participation and increased government stake in foreign-owned interests by as much as 49%.<sup>43</sup> However, this investment program was undermined by rent-seeking and clientelism, ultimately contributing to the downturn in the economy. Rather than enhance equity participation of the Nigerians bourgeoisie, it benefited a few in the bureaucracy, political class and the business community. This was because the local bourgeoisies were not united in the goals of Nigerian participation in the economy. Moreover, the state was perceived as a means of seeking economic wealth and furthering ethnic interests rather than national interests.<sup>44</sup> While some wanted a share of the proceeds of the most successful foreign dominated sectors of the economy others wanted niche protection of the economy from foreign competition. The policy accommodated the differing views and resulted in the creation of avenues of exploitation by those interested only in proceeds in collusion with the bureaucracy. Those interested in proceeds utilized political connections to secure loans from statutory institutions to procure shares. On the whole, the broadening of the productive base was not achieved because the shift to production of intermediate and high-end goods and services did not occur because the government did not want to undermine investments of the multi-national companies (MNC), while they also exploited loopholes in the policy to maintain their hold. The policy, however, succeeded in increasing Nigerian participation in the commercial sector.

Failure resulted from acts of omission and commission by the bureaucracy and subversion by foreign firms.<sup>45</sup> The failure to implement and of outcome indicated the government's tacit recognition of the importance of foreign investments in the economy and a deliberate measure to accommodate pressure from sections of the business class. On one hand, inherent flaws in the indigenization policy were exploited for personal gain by the political elite and business community in collusion with the bureaucracy and

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<sup>43</sup> Thomas Biersteker, "Indigenization in Nigeria: Rationalization or Denationalization?" in *The Political Economy of Nigeria*, ed. William Zartman (NY: Praeger Publishers, 1983), 189; and Akinsanya, "State Strategies," 157.

<sup>44</sup> Atul Kohli, *State-Directed Development: Political Power and Industrialization in the Global Periphery*, (NY: Cambridge University Press, 2004), 314-315.

<sup>45</sup> Akinsanya, "State Strategy," 161; N Ikpeze, C. Soludo and N. Elekwa, "Nigeria: The Political Economy of Policy Process, Policy Choice and Implementation," in *The Politics of Trade and Industrial Policy in Africa - Forced Consensus?* ed. Charles Soludo, Ha-Joon Chang and Michael Ogbu (Trenton, NJ: Africa World Press, 2004), 12.

foreign-owned enterprises. While the public sale of shares was regulated, private transactions were not. This created avenues of exploitation by the politically connected elite (interested in a share of the successful MNC) who had privileged information and access to capital from government financial institutions. Federal and state commissioners were granted exceptional power without checks and balances to amend schedules and grant exemptions.<sup>46</sup> In addition, the time allowed for compliance afforded companies ample time to manipulate provisions of the policy. Some companies placed Nigerians in a position of ownership or responsibility as cosmetic fronts to provide legitimacy, while others divided their operations along the government's categorization of investment profile. Furthermore, the rents created by state intervention drew local and even some foreign private investments away from long-term productive ventures to short-term investments with quick profits. On the other hand, the policy failed to reduce foreign control and restructure the productive base of foreign investments from production of low-end goods to intermediate and high-end goods and services. On the whole, the measures had a slight positive effect on Nigerian involvement in the commercial and service sectors, while foreign enterprises focused on manufacturing.

The government also used its increased revenue from oil exports to embark on various projects across the state. The government did not extend its involvement to the management and guaranteed foreign investment as a mark of recognition of the importance of good management and foreign capital. However, its stakes in the enterprises, which afforded it representation on the boards, were exploited for personal gain rather than national interests. These connections also afforded the companies avenues to influence government policies in their own interest while serving as a means of procuring foreign exchange. State officials were solicited by companies for foreign exchange allocations, exemptions from schedules and award of contracts in exchange for monetary and/or financial rewards. Thus, while the decree served to increase Nigerian participation, it created avenues of cronyism and corruption facilitated by the patrimonial foundation on which the civil service, political class and the military were founded, rather

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<sup>46</sup>Fiona Beveridge, "Taking Control of Foreign Investment: A Case Study of Indigenization in Nigeria," *The International and Comparative Law Quarterly* 40, no. 2 (April 1991): 311.

than promoting a local capitalist class.<sup>47</sup> Control of the commercial sector and part ownership of foreign firms went largely to civil servants, politically connected businessmen and members of the political class, resulting in a pattern of cooptation and clientelism rather than growth and development. Given the net effects of these measures, the objectives were undermined not by substance of the policies but by their implementation, which was in turn affected by the patrimonial nature of the state and the inability of the technocrats and bourgeoisie to overcome it.

Thus, some objectives of the policy were met in that the Nigerians became part-owners in the economy. However, ownership had been transferred from foreign entrepreneurs to local political elite and their clients, leaving the local bourgeoisie on the sidelines. Because access to the benefits of indigenization was dependent upon political connections rather than economic performance (and the new owners were political entrepreneurs rather than economic ones), newly locally-owned businesses failed to take root and thrive, management remained largely in the hands of foreign Multi-National Corporations (MNC), the structure of production remained largely the same, and the economic growth stagnated. Given these inadequacies, the arguments of the neo-liberals (based on human nature to maximize gains at every opportunity) that state intervention will facilitate corruption, cronyism, rent-seeking and neglect of the private sector is supported in this case.<sup>48</sup>

## **2. Financial Regulations and Control**

Before 1971, foreign companies were allowed full repatriation of profits and dividends as incentives for foreign capital investment. The Exchange Control Order of 1971 restricted repatriation of profit to 50% as a means of conserving foreign exchange and promoting reinvestment in the economy.<sup>49</sup> The foreign exchange that was not repatriated by MNCs was to be offered as an incentive to local investors to initiate import substitution enterprises, in recognition of the fact that import substituting industries require significant amounts of imported inputs. Foreign exchange payments for goods and machinery under Schedules I and II of the NEP Decree of 1972 were effected after

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<sup>47</sup> Chibuzo Ogbuagu, "The Nigerian Industrialization Policy: Nationalization or Pragmatism?" *African Affairs* 82, no. 327 (April 1983): 259-260.

<sup>48</sup> Rapley, *Understanding Development*, 67.

<sup>49</sup> Akinsanya, "State Strategies," 177.

90-180 days of importation following the Central Bank's approval.<sup>50</sup> In addition, credit facilities were made available for imported inputs such as machinery and plants under Schedules I and II.

However, here again the patron-client networks linking the business community, political class and the bureaucracy meant that the incentives became politicized — going to clients rather than those with the best investment plans — while foreign investors were able to use the same networks to get around the repatriation restrictions, both legally and illegally. For instance, foreign-owned enterprises requiring 40-60% foreign ownership were split into subsidiaries under Schedules I and II such that the parent company retained 60% equity in each and/or used “fronts,” thus facilitating the repatriation of more funds under the guise of importing machinery or inputs.<sup>51</sup> Furthermore, some foreign-owned enterprises negotiated technical agreements with Nigerian partners that mandated the provision of technology choice, maintenance and innovation, all of which enhanced the need to procure foreign exchange or machinery and other inputs.<sup>52</sup> At the extreme, the companies resorted to bribery of state officials.<sup>53</sup> Thus, the existing patron-client system reinforced the abuse of foreign exchange allocation, fully undermining the policy's objectives.

Given the close linkage between the business class and state officials, and the attendant exploitation of the policy for personal rather than national interest, the attainment of set goals was doubtful. Thus, while the policies might have been beneficial for the state and its citizens, the opportunities created for its exploitation in its implementation undermined its potential achievement. The neo-liberal argument that state involvement in the economy produces rent-seeking rather than development is again largely supported in this case.

### **3. Trade Policy**

Under the ISI strategy, the state also used a regime of tariffs, import quotas and trade restrictions to promote and protect its industrialization effort. Non-tariff barriers

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<sup>50</sup> Akinsanya, “State Strategies,” 177.

<sup>51</sup> Biersteker, “Indigenization in Nigeria,” 195-198.

<sup>52</sup> *Ibid.*, 193.

<sup>53</sup> *Ibid.*

such as import licenses and outright bans on imports that competed with ISI industries were also utilized. The licenses were designed to direct investment to areas of priority.<sup>54</sup> In addition to protecting and promoting industrialization, the government manipulated tariffs and non-tariff barriers to support its balance of payments.<sup>55</sup> For instance, when the balance of payment became unfavorable in 1983, the number of products under the import restrictions was increased from 235 to 387 as a means of reducing the trade deficit.<sup>56</sup> This undermined the coherence of the protection regime. While the adoption of the strategy envisaged a phased approach, the state never went beyond the first phase — the development of consumer goods industries — because the policy faltered there.<sup>57</sup> Furthermore, since reducing tariffs would deprive the state of revenue and expose local industries to foreign competition, tariffs were never reduced, and thus import substituting industries had no incentive to become competitive. In addition, issuances of licenses were abused by entrenched patron-client networks, ultimately undermining set goals. In its entirety, protection was not negative, but it was the implementation and the tariff structure that affected the performance of the industrial sector.

Given that state intervention enhanced industrial growth, the arguments of the development state school, that state intervention is required to promote diversification, appear to be supported on the surface. However, the sustainability of the growth was undermined by the same institutions which created it through rent-seeking and clientilism, buttressing the arguments of the neo-liberals.

#### **4. Agricultural Development**

Agricultural development during the period was poor due to neglect, poor policy choices and bias toward industrial development. The Second National Development Plan (1970-74) earmarked over 80% of total investment to urban areas, with only 4.8% for capital expenditure on agriculture despite the fact that 70% of the population resided in

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<sup>54</sup> Akinsanya, “State Strategies,” 174.

<sup>55</sup> Milton Iyoha and Dickson Oriakhi, “Explaining African Economic Growth Performance: The Case of Nigeria,” (interim report on Nigeria prepared for the African Economic Research Consortium Project titled “Explaining African Economic Growth Performance,” May 2002), 29.

<sup>56</sup> Ibid.

<sup>57</sup> Ibid.

rural areas and were engaged in agriculture.<sup>58</sup> The agricultural sector allocation was for the establishment of a national agricultural bank, extension and irrigation schemes, and conservation services. However, rural smallholders, who constituted the vast majority of farmers, did not benefit from credit facilities because often times they were hijacked or exploited preferentially by urban/elite farmers. For instance, the Nigeria Agricultural and Cooperative Bank allocated N341 million to 400 retired military personnel, civil servants, businessmen and their companies, compared to N18 million to 8,456 small farmers between 1973 and 1986.<sup>59</sup> At the extreme, rural farmers were displaced from their lands to barren lands to make way for irrigation projects, and were at times encouraged to sell their lands to state officials and wealthy farmers.<sup>60</sup> Urban/industrial bias generated income disparities as wage increases in the industrial sector outstripped income growth in the farming sector, which led to increased rural-urban migration and depletion in the rural labor force.<sup>61</sup> While sectoral per capita earnings as a percentage of overall per capita earnings in manufacturing and construction were 26% and 23% respectively, it was only 9% in agriculture.<sup>62</sup>

By 1974, the agricultural sector's share of GDP had declined to 26.5% from 48.8% in 1970, while agricultural export declined from 30% in 1970 to 7.2% in 1975.<sup>63</sup> This led to an increased focus on agriculture in the Third National Development Plan in 1974. In addition to increasing its direct involvement in agricultural production, government improved the rural infrastructure and subsidized agricultural inputs to curb rural-urban migration and increase agricultural production. In a bid to promote local processing industries and avoid domestic shortages, government (through the marketing boards) imposed a series of taxes on agricultural exports, and in some instances an outright ban

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<sup>58</sup> Henry Bienen, "Income Distribution and Politics in Nigeria," in *The Political Economy of Nigeria*, ed. William Zartman (NY: Praeger Publishers, 1983), 90-91.

<sup>59</sup> *Ibid.*, 206.

<sup>60</sup> *Ibid.*

<sup>61</sup> Michael Watts and Paul Lubeck,, "The Popular Classes and the Oil Boom: A Political Economy of Rural and Urban Poverty," in *The Political Economy of Nigeria*, ed. William Zartman (NY: Praeger Publishers, 1983), 131; and Bienen, "Income Distribution," 92.

<sup>62</sup> Ezeala-Harrison, "Structural Adjustment," 196.

<sup>63</sup> *Ibid.*, 198.

on agricultural export.<sup>64</sup> However, this measure resulted in the exploitation of rents and smuggling of agricultural commodities into neighboring countries where producer prices were higher by both farmers and wholesale merchants, generating an informal economy which undermined economic development strategies and deprived the state of tax revenues. The over-taxation (through low producer prices) also led farmers to shift production from exportable produce to food crops that could be consumed or sold in the local market, and to move into non-agricultural activities. This scheme failed not necessarily by the nature of the policy but due to implementation. The policy framework sought to redress the decline in performance and link with the industrial sector indicative of good plans. Its failure was due to its being hijacked by the urban elite.<sup>65</sup> The elite exploited the credit facilities and subsidization to the detriment of small rural farmers who constituted the majority by eliminating the off-set the subsidy would have provided on the taxes.

In addition, the state promoted mechanized and irrigation farming to boost production. However, the exorbitant cost of the establishment of the farms made the cost of agricultural production unaffordable by the rural farmers. For instance, the cost per hectare of irrigation ranged between N1,750 and N8,000; well above the income of rural farmers.<sup>66</sup> Agriculture increased from 20.6% of GDP in 1980 to 28.6% in 1983.<sup>67</sup> However, the increased share was due to a slight increase in agricultural export from 2.4% in 1980 to 3.6% in 1983,<sup>68</sup> and a decline in the international price of crude oil in the early 1980s. By 1985, the share of agriculture to the GDP had declined to 24%, while its share of exports declined even more drastically to 2% from a high of 70% in 1960.<sup>69</sup> This was primarily due to the recovery in the price of crude oil in the global market, and secondarily to the ban on the exporting of certain primary agricultural products as part of the effort to promote agro-industries.

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<sup>64</sup> Gary Moser et al., *Nigeria: Experience with Structural Adjustment* (Washington, DC: International Monetary Fund, 1997), 66.

<sup>65</sup> Ibid.

<sup>66</sup> Watts and Lubeck, "The Popular Classes," 122.

<sup>67</sup> Ibid., 195.

<sup>68</sup> Ibid., 198.

<sup>69</sup> Iyoha and Oriakhi, "Explaining African Economic Growth," 35.

In this area, the policy framework's goals were undermined by its substance as well as its implementation. Fixing prices below market value undermined farmers' incentives to sell to the marketing boards, leading them to smuggle their produce across the borders to neighboring countries where producer prices were higher. The network of patronage (middlemen), politicization, and the accumulated surpluses provided created opportunities (rents) for exploitation of the marketing boards which benefited personal rather than national interest. Furthermore, mechanization did not benefit the rural farmers who constituted the majority, while the urban farmers could barely afford the cost of production. On the other hand, the policies and their implementation hampered production and support the arguments of the neo-liberals that these mechanisms squeeze farmers, result in rural-urban migration and an overall decline in agricultural production. For instance, between 1970 and 1978 real food output per capita declined by 1.5% per annum while food imports rose from N57.7 million in 1970 to N790.3 million in 1977.<sup>70</sup> Given the exploitation of state mechanisms by the elite, the preference for urban development and the dramatic market-driven growth in the oil sector, it was no surprise that agricultural production declined. The emergence of elite farmers failed to boost agriculture, while the urban-rural wage differential drained manpower from the rural areas, depriving it of a work force. The arguments of the neo-liberals that state led development and ISI constitute a drain on agricultural development are supported in this analysis. Furthermore, the relative increase in production due to the intervention in infrastructural development under the Third and Fourth NDP is an indication of the efficacy of state indirect support to agriculture in which neo-liberals proffer.

## **5. Effects of State-led Development on the Economy**

In the short term, the industrial sector benefited the most from the government's involvement in the economy having attained an 11% share of the GDP by 1981.<sup>71</sup> Success was driven by increased foreign direct investment under ISI and the government's investment in industry and urban infrastructure. Government intervention also allowed politically and socially important considerations of regional balance to be factored into development and wealth creation. Furthermore, by controlling the

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<sup>70</sup> Watts and Lubeck, "The Popular Classes," 117-118.

<sup>71</sup> Ikpeze, Soludo and Elekwa, "Nigeria: The Political Economy," 1.

economy, the government succeeded in empowering the politically-connected Nigerian private sector through equity holdings in foreign-owned firms while it established capital-intensive industries that were beyond the reach of Nigerian.

On the other hand, the fact that plans sought to facilitate social change, politics and geographical spread rather than maximizing the efficiency in production played prominent roles in the location and siting of most of the industries. For instance, while crude oil is extracted in the Niger Delta region, a refinery was constructed in the north of the country about 1000 km away from the source of raw material and serviced by a network of pipelines covering about 3001 km, as a means to assuage the demands from the northern section of the country.<sup>72</sup> This increased the cost of production and inefficiency was beyond reason. Thus, instead of generating revenue for the state and establishing themselves as competitive import substituting enterprises, such industries became a burden on the government because of subventions and subsidies and on consumers because their tariff protected above-market sales prices. More important was the rent-seeking and clientelist network formation that followed from government control, exercised both by politicians and civil servants, over not only location decisions, but licenses, tariffs and other factors that determined the survivability and profitability of infant industries. The array of protective measures rather than encouraging competition and increasing productivity, and thus leading into the second phase of the ISI, resulted in contentment by local enterprises to concentrate on light consumer goods production behind high tariff barriers. By and large, the manufacturing sector remained uncompetitive, unable to enter the export markets and only able to maintain local market share.

The most obvious outcome of the ISI policy was a rapid increase in government expenditure in general, and in the industrial sector in particular. This expansion was occasioned by the fact that the government, apart from establishing these industries and others, was funding and subsidizing services and products even in the face of obvious losses. The losses were occasioned by the high cost of production resulting from a lack of competitiveness, rent-seeking by the management and political office holders, and the

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<sup>72</sup> Ikpeze, Soludo and Elekwa, "Nigeria: The Political Economy," 15.

poor attribute accorded such ventures as money-milking projects. What should have been temporary losses on the road to developing competitive manufacturing sectors became perennial losses in support of patron-client networks. The long term implication of these unwholesome practices and policy choices was a decline in the industrial sector share of the GDP from 11% in 1980 to 5.7% in 1985.<sup>73</sup>

## **F. THE 1986-1993 ERA**

The adoption of IMF imposed SAP in 1986 reversed the policies of development statism to a neo-liberal policy framework. The adoption followed a series of unsuccessful locally designed stabilization measures to reverse the downturn. Among other things, the objectives of the program were to achieve fiscal and trade balance, and promote non-inflationary economic growth using market forces. The goal of restructuring and diversifying the productive base was retained, but was now to be achieved through market forces. The key policies of the program included the tightening of fiscal policies, adoption of a market-determined exchange rate, elimination of price control and marketing boards, rationalization and elimination of public expenditure and commercialization or privatization of most federal public enterprises.<sup>74</sup> Each of these policies involved a reduction of the state's role and control in the economy.

### **1. Financial and Monetary Regulations**

The fixed exchange regime had facilitated corruption and manipulation by the state administration, business class and political elite, resulting in uncompetitive industries and stifling local investment. The Naira had become extremely overvalued, making devaluation a necessary incentive to boost local sourcing of raw materials, marketing of tradable goods, export growth and elimination of the black market.<sup>75</sup> Rather than a gradual devaluation, market-forces were allowed to determine the Naira's value. Consequently, the currency's value fell from parity with the U.S. dollar in 1986 to N7.40 to \$1 in 1989, leading to government's introduction of some measures to curtail its impact on the economy.<sup>76</sup> The devaluation of the currency was not accompanied with interest rate devaluation in line with the recommendations. The reluctance to reduce

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<sup>73</sup> Iyoha and Oriakhi, "Explaining African Economic Growth," 29.

<sup>74</sup> Ibid., 1; and Ikeze, Soludo and Elekwa, "Nigeria: The Political Economy," 17.

<sup>75</sup> Olukoshi, "Democratization," 18.

<sup>76</sup> Ibid., 96.

interest rates reflected a policy of encouraging savings and discouraging consumption while boosting production. In addition, a ceiling was imposed on credit to the private sector by the Central Bank.<sup>77</sup> The net effect of these measures was the inability of banks to provide loans to investors, who were in turn unable to take advantage of the improved investment environment. In addition, exports of agricultural produce became profitable, and farmers reaped the benefits thereof.

The result in the industrial and agricultural sectors turned out as expected by the BWI. Performance in uncompetitive industries declined while it increased in agriculture/agro-industries and industries utilizing local inputs/substitutes. For instance, while the cost of imported raw materials rose by 229% between 1986 and 1987, the cost of locally sourced materials rose by 96%.<sup>78</sup> Furthermore, the government's mechanisms to curtail inflation and boost production through savings likewise added to the increased cost of production due to the ceiling on credit to the private sector and the resorting to illegal means to secure foreign exchange. Similarly, the drive to promote exporting led to increased competition between export and local consumption/production; ultimately increasing the price of local raw materials. This was most prevalent in agro-allied industries that sourced inputs locally. Though the result reflected the anticipated outcome, the decline in performance of uncompetitive industries was perceived as unacceptable by local manufacturers and a majority of the citizens. In addition, it was contrary to the objective the state sought to achieve through SAP. This formed the basis of the criticism by the development state, local manufacturers and the reason for reintroduction of tariffs to protect some industries.

## **2. Trade Liberalization**

The import and export licensing schemes, which hitherto served as instruments of regulation of exportable and importable goods, and foreign exchange allocation were abolished. The new tariff regime was designed to protect some categories of local industries, redress the imbalances of ISI, boost industrial production through local sourcing of industrial inputs, and generate additional revenue.<sup>79</sup> Thus, trade policy was

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<sup>77</sup> Moser et al., Nigeria: Experience, 21.

<sup>78</sup> Ibid., 100.

<sup>79</sup> Olukoshi, "Democratization," 97.

liberalized, but reflected a compromise between ISI and neo-liberal market-led growth rather than complete liberalization. These measures sought to protect potentially competitive sectors, while reducing corruption by moving from non-tariff barriers, such as quotas and licenses, to tariffs, which create fewer rent-seeking opportunities. Tariffs were also reduced, ranging from 5% to 30% on intermediate and final capital goods, and from 20% to 30% on final durable consumer goods, and 100% to 120% on final non-durable basic consumer goods.<sup>80</sup> Thus, the basic ISI framework was maintained with greater emphasis on maximizing efficiency of ISI while containing rent-seeking. However, the lower tariff levels left most local enterprises unable to compete against imports. Even with 100% tariffs, imported non-durable consumer goods were less expensive than locally produced alternatives.

Local enterprises that had been depending upon domestic price regulation of inputs (e.g., agro-industries) were simultaneously hit by liberalization of domestic prices. The Price Control Decree of 1971 and the Commodity Board Decree of 1977 were repealed allowing agricultural commodity prices to be set by the market. The rationale behind the actions was the need to improve production and profitability of the non-oil sector (agriculture), and reduce corruption and government taxation, which had stifled production and encouraged smuggling.<sup>81</sup> These goals were met for the agricultural sector, but in so doing they further undermined the competitive position of the manufacturing sectors that used local inputs.

The outcome of the new tariff regime revealed the intended consequences of the policy: the decline in performance and subsequent closure of uncompetitive industries, and growth in agricultural and agro-industries. The closure of some industries formed the basis of the criticism by the developmental state advocates that SAP led to deindustrialization. For instance, capacity utilization in the automobile industry fell from 26% in 1985 to 19% in 1989 and from 37% in 1985 to 24% in 1989 for the steel industry.<sup>82</sup> Though this was one of the objectives of SAP (eliminating industries the state lacked the comparative advantage), it is evident the state was not disposed to the idea

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<sup>80</sup> Olukoshi, "Democratization," 96.

<sup>81</sup> *Ibid.*, 12.

<sup>82</sup> Moser et al., *Nigeria: Experience*, 28.

from its review. Given that the regime sought to provide some protection and enhance local sourcing of raw materials in principle, the trade policy could be termed not liberalized. However, in practice, the reverse was the case as it was liberalized, even with efforts to protect local industries. Though the result supports the arguments of neo-liberals, it was evident that the state was disposed to its industrialization effort and would like the industries to continue operation.

### **3. Public Sector Reform**

Commercialization and privatization programs formed the bedrock of the public sector reform. Privatization entailed government divestment from SOEs, while commercialization involved the operation of SOEs as profit-making ventures with state budgetary support, but operating entirely apart from the state administration. Government divestment and staff cuts were intended to reduce the huge financial burden of unproductive companies and bloated administration as a means of balancing the government's budget and curtailing corruption. The government earmarked some state-owned enterprises for either full or partial privatization or commercialization. The state-owned petroleum, communication, banking, steel, and transportation enterprises were among the enterprises listed in the program. However, the government retained ownership of strategic industries divesting from less important ones. For instance, it retained its hold in some oil, communications and transport sectors while it sold agricultural and banking enterprises. In addition, of the more than 120 SOEs earmarked for sale, only sixteen enterprises were actually sold in 1989. These consisted of two oil marketing companies, thirteen insurance companies and one flour mill. In 1990, five other companies were privatized. This was largely the result of a lack of interest from the private sector: SOEs that had never been profitable were not seen as good investment opportunities. Little progress was made at commercializing public enterprises as well, as the government continued to provide subventions to the major SOE and received no dividends from any of the seven largest. Although allocations to SOEs fell from 33% of the government's budget in 1986 to 7% in 1990, total lending from the state rose from N0.4billion to N1.4billion within the corresponding period.<sup>83</sup> This indicated the failure of commercialization and the continued burden of SOEs on the state.

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<sup>83</sup> Moser et al., *Nigeria: Experience*, 25.

State institutions were also reorganized and strengthened to improve regulation of the financial sector. In particular, the Securities and Exchange Commission Decree of 1988 repealed the 1979 Decree and empowered the commission to regulate and supervise the capital market. This was expanded with the Companies and Allied Matters Decree of 1990, which strengthened the Securities and Exchange Commission's regulatory role on mergers and acquisitions. The Nigerian Deposit Insurance Corporation and Securities and Exchange Commission Decree of 1988 enhanced the financial and non-financial sector by protecting depositors and instilling confidence in the capital market through registration and revoking of stockbrokers, mergers and acquisitions. However, the incidences of failures and illegalities in the banking sector in the early 1990s suggest the bodies failed in their roles.

Given the failure to totally divest from the industrial sector and government's provision of subvention to SOEs, much was left to be desired on the attainment of set goals. Also, the retention of equity in some categories of SOEs by the state is an indication of differing opinions between the government and the IMF on the importance of industrialization in the economy. The implication of this was reflected in the recurrent expenditure, which rose from 10.5% of the GDP in 1986 to 15.9% in 1990.<sup>84</sup> In a nutshell, the continuous involvement of the state in the SOEs and retention of a large work force constituted a drain on revenue and justifies the call of neo-liberals for reduced state involvement in the economy. In general, the lack of commitment to the program limited the anticipated impact of neo-liberal public sector reform policies.

#### **4. Promoting Private Capital**

The Indigenization Decree of 1977 was repealed by the Nigerian Enterprise Promotion Decree of 1987. This action was one of numerous measures to attract foreign investment. Others included the abolition of the compulsory import surcharge of 30%, refund of excise duties, and retention of 50% of foreign exchange earnings by manufacturers and tax-free dividends for three years.<sup>85</sup> In addition, the Decree reduced the number of restricted areas of investments under the Indigenization Decree of 1977 and increased the maximum equity holding of foreign capital in banks, insurance, oil

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<sup>84</sup> Moser et al., *Nigeria: Experience*, 23.

<sup>85</sup> Olukoshi, "Democratization," 98.

production and mining enterprises to 40%.<sup>86</sup> To boost private investment in agriculture, the Directorate for Foods, Roads and Rural Infrastructure was established to develop the public infrastructure in rural areas.<sup>87</sup> Of the estimated 60,000 km of road network to be rehabilitated and built under Phase 1, only 30,000 km were met by 1988.<sup>88</sup> This was due to the reduced funds allocated to the project. In 1986, only N300 million of the authorized N433 million was released to the directorate. Most importantly, the plan did not take into account the different needs of the rural areas and was not coordinated with other development mechanisms. In spite of these limitations, there were significant improvements in agricultural production. On the whole, these measures did not attract much sought after foreign investment. Likewise, the unfavorable tariff regime and deregulation of the interest rate made the incentive structure unattractive to new investments. Private investment peaked at 10.9% of the GDP in 1986, but declined to 3.9% in 1990.<sup>89</sup>

## **5. Effects of SAP on the Economy**

The overall effect of SAP on the economy was mixed. While there was growth in the agricultural sector, growth in the industrial sector was uneven. This is attributable to the policies themselves and their implementation. SAP produced growth in the agriculture and manufacturing sectors for the first time in years, with GDP expansion exceeding 7% between 1988 and 1990.<sup>90</sup> Capacity utilization rose from 38% in 1985 to 44% in 1989 before falling to 40% in 1990.<sup>91</sup> The most significant increase was in industries using local raw materials. For example, capacity utilization in textile industries rose from 45% in 1985 to 60%, while that of the steel sector declined from 37% to 24% in the corresponding time frame.<sup>92</sup> This is expected given the comparative advantage of the agro-based sector over the industrial sector, and suggests the emergence of a more

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<sup>86</sup> Olukoshi, "Democratization," 98.

<sup>87</sup> L.M. Olayiwola and O.A. Adeleye, "Rural Infrastructure Development in Nigeria: Between 1960 and 1990-Problems and Challenges," *Journal of Social Sciences* 11, no. 2 (2005): 94.

<sup>88</sup> *Ibid.*, 95.

<sup>89</sup> Moser et al., *Nigeria: Experience*, 33.

<sup>90</sup> Peter Lewis, "From Prebendalism to Predation: The political Economy of Decline in Nigeria," *The Journal of Modern African Studies* 34, no. 1 (March 1996): 86.

<sup>91</sup> Moser et al., *Nigeria: Experience*, 27; and Olukoshi, "Democratization," 103.

<sup>92</sup> *Ibid.*, 27.

sustainable manufacturing sector based on local inputs. Overall, however, industrial performance was declining. Moreover, most of the industries produced solely for the domestic market, indicating that they remained internationally uncompetitive unlike the agriculture sector which earned substantial revenue from exports.

Agricultural output rebounded tremendously following the devaluation of the currency, elimination of the marketing boards, and price control instruments. This was enhanced by improvements in the public infrastructure in rural areas and increases in world market prices of agricultural produce. Cash and food crop production increased by an annual average of 12% and 13% respectively between 1986 and 1990, against 2% and 4% during the pre-SAP era.<sup>93</sup> The performance of agro-allied industries also improved significantly, largely because they utilized local raw materials or alternatives satisfying some of the objectives of the program.

The unevenness in performance was a result of pluses and minuses of the policy and the government's commitment to state-led development. For instance, the devaluation of currency raised the cost of production for industries that relied on imported raw materials and inputs, working against policies designed to support manufacturing industries. Similarly, the demand for local inputs by processing industries, local consumers, and exporters resulted in an increase in the price of agricultural produce which contributed to inflation and raised the cost of production. Furthermore, tight credit to the private sector designed to control inflation, imposed serious constraints on raw materials and other input procurement. The new tariff regime and deregulation of foreign exchange resulted in the flooding of the local market by cheap imports of finished products much to the detriment of local industries. Commercialized SOEs remained uncompetitive and continued to be dependent on the government for subventions. The much anticipated increase in foreign direct investment anticipated by SAP did not materialize.

Overall, SAP was designed to reduce government involvement in the economy while increasing the role of the private sector. However, while this was achieved to a significant extent in the agricultural sector, the same cannot be said for the financial and

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<sup>93</sup> Moser et al., *Nigeria: Experience*, 27; and Olukoshi, "Democratization," 103.

industrial sectors. The relative success achieved in the agricultural sector could be attributed to the lack of the government's direct involvement in production in the sector historically. Removal of institutions that stifled competition and facilitated corruption, along with government investment in improving the infrastructure in rural areas, significantly increased production. On the other hand, the government's direct involvement in finance and industry was more difficult to overcome. The government's refusal to remove subsidies continuously fueled its increasing expenditure. The refusal was due to opposition to the policy which resulted in riots, entrenched interests and concerns on the implication on local industries. However, when subsidies and/or protection were lowered, local industries failed in the face of competition. The fundamental problem that ISI policies had been designed to address remained the same. Without government intervention, the economy would fall back on exporting raw materials and importing manufactured goods, limiting the prospects for growth and development over the long run. Given this reality, the period was a reflection of selective implementation of some neo-liberal policies in the early years and a reversal to some development state policies as time went by, and it became clear that much of the industrial economy would not survive the liberal policy.

#### **G. THE 1999-2005 ERA**

The formulation and adoption of the National Economic Empowerment and Development Strategy (NEEDS) in 2003 finally reduced the state's involvement in direct production and strengthened its regulatory and supervisory role in the economy. The adoption followed the return of democratic rule in 1999 and a regime committed to reduction in the government's expenditures. The strategy reflected a new mix of home-grown neo-liberal and state-led policies. The Plan was premised on a private sector driven economy focused among other things on macroeconomic, structural, public sector and governance reforms.<sup>94</sup> The objectives of the macroeconomic reforms were to stabilize the economy, improve budgeting and planning, and diversify the economy to accommodate growth of the non-oil sector. Many of the objectives of the Strategy continued those of SAP, with increased emphasis on good governance and management of the economy. The inclusion of governance and management was based on observed

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<sup>94</sup> Ngozi Okonjo-Iweala and Philip Osafo-Kwaako, "Nigeria Economic Reforms: Progress and Challenges," (Working paper no. 6, Brookings Global Economy and Development, March 2007), 1-28.

weaknesses in the administration and regulatory bodies during SAP, continuing weaknesses in the financial and banking sectors, and lessons learned from elsewhere.

### **1. Financial and Monetary Regulations**

The latest reform of the financial sector was designed to address continuing poor regulatory performance of the Central Bank and commercial banks' inability to provide loans to private investments and short-term arbitrage. The weaknesses in the banks were attributed to poor implementation of prior liberalization reforms and lapses in the adjustment program of the mid-1980s. For instance, banks exploited the opportunities presented by the liberalization of the foreign exchange market and increased demand through foreign currency round-tripping. The devalued exchange rate was below the market value creating avenues for quick profit. Therefore, a new exchange regime was instituted to eliminate the black market trade of commercial banks through market forces and state intervention when needed. New monetary regulations sought to diversify government revenue sources and reduce inflation while adhering to monetary targets.<sup>95</sup>

In addition to the financial regulations, the banking and insurance sectors were reformed through consolidation. The rationale behind the reform was the need to improve the availability of credit to the private sector and strengthen the banking sector. This entailed the consolidation of weak and fragmented banks with little capital base into strong banks with reasonable capital base. Thus, the minimum capital base of banks was raised from \$15 million in 2004 to \$192 million in 2005.<sup>96</sup> Likewise, the legally required minimum capital base of enterprises in the insurance sector was raised from \$1.2 million to \$15 million for life insurance and \$23 million for general insurance. This resulted in mergers and a reduction of commercial banks from eighty-nine to twenty-five, a generation of \$3 billion from the domestic market and \$652 foreign direct investment in the banks.<sup>97</sup> The achievements in this instance are driven by state intervention in the sector.

Budgetary planning and execution was strengthened by setting government expenditure on an oil price benchmark with excesses saved in a special crude account.

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<sup>95</sup> Okonjo-Iweala and Osafo-Kwaako, "Nigeria Economic Reforms," 9-10.

<sup>96</sup> Ibid., 15.

<sup>97</sup> Ibid.

For instance, the bench mark was set at \$25 and \$30 per barrel in 2004 and 2005, respectively, when the price of crude oil in the international market was \$38.3 and \$54.2.<sup>98</sup> This limited the effects of external shocks on the economy by creating a reserve which could be used to finance imports or other expenditures when the need arose. Similarly, sectoral spending reflected government development priorities, while institutionalized budget implementation reports reviewed strengths and weaknesses in execution.<sup>99</sup> This measure resulted in a reversal of government budget deficit of 3.5% of GDP in 2003 to a surplus of 10% in 2004 and 11% in 2005, and an increase in foreign reserve from \$7.5 billion in 2003 to \$38 billion in 2006.<sup>100</sup> The accumulation of public reserves facilitated an increase in credit to the private sector.<sup>101</sup> The reversal from deficit budget to surplus, increased availability of capital to the private sector, and a rise in foreign reserves confirms the assertions of the neo-liberals on the efficacy of adherence to monetary policies. While the run-up in the international price was a key driver in the accumulation of resources, the effective use of those resources for investment was only attainable under sound management. A similar windfall during the first Gulf War led to a surge in oil revenues that went unaccounted for by the government of the day.

## **2. Trade Liberalization**

Trade reforms were intended to address inconsistencies in trade policies introduced in response to pressure from domestic investors during the SAP era, which undermined predictability and left a tariff regime that did not create an effective incentive structure for import substitution industrialization. Under the new policy, tariffs range from 2.5% to 150% on imports.<sup>102</sup> The country adopted the Common External Tariff of the Economic Community of West African States to simplify the tariff regime and improve transparency in trade policy. The common tariff regime is geared toward encouraging added value and diversification of the economy, with built-in gradual reductions in the tariff structure to prevent protection from becoming permanent as it had in previous regimes, and thus give protected enterprises the necessary incentives to

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<sup>98</sup> Okonjo-Iweala and Osafo-Kwaako, "Nigeria Economic Reforms."

<sup>99</sup> Ibid., 12.

<sup>100</sup> Ibid.

<sup>101</sup> Ibid., 10.

<sup>102</sup> Ibid., 16.

increase their productivity and competitiveness rapidly. Tariffs were designed to give more protection to industries that were not yet competitive, such as confectioneries and rice and chocolate processing industries while encouraging competitiveness in those that were close (non-electrical, textile and clothing industries) by reducing tariffs on imported products.

Tariffs on agro-industrial imports varied with the availability and level of production in the country. Rates were generally high for those which are locally available but in the first stage of production. Thus rates on fruits, water, and cigars are high while those on oil seeds, fats and oils, and animal products, in which the country has a comparative advantage, are low. A similar structure is reflected in the manufacturing sector, where tariffs on petroleum and non-electrical products are relatively low at about 11-13%, and high in footwear, rubber, fish and fish products at about 28-30%.<sup>103</sup> The success of this new regime is dependent on how well the tariffs are reduced to expose the industries to competition to ensure their productivity and competitiveness; otherwise, the industries revert back to the pre-SAP era when they hid under tariff barriers.

### **3. Civil Service Reform**

The reform of civil service in this period was two pronged. On one hand, civil service was reformed to enhance its efficiency by the rationalization of its manpower usage and reduction of waste. In 1999, only 8% of the work force in the Ministry of Finance had degrees relevant to economics, accounting and finance, while about 70% were low-level staff with secondary education or equivalent.<sup>104</sup> The organizational structure of ministries and parastatals were reviewed and rationalized, the appropriate manpower recruited, while anti-corruption mechanisms were institutionalized to curb corruption. For instance, a value-for-audit system was introduced in the public procurement process, publication of monthly allocation of revenue to the three tiers of government and the Extractive Transparency Initiative was adopted. The attainment of the set goals is, however, dependent on the sustenance of the reforms.

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<sup>103</sup>Inye Briggs, "Nigeria: Mainstreaming Trade Policy into National Development Strategy," *ATPC Work in Progress* 52 (January 2007): 10.

<sup>104</sup> Briggs, "Nigeria: Mainstreaming Trade," 14.

On the other hand, institutional and governance issues were reformed to tackle corruption and patronage within the political class and civil service. Two anti-corruption institutions were established to reduce corruption within the polity. The institutions have been relatively effective during the period because the president was disposed to its establishment. However, the long-term impact could depend on succeeding leaders. These measures, though noble, met with opposition from political office holders in the case of monthly publications and contractors and their partners in the civil service; their effectiveness depends on implementation in the long-term. Overall, these measures have yielded some improvements with the reduction in Transparency International's ranking of corruption perception index from 1.2 in 2000 to 1.9 in 2005.<sup>105</sup>

#### **4. Effects of NEEDS on the Economy**

By 2006, eighty-six additional SOEs had been privatized against only twenty-one in 1990 under SAP. It should be noted that not all SOE have been privatized, commercialized or concessioned. Most importantly, the national oil company remains state-owned and directly controlled by the government. One significant benefit of the program was the growth in foreign direct investment in the country, which rose from \$1.3 billion in 1999 to over \$3 billion 2005.<sup>106</sup> The FDI was a result of the purchase of SOEs and new investments in existing and deregulated sectors of the economy. The work force of the bureaucracy has been reduced by about 35,700 redundant and unskilled hands, and about 1000 graduates in various disciplines have been recruited in five ministries and nine parastatals; resulting in a reduction in government recurrent expenditure and expectation for increased efficiency. The open bidding of contracts through the value-for-money audit is estimated to have saved the government over \$1.5 billion between 2001 and 2005, while eliminating one important avenue of rent-seeking.<sup>107</sup>

The liberalization of the banking and financial sectors positively impacted the economy, making credit readily available at no extra cost to investors, indicating the

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<sup>105</sup> Transparency International, "Policy and Research," [http://www.transparency.org/policy\\_research](http://www.transparency.org/policy_research). (accessed March 4, 2008).

<sup>106</sup> Augustine Nwabuzor and Dennis Anyamele, "Foreign Direct Investment into African Nations (1970-2000), Journal of Sustainable Development in Africa 4, no. 1 (spring 2002); <http://www.jsd-africa.com/jsda/spring2002/articlespdf> and <http://www.unctad.org/Template/webflyer.asp?> (accessed January 29, 2008).

<sup>107</sup> Nwabuzor and Anyamele, "Foreign Direct Investment."

efficacy of neo-liberal policies. Equally revealing is the effect of state-led involvement in the banking sector which helped consolidate and strengthen the bank's ability to perform their responsibilities. On the whole, while market forces played significant roles, state intervention through sound and good plans, implementation and management was the primary driver. The average annual growth rate in the agricultural sector from 2004–2006 was 7%, while growth in the industrial sector was 8-9% indicating balanced growth.<sup>108</sup> In large part, access to credit, export promotion initiatives and tax exemptions drove the increases in agricultural production. The growth in the industrial sector was driven by the export of plastic products (petrochemicals) to the West African sub-region and international market. However, the contribution of the sector to GDP remains low (averaging 4%) within the period.<sup>109</sup> Nevertheless, this marked a significant improvement in the economy compared to earlier efforts.

Overall, some of the effects of the policies of NEEDS support the arguments of the neo-liberals and development school on the debate of economic growth and development. Most importantly, the devaluation of the currency and the determination of value by market forces, privatization and liberalization of the public sector, and the elimination of commodity boards are very much in line with the practice. As much as these policies in totality reflect these practices, inherent differences remain. For instance, government retention of equity in some SOEs, continued promotion of ISI, involvement in infrastructure development and a semblance of regulation of the banking and financial sector run counter to neo-liberal policies. Similarly, state intervention has been indirect and within a limited time frame. This suggests that perhaps that some level of state intervention is needed to guide the economy. This is also obvious in the industrial sector given the commitment to ISI, state role in the tariff structure and financial regulation, and the relative performance in the sector.

## **H. CONCLUSION**

Nigeria inherited a free market economy driven by agriculture and low-level industrial production from the British administration. While agriculture thrived up until

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<sup>108</sup> International Monetary Fund, "Nigeria Poverty Reduction Strategy Paper- Progress Reports," *IMF Country Report* 07/270, (August 2007): 9.

<sup>109</sup> *Ibid.*

the late 1960s, it was the industrial sector performance that became significant with the beginning of oil extraction in the 1970s. In spite of the dramatic increase in government revenue accruing from the oil sector, poor policy choices and planning have adversely affected the economy. ISI policies adopted between 1970 and 1985, rather than enhance agricultural and industrial performance, undermined it. The policies were reflective of the developmental state approach in which government regulation and management of market forces through a number of mechanisms served to promote industrialization. These include, among other things, utilization of marketing boards and price controls to purchase, fix and export agricultural production, a fixed foreign exchange regime, and utilization of a tariff regime to protect local infant industries. While the measures met the objective of facilitating state development at the early years of independence as argued by regional specialists, they proved unsustainable in developmental terms in the long run owing to corruption, patronage and the heavy burden borne by the state. These problems formed the basis for neo-liberal criticisms of state managed development.

The period of 1986-1999 saw the state's haphazard effort to alter the nature of the economy through SAP. While it sought to diversify and run a free market, the retention of earlier policies and the reversal of some of the BWI policies negatively impacted the economy. Growth in the agricultural sector and agro-allied industries was facilitated by the removal of price control and marketing boards of the preceding decade, improvement of a rural infrastructure and devaluation of the foreign exchange regime in the early years. However, the reverse was the case in the industrial sector where growth was uneven due to currency liberalization and state's regulation of interest rate. Most importantly, the rollback of the state was minimally achieved as the state held on to some policies enhancing its involvement in the economy. Thus, the period was more or less made of two contrasting policies of a liberal and a state-led economy. Findings ultimately reveal that neo-liberal policies enhance agricultural production and agro-industries, while at the same time weeding out areas of the industrial sector where the comparative advantage is low. On the whole, the policies were insufficient to totally address inherent weaknesses in the state.

The adoption and implementation of NEEDS in 2003 was a far reaching effort at implementing the neo-liberal policies advanced by the BWI through SAP. Much like

SAP, the policies among other things, sought to reduce the involvement of the state in direct production, while enhancing its regulatory and governance responsibilities. The improvements in the shortcomings in SAP and local ownership of the program facilitated its acceptance and implementation unlike the structural adjustment. Most importantly, stricter adherence to the policy, public sector reform in general, and privatization and reform of the bureaucracy in particular made the most significant contributions to improved results compared with the SAP period. While the non-oil sector improved significantly with export potentials compared to preceding periods, there is still much to be desired from the industrial sector. In large part the growth in the sector continues to be driven by petroleum while industrial export is largely limited to neighboring countries. The relative performance in the industrial sector is attributable to regulations in tariffs and, to an extent, the banking sector. This confirms that continuation with the ISI strategy is dependent on some level of state protection. What needs to be done is to design a blend of market and state mechanisms that gradually expose industries to competition as the country attains some level of comparative advantage. This in turn requires effective implementation of economic policy by a strong government bureaucracy. NEEDS has moved Nigeria in the right direction on both of these counts.

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### **III. BOTSWANA**

#### **A. INTRODUCTION**

This chapter examines the role of the state, its policies and the performance of the agricultural and industrial sector in Botswana from independence until 2004. In particular, the chapter will examine how the policies have facilitated developments, and what the implications of this are for the neo-liberals and development state theories. Two distinct economic and development policies formed the bedrock of development in Botswana. Between 1966 and 1982, neo-liberalism drove the policies of the state. The economy was driven by market forces while the government restricted its involvement to infrastructural development. The policies resulted in tremendous growth in the mining industry. Though the cattle industry recorded significant growth, growth in other areas of the agricultural sector was insufficient to achieve significant growth in the sector overall. Between 1982 and 2004, the state adopted a mix of neo-liberal and state-led development policies in an effort to promote industrialization. This policy framework diversified the productive base of the economy, but failed to stimulate industrial growth, as the mining sector continued to contribute the most to GDP growth. The policies also failed to restructure and reverse the decline in the agricultural sector, which continues to be dominated by the cattle industry. Overall, the chapter will show that neo-liberal policies resulted in growth in the sectors where there was a comparative advantage, and was incapable to diversifying the productive base. State-led development, on the other hand, enhanced areas with potential advantages, which the market further exploited, resulting in growth.

#### **B. A BRIEF POLITICAL HISTORY**

Botswana gained independence from Britain in 1966. It has been a protectorate rather than a colony, and has thus experienced more limited British rule and administration.<sup>110</sup> The British intended to amalgamate the territory with South Africa through an Act of Union.<sup>111</sup> This plan was shelved, however, due to World War II, opposition by traditional rulers in the territory and the rise of the National Party in South

<sup>110</sup> Daron Acemoglu, Simon Johnson and James Robinson, "An African Success Story: Botswana," (working paper 01-37, MIT Department of Economics, July 2001): 12.

<sup>111</sup> Ibid.

Africa. Preparations for independence led to the enactment of a constitution and establishment of legislative bodies. Multi-party elections were conducted in 1965 and power was transferred in 1966. Though the country has maintained a multi-party democracy since then, the Botswana Democratic Party has dominated since its initial victory in the 1965 elections. However, unlike most countries in SSA, it has been politically stable.

### **C. POLITICAL ECONOMY**

Livestock production was the mainstay of the economy prior to the discovery of mineral resources. This was facilitated by traditional property rights, accumulation of wealth among a minority of cattle owners, levy and wage-labor relationships between local chiefs and the community.<sup>112</sup> While land ownership was vested with the chiefs, the citizenry owned cattle and/or earned a living by grazing cattle on behalf of the chiefs on community lands in exchange for a wage. The labor market was enhanced by the introduction of Hut and Native tax by the British administration in 1899 and 1919 respectively, forcing the locals to earn money to pay taxes.<sup>113</sup> The introduction of commercial ranching in the 1930s by the British administration facilitated the extension of property rights on grazing lands and water supply to individuals, thereby boosting cattle production.<sup>114</sup> The development favored the chiefs, their close associates and the rich, enhancing its acceptance and entrenchment. These formed the backbone of a market economy in the country.

In addition to its agrarian economy, the country functioned as a labor pool for South Africa because of an initial British policy on labor migration and its unfavorable agricultural conditions.<sup>115</sup> This was compounded by Botswana's relatively low economic potential compared to South Africa, which had a much bigger and developed economy. This, among other things led to Botswana's incorporation in the Southern African Customs Union (SACU) in 1910, a free trade union, and its use of the South African

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<sup>112</sup> Kenneth Good, "Interpreting the Exceptionality of Botswana," *The Journal of Modern African Studies* 30, no. 1 (March 1992): 69.

<sup>113</sup> Acemoglu, Johnson and Robinson, "An African Success Story," 13; and Louis Picard, *The Politics of Development in Botswana: A Model for Success?* (CO: Boulder, CO: Lynne Rienner Publishers, 1987): 111.

<sup>114</sup> Good, "Interpreting," 72.

<sup>115</sup> Ibid; and Acemoglu, Johnson and Robinson, "An African Success Story," 13.

Rand as currency.<sup>116</sup> Botswana's membership in the union guaranteed foreign exchange and relieved it of monetary and financial concerns, as it received a fixed share of tariffs collected at the South African entry points, and relied upon the internationally accepted South African Rand. It was under this semblance of a free market that the country attained independence in 1966.

#### **D. ECONOMIC AND DEVELOPMENT POLICIES**

Botswana was sustained by proceeds from cattle/beef exports and transfers from Britain prior to independence.<sup>117</sup> At independence, a series of five-year development plans were instituted with the objective of growing the economy. Given its manpower and skill deficiencies, it retained an expatriate administrative staff that was responsible for central planning and implementation of the development plans. This ensured the continuity and deepening of inherited practices and served to imbibe and prepare the local staff with technocratic ethos and requisite skills in economic and development planning. Botswana has implemented nine development plans, beginning with the First National Development Plan (NDP) of 1966. The attainments of macroeconomic stability, fiscal discipline and economic growth have been the objectives of all of the plans. While the First NDP focused on development of the rural sector through the provision of infrastructure, the Second NDP (1970-1975) emphasized the development of the mining sector and its supporting infrastructure.<sup>118</sup> The Fourth, Fifth, Sixth and Seventh NDPs focused on agricultural development in response to the decline in production and increased food importation, while the Eighth NDP focused on industrial development. Two distinct development approaches are observed in the evolution of the country's development plans. Between 1966 and 1982, the state adopted free market policies with limited government intervention. In the second period (1982-2004), the state became active in the economy through direct and indirect involvement in production.<sup>119</sup>

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<sup>116</sup> Picard, *The Politics of Development*, 107-108.

<sup>117</sup> Acemoglu, Johnson and Robinson, "An African Success Story," 17.

<sup>118</sup> Picard, *The Politics of Development*, 236.

<sup>119</sup> Abdi Samatar, *An African Miracle: State and Class Leadership and Colonial legacy in Botswana Development* (Portsmouth, NH: Heinemann, 1999), 139.

## **E. THE 1966-1982 ERA**

Botswana initially pursued a private sector driven economy with the state providing the enabling environment. This was achieved by promoting private capital investment through incentives, development of an infrastructure and the establishment of statutory institutions. The statutory institutions include the Botswana Development Company (BDC), National Development Bank (NDB), and Botswana Development Enterprise Unit (BDEU).

### **1. Trade Policy**

Botswana's membership in SACU afforded it two key benefits. Membership provided the country a guaranteed source of revenue from duties and tariffs collected from the entry and exit points in South Africa, and served to attract foreign capital investment. Botswana's tax structure placed no restrictions on profit repatriations. However, while Botswana did receive significant revenue, it was unable to entice foreign capital investments because of the small size of the domestic market, limited economic potential and lack of adequate and requisite skills, and greater distance from shipping ports compared to South Africa. This deepened its economic dependence on South Africa.

The agreement with SACU was renegotiated in 1969 due to perceived bias against the smaller countries and a limited tax base. This resulted in a significant increase from R1.4 million in 1968-9 to R30.46 million in 1974-5, and P104<sup>120</sup> million in 1981-2.<sup>121</sup> The increases were also driven by the increased export of cattle and beef products from 103,776 heads in 1968 to 188,440 heads in 1975.<sup>122</sup> In spite of the increase in trade taxes, investments in the mining sector and food imports outstripped cattle and beef exports and resulted in a negative trade balance. The balance of trade was negative for the first fourteen years of independence, with the exception of 1970-71 and 1978-80.<sup>123</sup> The trade deficit generally declined from 1973-4, when the mines began production, but diamond exports still did not completely offset the inflow of investment resources and

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<sup>120</sup> It (Botswana) introduced a national currency, the Pula in 1976, hence the change in currency.

<sup>121</sup> Samatar, *An African Miracle*, 138.

<sup>122</sup> *Ibid.*, 110.

<sup>123</sup> *Ibid.*, 146.

imports. In addition to its membership of SACU, the state secured a guaranteed market for its beef products in the European Economic Community. Unlike most countries in the region, it has sustained its access to the market and reaped the benefits thereof. The access and sustenance is a measure of the competence of the civil servants and the Botswana Meat Company. This is attributed to the fact that most civil servants were large cattle owners and it was in their best interest to sustain the access.

While free trade enhanced the revenue of the state, it was inadequate to stimulate the investment drive in other sectors except mining. Neo-liberal policies did not facilitate economic diversification and was inadequate to grow other sectors due to constraints such as proximity of a bigger economy and dearth of requisite skills. Furthermore, the guaranteed market in EEC, which was negotiated favorably for many years, is an indication of the convergence of interest between the civil service and business class, and competence of the bureaucracy in economic development.

## **2. Monetary and Financial Policies**

Until 1976, Botswana used the South African Rand as its national currency which shielded it monetarily and financially from the needs of a national currency. Though unintentional, this transitional period enabled the country to develop requisite skills and experience before assuming control over a national currency. This seems to have largely offset the negative effects of its accumulated foreign reserve being retained and used in South Africa during the decade.<sup>124</sup> More problematic was the dominance in the Botswana banking sector by South African subsidiaries of transnational banks, which were able to dictate interest rates in the absence of government control with significant consequences for the economy. Most credit from the banks went to the mining and cattle sector (the externally-focused sectors) while that to other sectors was low, thus deepening the imbalance in the economy.

Monetary and financial policy thus began only in 1976, with the adoption of the Pula as Botswana's national currency and the establishment of a central bank. The policies were aimed at curbing "excessive reparations through transfer pricing, abnormal

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<sup>124</sup> Neva Makgetla, "Finance and Development: The Case of Botswana," *The Journal of Modern Africa Studies* 20, no. 1 (March 1992): 72.

interest rates.”<sup>125</sup> The government adopted measures to limit banks’ legal remittances abroad to profits and interest and domesticate capital accumulation in the Bank of Botswana.<sup>126</sup> However, the continuing lack of control over tariffs under SACU, the linkages between the transnational banks and the mining industries, and the size of the economy constrained the effectiveness of the policy in the early years. For instance, efforts to reduce the contagion of the inflation from the South African economy through devaluation of the Pula had minimal impact.<sup>127</sup>

Given the liberal economic disposition, the government allowed exchange rates to be determined by the market, with private banks appointed as dealers in foreign exchange. This guaranteed a true value of the currency. Given capital scarcity, neo-liberal theory would suggest that the market would allocate capital surpluses efficiently and thus drive economic development. However, it did not. Between 1976 and 1980, deposits in the Bank of Botswana rose from P47 million to P128 million, while foreign reserves accumulated, reaching eight months worth of imports.<sup>128</sup> Capital sat idle because of the size of the local market, lack of requisite skills, and proximity of a bigger and more viable market. The failure of the market to move accumulated financial resources led to the initiation of the Financial Assistance Program (FAP) in 1982. The state used the program to maximize the investment of accumulated surpluses in new areas of the economy, especially the industrial sector, through financial support.

Meanwhile, the Botswanan government used grants, foreign aids and soft loans — instead of its own accumulated surpluses — to finance infrastructural development in support of the mining sector. Thus, while its expenditures rose, those expenditures generated new revenues almost immediately, while at the same time stabilizing the trade balance by facilitating the growth of exports; an indication of the efficacy of good planning and management by the bureaucracy, which the African regional specialists argue over.

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<sup>125</sup> Makgetla, “Finance and Development,” 73.

<sup>126</sup> *Ibid.*, 72.

<sup>127</sup> *Ibid.*, 80-81.

<sup>128</sup> *Ibid.*, 70.

### 3. Promotion of Private Capital

Economic development strategy during this period was premised on foreign private capital investment in line with colonial practice and in recognition of a dearth in local capital. This was buttressed by the convergence of ideas between the expatriate bureaucrats and indigenous political class on the importance of market-friendly policies and individual property rights. Thus, rather than directly involving itself in the economy, the state provided capital and technical incentives and infrastructural development to promote industrialization and agriculture. The government-established statutory bodies were established to extend these services. In contrast to global practices, these statutory bodies operated but did not share in the cost of the investments.<sup>129</sup> This guaranteed the sustenance of the corporations over the long-term by promoting fiscal discipline but affected the government's ability to restructure the economy since the private sector bore the cost of new investments. This was reflected in the failure of the private sector to embark on new investments other than in the booming mining industry.

The NDB promoted indigenous investment. The institution exemplifies one of the means in which state monetary surpluses were distributed to Batswana<sup>130</sup> to boost local investment and reduce the dependence of the economy on foreign capital.<sup>131</sup> The NDB supported investments were considered too risky, costly or unattractive to private investors and banks, giving preference to infrastructural development. In contrast to Nigeria, the NDB directed support largely to small- scale agriculture and industry on commercial terms. For instance, it provided credit to the cattle-based bourgeoisie to drill or procure existing state-owned boreholes and acquire freehold farms for cattle production.

It was, however, unable to meet its obligations because a large portion of the loans were earmarked for infrastructural development. Between 1979 and 1980, the NDB had outstanding commitments of P3.7 million and P9.4 million to beneficiaries. By 1980, of the expected 60-70,000 targeted beneficiaries, only 500 received credit in the

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<sup>129</sup> Makgetla, "Finance and Development," 81.

<sup>130</sup> The Tswana comprises the predominant ethnic group in Botswana. Batswana (plural) commonly refers to all citizens of Botswana.

<sup>131</sup> Makgetla, "Finance and Development," 82.

planter/cultivator packages, indicating a failure in goals.<sup>132</sup> While the NDB focused on credit extension to the private sector, the BDC was established to facilitate industrial and services development, and the BHC to address the housing needs of private investors. Botswana avoided the pitfalls into which similar institutions in Nigeria fell, becoming involved in direct production, only to be hijacked by the urban elite and see their sustainability undermined by corruption and clientelism. However, while the institutions were sustainable in Botswana, their goals were nevertheless undermined by dearth of capital, and the inability of the government to shape the economy because of the nature of assistance granted by the statutory bodies.

The BDC was established in 1970 as a commercial enterprise. It partnered with foreign investors seeking to promote local capital's participation in agricultural and industrial development and embarking on independent projects when necessary. Pursuant to the government policy of avoiding state dependency, industries under the BDC were profit-oriented right from conception, and this was reflected in the investment profile. The profile indicates a pattern which exploits service sectors where the challenges of relevant skills and needs of the sector are not too challenging for the domestic market. Between 1970 and 1975, 11% of the projects were in industry, 10% in agriculture, 62% in estates, 1% in transport, 2% in finance and 14% in hotels/tours.<sup>133</sup> The concentration of investments in estates was intended to attract foreign capital investment.

Owing to the scarcity of funds, the initial funds for projects came from grants from Britain to maintain macroeconomic stability. The trend was reversed with the attainment of financial capacity after diamond exports took off and the Public Debt Service Fund (PDSF) was established to support future projects. The PDSF charged an interest rate of 14.6% on its loans. The result of these measures is reflected in the performance of the statutory institutions. BDC reported profits from 1972 until 1994.<sup>134</sup> The only occasion of loss was in the first year of its operation. Its sustainability was due to its commercial orientation and adherence to fiscal responsibility. The successes in this

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<sup>132</sup> Makgetla, "Finance and Development," 83.

<sup>133</sup> Samatar, *An African Miracle*, 158.

<sup>134</sup> *Ibid*, 160.

instance, again, are driven by the initial mechanisms of the state to exploit potential skills which the market failed to do. Its sustainability is due to the market-friendly design.

Other mechanisms used to boost private sector production were the ARDP, Arable Land Development Program (ALDP), and Tribal Grazing Land Policy (TGLP) of 1975. The ARDP sought to provide social services such as schools, roads, and health care in the rural areas in principle. However, the program was designed for political goals to ensure political loyalty and support of the rural areas to the ruling party prior to the October 26, 1974 elections.<sup>135</sup> It ended almost the same way it was conceived after the election because it served the political needs of the ruling party. Most projects were a year behind schedule once the ruling party achieved victory in the election. After the experience with the program, the state avoided projects that would politicize rural dwellers, ending avenues that would introduce patronage in the polity.

The ALDP was established in 1978 under the Fifth National Development Plan (1979-1985) to boost small-scale arable farming. The plan was the first concerted effort at addressing farming. Previous plans, including the Fourth NDP (1975-1980), had focused on livestock production to the detriment of arable farming. For instance, 73% of capital allocation to agriculture was earmarked for livestock development in the Fourth NDP in spite of the fact that the majority of the populace did not own cattle.<sup>136</sup> The purpose of the ALDP was to “develop [an] improved technology package and disseminate [it] at [a] subsidized cost to farmers.”<sup>137</sup> The goals were to increase food production, enhance income from food production and the curbing of rural-urban migration.<sup>138</sup> The target audience was small-scale farmers with less than ten hectares of land, who formed the majority of the productive base. Cognizance of the differences in problems confronting the farmers was noted in the intervention measures and addressed appropriately. For instance, measures used to assist farmers with draught power were different from those for farmers who did not have access to draught animals.<sup>139</sup>

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<sup>135</sup> Picard, *The Politics of Development*, 241-242.

<sup>136</sup> Ibid., 257.

<sup>137</sup> Ibid., 260.

<sup>138</sup> Ibid.

<sup>139</sup> Ibid., 298-299.

However, the incentives to increase food production were offset by the high value of the Pula against the South African Rand, which made imported food cheaper than local production. This intervention thus failed.

The TGLP represented the state's attempt to address economic and ecological transformation of the rural areas. The policy encouraged farmers to collectivize, reduced environmental degradation and commercialized grazing land.<sup>140</sup> Land was divided and designated as commercial, communal or reserved and limits were imposed on the number of cattle permitted in the grazing fields. The proceeds from commercialized lands were to be used to maintain communal lands that were free for public use.

The bureaucracy resisted the policy, however. Opponents focused on the impact of commercialization on rural dwellers. While the bureaucrats in the Ministry of Finance and Development Planning were disposed to commercialization, officials of the Ministry of Local Government and Lands were against it because they felt it would leave the rural dwellers landless and without a means of livelihood. In spite of the accommodation of the differing views, the policy did not achieve its intended goal. Limitation on stock level on grazing areas was dropped, only few cattle owners moved to commercial lands while payment of rent was shelved for three years. The failure was due to resistance from the cattle owners due to the cost of implementation and incorrect planning factors by the bureaucrats. Given the fact that most political leaders owned commercial farms and the opposing views in the bureaucracy prevailed, it can be deduced that the political and bureaucratic class are somewhat independent of one another, in contrast to the Nigerian case. The emanation of initial resistance from within the bureaucracy equally suggests the independence and competence of the institution.

Overall, efforts to boost agricultural production had mixed results. Cattle production rose from 132,232 heads in 1966 to 140,783 heads in 1980 having peaked at 229,000 in 1979,<sup>141</sup> while crop production fell from 111.1 metric tons in 1974 to 8.5 tons

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<sup>140</sup> Robert Curry, "Adaptation of Botswana's Development Strategy to Meet Its Peoples' Needs for Land, Jobs: the Southern African Capitalist Democracy Can Maintain Its Growth by a New Problem-Oriented Policy," *American Journal of Economics and Sociology* 45, no. 3 (July 1986): 301.

<sup>141</sup> Samatar, *An African Miracle*, 110.

in 1979, but rose to 44.8 in 1980.<sup>142</sup> The sharp decline in 1979 was due to drought. On the whole, the contribution of agriculture to the GDP declined from 39% in 1966 to 24% in 1976 before the drought. The boost in cattle production resulted from the incentive structure provided by the policy, the lack of state involvement in production, and the decision not to impose taxes or extract rents from the industry. Likewise, the slight increase in agricultural output was due to renewed focus on arable farming under the ALDP.

It is obvious that the close link between the state and cattle interest, and thus political rather than economic considerations, undermined arable farming. The political leaders in Botswana evolved from the traditional ruling class, whose economic interests the traditional and inherited capital economy favored. This contrasts sharply to Nigeria, where the political class largely evolved from the administrative staff of the colonial state, and sought to acquire economic power to challenge the traditional political class.<sup>143</sup> For them, rent-seeking through the state was the primary source of wealth creation. For the ruling class in Botswana, in contrast, wealth accrued from their cattle businesses, and thus policy reflected the economic rather than the political interests of the elite. This in turn served the economic interests of the state and its citizens overall, through support to the cattle sector. The success in the Botswana is primarily due to the fact that the institutions were addressed as commercial enterprises and limited to infrastructural development. This approach guaranteed the sustainability of state institutions, avoided the dependence of investments on the state, and ensured the competitiveness of the investments. In addition, the evolution of the business and political class fostered convergence of economic interest.

#### **4. Bureaucracy**

The gains and developments achieved by the state were driven by, and dependent upon, the nature and policies of the bureaucracy. Rather than indigenizing the civil service rapidly following independence, the government decided to retain its expatriate administrative staff and gradually “localize” it as local skilled administrators became

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<sup>142</sup> Robert Curry, “Mineral-Based Growth and Development-Generated Socioeconomic Problems in Botswana: Rural Inequality, Water Scarcity, Food Insecurity, and Foreign Dependence Challenge New Governing Class,” *American Journal of Economics and Sociology* 44, no. 3 (July 1985): 326.

<sup>143</sup> Kohli, *State-Directed Development*, 304.

available.<sup>144</sup> The success of the bureaucrats at negotiating the SACU agreements and Shashe mining interests reinforced the initial decision to maintain the expatriate staff, demonstrating that the expatriate-dominated bureaucracy would apply its competence in the national interests of Botswana. This was in marked contrast to other African countries, which were rapidly Africanizing their administrative staff.

Furthermore, priority was consistently given to merit and skills rather than the need to balance the ethnic composition of the state. The relative ethnic homogeneity and harmonious and inter-ethnic relations of the country likely contributed to the ability of the government to adopt such a policy. Most importantly, this policy maintained the separation of the political leaders and the bureaucrats, resulting in the independence of the bureaucracy and its relative imperviousness to political interference. This was due to the fact that the interests of the political leaders were immediately and consistently served by technocratic implementation of the state policies that promoted free market, which was dominated by their cattle interests. The strength of the institutions lay in the foundations of the expatriate staff, commitment of the political leaders and a careful building of indigenous civil service learning requisite skills from the expatriate staff and relevant institutions.

##### **5. Effects of Liberal Policies on the Economy**

The growth rate for the period rose above 10%.<sup>145</sup> Per capita income rose from \$372 in 1965 to \$1,032 in 1975.<sup>146</sup> The diversity of investments by the BDC and allocation of 50% or more of her gross domestic product resulted in high growth.<sup>147</sup> The most significant success in attracting investment was in the mining sector. Correspondingly, the sectoral share of mining in GDP rose from 0% in 1966 to 37% in 1981-82.<sup>148</sup> However, initially, owing to the law guaranteeing repatriation of profit, much of the profit was remitted to the parent company, while the government's share was held in banks in South Africa. The exercise of some monetary control provided a leeway

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<sup>144</sup> Samatar, *An African Miracle*, 79-80.

<sup>145</sup> World Bank, *Sub-Saharan Africa: From crisis to Sustainable Growth* (Washington DC: World Bank, 1989): 222.

<sup>146</sup> Ibid.

<sup>147</sup> Samatar, *An African Miracle*, 157-159.

<sup>148</sup> Curry, "Mineral-Based Growth," 478.

to shape and utilize accumulated surpluses in the economy. The increase in contribution of the mining sector to GDP and the corresponding increase in trade balance from P27 million in 1972-73 to P3 million in 1980-81 before the introduction of the Financial Assistance Program (FAP) are reflections of the efficacy of the policies choices (macroeconomic stability). This contrasts sharply in Nigeria, where the trade balance continued to decrease in spite of increased oil rents due to failure to ensure macroeconomic stability.

However, despite this dramatic growth, there was an evident lack of development in other sectors of the economy. Credit from the banks reinforced the economic structure rather than broadening it, as the market drew investment to the booming mining sector. This was only reversed by the government's intervention through the statutory bodies after 1975. The involvement of the state boosted foreign investments while shaping the direction of economic development. This brings some convergence in the arguments of the two schools with differences on the form statutory institutions should take. It is obvious that the market maximized short-term efficiency in private investment. However, it is unable to broaden the productive base. Botswana's statutory institutions and projects succeeded in doing this largely because the institutions operated as commercial ventures, while the state ensured macroeconomic stability through competent bureaucracy.

#### **F. THE 1982-2004 ERA**

While the preceding decade witnessed limited government intervention, the state took a more active role in steering the economy from 1982 with the FAP. This shift followed increasing dominance of foreign capital in the economy and the perceived need to broaden Botswana's economic base. The ALDP and other instruments of the preceding era were very much consistent with this new approach. The FAP aimed at diversifying the economy and upgrading the skills of the workforce.<sup>149</sup> It was premised on the failure of the market to diversify the productive base in spite of the available capital and appropriate incentive structures as well as the continued dominance of foreign

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<sup>149</sup> Francis Owusu and Abdi Samatar, "Industrial Strategy and the African State: The Botswana Experience," *Canadian Journal of African Studies* 31, no. 2 (1997): 280.

capital.<sup>150</sup> It sought to maximize the use of public funds in various sectors of the economy to jump-start the local private sector. The program categorized investment support into small-scale, medium-scale and large-scale enterprises (SSE, MSE, and LSE, respectively) based on the capital base. While small-scale supported investment with fixed assets of P25,000, medium-and large-scale supported investments of between P25,000 to P900,000 and in excess of P900,000, respectively.<sup>151</sup>

The FAP took cognizance of the failure of most developing countries to utilize planning, subsidies and joint ownership to stimulate industrial development. Thus, it adopted a market determined intervention mechanism, where investors made their choice, the state provided initial capital grants to viable projects, reimbursed a portion of wages and training costs for a maximum of five years.<sup>152</sup> This incentive structure gave preference to small-scale industries in rural areas, owned by women and owner-operated. By 1993, the FAP supported investments had reached 4,000 in various areas of manufacturing and agriculture.<sup>153</sup>

Unfortunately, the FAP's impact was insignificant both in reducing imports and in generating exports. Even so, most enterprises operated beyond the five years support provided by the policy, indicating that the policy was generating self-sustaining businesses. For instance, the failure rate of the SSE, MSE and LSE after the five year period was less than 50%, below international standards of 50%.<sup>154</sup> The BDC investments increased from supporting 12 firms in 1970 to 119 firms in 1996.<sup>155</sup> The FAP was evaluated and reviewed occasionally to ensure it met the set objectives. In 2001, the Citizen Entrepreneurial Development Agency (CEDA) replaced the FAP. This was premised on the inability of the FAP to meet set goals, sustainability and cost of establishing new projects, proneness of grants to abuse, fraud and administrative

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<sup>150</sup> Samatar, *An African Miracle*, 145.

<sup>151</sup> Owusu and Samatar, "Industrial Strategy," 276.

<sup>152</sup> Samatar, *An African Miracle*, 147-150.

<sup>153</sup> *Ibid.*, 150.

<sup>154</sup> Owusu and Samatar, "Industrial Strategy," 280-283.

<sup>155</sup> *Ibid.*, 157.

lapses.<sup>156</sup> Unlike the FAP, it gave loans rather than grants, in addition to entrepreneurial and management training, monitoring and mentoring.<sup>157</sup> Forty-five percent of approved projects were in the service sector, 25% retail, 13% agriculture, 10% manufacturing and 7% in estates.<sup>158</sup> The failure rate was high with few successes in the transportation and information technology sector.<sup>159</sup> This exemplifies another instance where the state has been able to shape the economy for the market to exploit, i.e., a market-facilitating state intervention. Furthermore, the ability to identify and address weaknesses in policy programs is an indication of the important role played by a competent and far-thinking bureaucracy.

The decision to conduct viability studies and give preference to owner-operated projects ensured that projects were based on skills and competencies readily available, and potentially sustainable in the economy. Likewise, providing one-time grants rather than ongoing subsidies prevented dependence on government support. However, the incentive regime failed to promote large-scale production for the local market or for export, which prevented the program from influencing the import and export portion of the economy. Nevertheless, these business ventures improved the standard of living of small-scale producers, who might otherwise have been left out of the benefits of national development. Similarly, it is obvious that given the design of the FAP, the market alone was insufficient to achieve meaningful effects in the overall economy, while state-led development could facilitate diversification. However, the form of such involvement is critical. Here again, the key to success was carefully designed, market facilitating government interventions.

### **1. Effects of State Intervention on the Economy**

The monetary and financial regimes resulted in domestic accumulation of capital, but this was insufficient in and of itself to drive economic development in the face of limited skills and incentives. The FAP sought to redress some of the imbalances, but it failed to achieve significant diversification. By 2003-04, mining constituted 34.7% of

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<sup>156</sup> Organization for Economic Co-Operation and Development (OECD), "African Economic Outlook: Botswana," 114, <http://www.oecd.org/dataoecd/11/58/36748457.pdf> (accessed January 29, 2008).

<sup>157</sup> Ibid.

<sup>158</sup> Mbabazi and Taylor, *The Potentiality*, 86-87.

<sup>159</sup> Ibid.

GDP, while manufacturing had declined from 4.7% in 1990 to 3.7% in 2003-04, and agriculture was down to less than 3%.<sup>160</sup> However, financial services, trade and tourism recorded significant growth. Tourism contributed 4% to the export sector, making it the second largest contributor after diamonds and before cattle. This was made possible by the investments in infrastructure and the hotel and tourism sectors by the BDC and the FAP.<sup>161</sup>

This general decline of agriculture is the result of the miniscule efforts to address the sector through various programs. For instance, cereal production between 1982 and 1986 was barely 10% of domestic needs, indicating a significant shortfall in target.<sup>162</sup> While arable farming declined, cattle production grew and remained profitable. By 1994, output from the company was 158,000 heads, up from 132,232 heads in 1966, with a revenue of P222,279 against P6,805 in 1966.<sup>163</sup>

State support to industrialization through the FAP achieved some successes in stimulating employment: 8,200 jobs were created between 1982 and 1993, with SSE creating 41.1%, MSE 49.5% and LSE 9.8%.<sup>164</sup> However, the objective of expanding the industrial base was not met. Indeed, manufacturing's share of GDP actually dropped from 8% in 1976 to 5.3% in 1993-94,<sup>165</sup> and 3.7% in 2003-04.<sup>166</sup> However, some diversification was achieved in the textile and metal works industries. Growth in the trade sector was facilitated by the continued membership of SACU and the monetary and financial regime. Revenue from SACU grew from P73.9 million in 1971 to P852.6 million in 1992.<sup>167</sup> Of note was government intervention in the monetary policy. Though primarily determined by market forces, the government intervened occasionally to ensure

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<sup>160</sup> OECD, "African Economic Outlook: Botswana," 106-107.

<sup>161</sup> *Ibid.*, 108.

<sup>162</sup> Makgetla, "Finance and Development," 83.

<sup>163</sup> Samatar, *An African Miracle*, 119-120.

<sup>164</sup> Owusu and Samatar, "Industrial Strategy," 280-283.

<sup>165</sup> *Ibid.*, 283.

<sup>166</sup> OECD, "African Economic Outlook: Botswana," 107.

<sup>167</sup> Balefi Tsie, "The Political Context of Botswana's Development Performance," *Journal of Southern African Studies* 22, no. 4 (December 1996): 613.

the Botswana economy remained competitive, primarily through the tools of currency devaluation and pegging the Pula to a basket of currencies.

## **G. CONCLUSION**

It is apparent that the market drove economic growth in the cattle industry due to the capacity and nature of the bureaucracy and inherent traditional antecedents of a free market. This case exemplifies the efficacy of ensuring macroeconomic stability for sectors in which the economy has a comparative advantage. However, the liberal policies failed to diversify the productive base of the economy, necessitating the state's intervention, which was also insufficient to achieve significant sectoral development. The relative success and survival of the intervention mechanism and private investments promoted by it was due to the adoption of market friendly, limited and commercialized state support. This differed significantly from the practice in Nigeria, where the state provided subsidies and held substantial equity in a large number of SOEs. Growth was recorded in the service sector where the infrastructure was available and skills requirements were lower than in manufacturing. On the whole, neither approach achieved economic development despite sustaining the world's highest economic growth rate for decades. However, Botswana's experience does demonstrate that a balance must be struck between market- and state-led approaches if any meaningful development is to be achieved. State interventions must be commercially oriented to ensure fiscal responsibility, and sustainability, and must provide support only within the shortest possible time for the market to enhance efficiency and its competitiveness. Still, Botswana, like Nigeria, ultimately failed to promote sectorally balanced economic development.

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## IV. MALAYSIA

### A. INTRODUCTION

This chapter examines the effects of the role of the state and its policies on the performance of the agricultural and industrial sectors in Malaysia from independence until the early 2000s. In particular, the chapter will examine how the policies facilitated development vis-à-vis the arguments of the neo-liberals and developmental state advocates. Malaysia first adopted liberal and later a mix of neo-liberal and state-led policies in its development strategies. Neo-liberalism formed the bedrock of development policy between 1957 and 1970. This resulted in growth in both the industrial and agricultural sectors. The adoption of state-led policies between 1970 and 1990 was premised on the accumulation of sufficient capital in the preceding years, and the need to both empower the indigenous Malays and diversify the economic base.

Unlike the previous two cases, the Malaysian approach facilitated growth in both the industrial and agricultural sectors. The economic base broadened from its dependence on agriculture to include consumer and intermediate industrial goods. Between 1999 and 2000, the role of the government in the economy was reduced in the wake of dwindling foreign direct investment while the state exercised control on the foreign exchange regime against all odds. The blend of neo-liberalists and state-interventionist policies created growth in both sectors of the economy. This suggests that economic development in developing countries such as in SSA is achievable only within a right mixture of the approaches. Unlike elsewhere, patronage did not have negative consequences on the economy, contesting the assertions of neo-liberals.

### B. BRIEF POLITICAL HISTORY

Malaysia gained independence from Britain in 1957 under a Westminster-style government. British involvement began in 1874 when the Sultan of Perak, head of one of the federating states, accepted British indirect rule.<sup>168</sup> This initiated similar action in other territories in what became known as the Federated Malay States (FMS) in 1909.<sup>169</sup>

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<sup>168</sup> Donald Snodgrass, *Inequality and Economic Development in Malaysia* (Malaysia: Kuala Lumpur, (Oxford University Press, 1980), 17.

<sup>169</sup> Ibid.

The country had been under Portuguese and Dutch administration at various times before British rule. The vastness of its mineral resources, low population and limited indigenous technology resulted in migration and settlement of Chinese, Indian and other Asians citizens. By 1931, the immigrant population outnumbered the indigenous Malay population, leading to an embargo on further immigration.

As in most developing countries, indigenous nationalist organizations formed after World War II. The United Malay National Organization (UMNO) came together in 1946 in opposition of British plans to unite the federated states under a unitary government, creating an umbrella Malay political organization. An Indian party, the Malayan Indian Congress (MIC), also formed in 1946 after the visit of the Indian Prime Minister.<sup>170</sup> The period also witnessed the emergence of a Chinese insurrection seeking political power, which was defeated by the British administration in 1953.<sup>171</sup> These actions and agitations elsewhere changed British perceptions of the situation, and led to a promise of independence in the shortest possible time. This appealed to the Malays and Indians, and undermined the Chinese insurgency. Among other things, it resulted in the formation of an alternate Chinese party, the Malayan Chinese Association (MCA), more favorable to British interests.<sup>172</sup>

During the constitutional conference of 1948, the UMNO capitalized on the absence of the Chinese and Indians to secure a good bargaining position with the British administration.<sup>173</sup> The powers of their traditional rulers were reinstated, unification of the colonies was shelved, citizenship residence requirements were extended to fifteen years, and the ability to speak Malay was added as a requirement for Malay citizenship.<sup>174</sup> Furthermore, the agreement strengthened the central government and provided for a legislative council. In 1954, the three parties merged and formed the

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<sup>170</sup> Edmund Gomez and KS Jomo, *Malaysia's Political Economy: Politics, Patronage and Profits* (United Kingdom: Cambridge University Press, 1997), 12.

<sup>171</sup> Snodgrass, *Inequality*, 21.

<sup>172</sup> Gomez and Jomo, *Malaysia's Political Economy*, 12.

<sup>173</sup> Snodgrass, *Inequality*, 20.

<sup>174</sup> *Ibid.*, 21.

Alliance Party.<sup>175</sup> The agreement formed the basis for the constitution of Malaya in 1957 and Malaysia in 1963. The Malays and Chinese/Indians negotiated the political and economic direction of the country, based on Chinese/Indian dominance in the economic realm and Malay dominance of political power. They agreed to institutionalize citizenship to all who were born in the country before August 31, 1957, and to adopt Malay institutions, religion and symbols for the state.<sup>176</sup> In the election of 1955, the Malays won most political posts with a small number going to the Chinese and Indians. However, Chinese and Indian political involvement has risen consistently under the democratic regime that has remained in place since independence.

### **C. POLITICAL ECONOMY**

Tin and gold mining were the mainstay of the economy in the nineteenth century. Trade in minerals was facilitated by the British East Indian Company.<sup>177</sup> Control was, however, exercised by the traditional chiefs through taxes. Exploration was enhanced by the introduction of new technology by the Chinese and British and increased global demand. While tin boomed in the nineteenth century, the demand from the automobile industry in the United States transformed rubber production into an export commodity in the early twentieth century. Production was facilitated by the establishment of very profitable plantation farms by European investors. Rubber plantations paid dividends of between 225% and 375%.<sup>178</sup> In response to the shortage of local labor, the colonial administration encouraged the migration of Chinese and Indians to fill the needs of the plantations and emerging industries. To facilitate export, the administration also constructed rail and road networks. These actions resulted in the creation of a wage labor market, international trade and some semblance of capitalism in the colony.

The depression of 1932 exposed the imbalance in the economy (dependence on the global market and reliance on export of only a few primary products). This led to regulation of exports as a mechanism of influencing global prices (achievable because Malaysia produced half of the worlds supply of rubber) and diversification of the

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<sup>175</sup> Bryan Ritchie, "Politics and Economic Reform in Malaysia," (working Paper 655, William Davidson Institute, February 2004), 6-7.

<sup>176</sup> Ritchie, "Politics and Economic Reform," 46.

<sup>177</sup> Snodgrass, *Inequality*, 16.

<sup>178</sup> Gomez and Jomo, *Malaysia's Political Economy*, 13.

economic base to include rice production.<sup>179</sup> Rice production was facilitated by the construction of infrastructural facilities, research and extension services.

Promoting rice also assuaged resentment among the indigenous Malays by enhancing their financial power through rice cultivation. In the 1950s, the economy was controlled 100% by foreign capital. The Europeans controlled 60% of the tin industry while the Chinese controlled the remaining 40%. In addition, Europeans controlled 83% of rubber plantations while the Chinese controlled most of the rest (14%).<sup>180</sup> This dependence on foreign capital resulted in capital flight through repatriation of profits of M\$ 844 million between 1955 and 1961.<sup>181</sup> This was largely driven by European investors. It was with this market economy dominated by foreign capital and trade that the country was granted independence in 1957.

#### **D. ECONOMIC AND DEVELOPMENT POLICIES**

Malaysia has grown from being an exporter of rubber and tin to an exporter of manufactured industrial goods. This achievement was facilitated by inherited and adopted policies, which resulted in increased local capital and investment in the economy. Three distinct eras are identifiable in the evolution of economic policy. The first twelve years (1957-69) were a period of market-driven growth with limited government intervention in the economy. The next twenty years (1970-90) saw significant government intervention, and the period since 1997 has seen a reversal in some of the intervention mechanisms adopted in the preceding two decades, and a mix of liberal and interventionist policies.

#### **E. THE 1957-1969 ERA**

Pursuant to the compromise agreement between the nationalities in the 1957 constitution, the state initially pursued a predominantly liberal policy and rural development plan using state instruments to shape the economy in ways in which the market takes precedence. This was based on an open market driven by foreign private capital. The state encouraged and supported industrialization with infrastructural development, extension of credit facilities and protection to “infant industries.” Unlike

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<sup>179</sup> Snodgrass, *Inequality*, 18-19.

<sup>180</sup> Gomez and Jomo, *Malaysia's Political Economy*, 13-14.

<sup>181</sup> *Ibid.*

most developing countries, it did not get involved in direct production.<sup>182</sup> Its First and Second Malaya Plans of 1955-65 and First Malaysia Plan (FMP) of 1966-70 focused on infrastructural development, allocating over half of capital expenditure to the sector with the goal of facilitating private investment.<sup>183</sup>

### **1. Promotion of Private Capital**

The promotion of local private capital was facilitated by adherence to the compromise agreement that the economy be private sector-driven. This was tacitly instituted in the FMP, which limited the government's role to infrastructural development of rural areas and a commitment to favorable fiscal, monetary, and trade policies. The Pioneer Industries Ordinance of 1958 and assurances/guarantees on nationalization and free repatriation of capital and profits promoted badly-needed foreign investments.<sup>184</sup> The ordinance accorded investors incentives on taxes, labor, export and location. New labor-intensive industries were granted tax relief of 40% on profits for 2-5 years depending on the size of the initial investment.<sup>185</sup> Investments in excess of \$250,000 were granted a five-year tax exemption. Furthermore, the policies offered infant industries temporary protection to shield them from competition.<sup>186</sup>

By the late 1960s, the development strategy had not achieved an increased in domestic participation and backward linkage among other things. Although foreign capital investments grew, most companies established subsidiaries utilizing imported raw materials and semi-finished products rather than utilizing local inputs.<sup>187</sup> The products were produced for the domestic market, following the incentives created by the tariff regime. The net result of these policies was a deepening of the poor linkage between the agrarian and industrial sectors and dependence on export of primary agricultural produce. Similarly, the number of employees was far below the expected target because the

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<sup>182</sup> Gomez and Jomo, *Malaysia's Political Economy*, 16.

<sup>183</sup> Ibid; and Snodgrass, *Inequality*, 50-53.

<sup>184</sup> N Karunaratne and M Abdullah, "Incentive Schemes and Foreign Investment in the Industrialization of Malaysia," *Asian Survey* 18, no. 3 (March 1978): 263.

<sup>185</sup> Snodgrass, *Inequality*, 207.

<sup>186</sup> Ritchie, "Politics and Economic Reform," 9.

<sup>187</sup> Gomez and Jomo, *Malaysia's Political Economy*, 17.

industries generated few jobs. The result of the policies underscores the consequences of such trade structure and ISI, an argument neo-liberals assert against such policy choices.

Given the failure of the policies and exhaustion of ISI, the government shifted emphasis to export-oriented industrialization (EOI). EOI was institutionalized through the Investment Incentives Act of 1968. The earlier incentives under ISI were retained in addition to the new strategy. The act aimed to stimulate industrialization, diversify the economy, and most importantly, reduce imports and increase exports.<sup>188</sup> The incentives included tax holidays for eight years, an income tax, and import duties exemptions.<sup>189</sup> Correspondingly, a new tariff regime was instituted to protect the production of consumer goods for the domestic market. By 1970, foreign involvement in the economy stood at 60.7% with ethnic Chinese, Indian and Malay controlling 22.5%, 15% and 1.9%, respectively. This is to be expected given the preference for foreign capital. By 1970, the contribution of agriculture to GDP had fallen from 40% in 1960 to 31%, while manufacturing rose from 9% to 13%.<sup>190</sup> However, tin and agricultural exports still accounted for about 80% of foreign exchange earnings.<sup>191</sup> The decline in agricultural share was due to an increase in the contribution of manufacturing and other sectors and a fall in global prices of rubber, not a decline in production. Similarly, the continued dominance of tin and agricultural exports reflected the consequences of ISI (exports under EOI was in its infancy) in increasing manufactured production for the domestic market through most of the decade, consistent with the arguments of the neo-liberals on the effect of tariff protection on the economy. The increases in foreign private capital investments were not necessary due to market forces, but by state intervention. However, the results of the interventions were unable to contribute significantly to the economy. Also obvious is the fact that the market only exploited areas of comparative advantage, in this case agricultural production.

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<sup>188</sup> Joseph Wood, "The Colonial Economy, 1967: The Case of Malaysia," *Asian Survey* 9, no. 6 (June 1969): 443.

<sup>189</sup> Gomez and Jomo, *Malaysia's Political Economy*, 19-20.

<sup>190</sup> *Ibid.*, 41.

<sup>191</sup> Daniel Charette, "Malaysia in the Global Economy: Crisis, Recovery and the Road Ahead," 5. [http://www.dai.com/pdf/Malaysia\\_in\\_the\\_Global\\_Economy.pdf](http://www.dai.com/pdf/Malaysia_in_the_Global_Economy.pdf). (accessed January 29, 2008).

## 2. Infrastructural Development

Malaysia also pursued infrastructural development to stimulate private sector investment in the economy. This covered both urban and rural areas. While rural development was geared towards boosting agricultural production and enhancing the economic power of Malays, urban development targeted infrastructural support to foreign capital investment. Thus, the state allotted a significant portion of expenditures in the first three development plans to infrastructural development (52%, 46% and 32%, respectively).<sup>192</sup>

Rural development was geared towards reducing inequality, stimulating economic development and diversifying the economic base. It entailed direct and indirect interventions, including the establishment of statutory institutions, provision of extension services and improvement of the infrastructure. The most concerted government effort in rural development was through the Federal Land Development Authority (FELDA), which evolved from a coordinating and financing scheme to a direct player in agricultural production and development.<sup>193</sup> It established farming settlements with the necessary infrastructure and relocated rural dwellers to the settlements. The farms were managed by the authority and operated by the farmers until the cost of establishment was off-set by the farmers. As a result of the program, oil palm production increased as the world price of rubber was declining. Communal buy-in was enhanced through the payment of wages in exchange for labor. FELDA paid M\$400 per family per month, which was above the average wage income during the period.

Given all of this, it is clear that the state used a dual approach to stimulate agricultural production. On one hand, it owned settlements and farms which it used to shape and direct agricultural production. On the other hand, it avoided it becoming a burden on the state by selling to the farmers. Thus, the expectation that the farms would eventually be owned by the farmers shifted the source of revenue from the state to the farms and its produce, thereby ensuring they were sustainable for the long-term. This reveals a blend of policies from the two schools, an approach which met with significant success. Oil palm acreage had increased from 100,000 acres in the 1950s to 675,000 in

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<sup>192</sup> Snodgrass, *Inequality*, 50.

<sup>193</sup> *Ibid.*, 176-178.

1970, while rubber declined from 2 million to 1.5 million acres.<sup>194</sup> Likewise, rice production rose by 150% from the early 1950s to the early 1970s.<sup>195</sup> While state involvement in production had undermined development in Nigeria, the reverse was the case in Malaysia. The effects of the policies diverged between the countries because in Malaysia the policies ensured that state involvement was relinquished to the farmers, who were treated as part-owners. Moreover, Malaysia avoided providing grants or subsidies to the farmers, thus reducing avenues of fraud or corruption. In addition, the provision of the settlements and wage served as an incentive to buy-in.

### **3. Bureaucracy**

Malaysia inherited a fairly competent bureaucracy, unlike Nigeria. The bureaucracy was indigenized gradually, ending in 1970.<sup>196</sup> The colonial administration implemented a difficult promotion program and slow system that ensured limited progression of Malaysians (in the junior service) to the senior cadre largely occupied by the Britons. Thus, reasonable skills and some specialization were achieved prior to 1948, when the British began to gradually transfer decision-making to indigenous leaders. This ensured that indigenous civil servants acquired relevant skills before assuming full responsibility for policy making. More so, the federal system of government ensured that Malaysians learned to work together across ethnic divides prior to independence.

The bureaucracy in Malaysia has never been independent of the political class due to the antecedents. It serves as an instrument of UNMO-led Malay economic advancement and political dominance of the country.<sup>197</sup> For instance, the first-generation of political leaders were initiated into governance through the colonial bureaucracy. The import of this close link manifested in the close link between the two classes following state intervention in the economy. Efforts to curtail weaknesses and abuse of office through institutional and procedural mechanisms such as the Anti-Corruption Agency

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<sup>194</sup> Snodgrass, *Inequality*, 173.

<sup>195</sup> *Ibid.*, 185.

<sup>196</sup> Gayl Ness, "Modernization and Indigenous control of the Bureaucracy in Malaysia," *Asian Survey* 5, no. 9 (September 1965): 469.

<sup>197</sup> Hong-Hai Lim, "Ethnic Representation in the Malaysian Bureaucracy: The Development and Effects of Malay Domination," *International Journal of Public Administration* 30, no. 12 (October 2007): 1507.

(ACA) and Auditor Generals Office (AGO) were not successful.<sup>198</sup> The failure is due to the close link between the civil servants and the political class, shortage of necessary skills and manpower in the ACA and AGO, slow bureaucratic processes and dependence of these institutions on the state.<sup>199</sup>

#### **4. Implication of Liberal Policy Regime on the Economy**

By the end of 1969, government interventions and private sector investment had produced significant development. Manufacturing share of GDP rose from 9% in 1960 to 13% in 1970, though mining stagnated at 6% while agriculture declined from 40% to 31%.<sup>200</sup> In the export sector, oil palm increased from 2% to 4% and tin from 17% to 25%, while rubber declined from 63% to 44% between 1956-60 and 1966-69.<sup>201</sup> Earnings from export rose from US\$0.842 million in 1961 to US\$1.368 million in 1970.<sup>202</sup>

#### **F. THE 1970 – 1986 ERA**

Beginning in 1970, the state intervened more actively in the economy through the Outline Prospective Plan, otherwise called the New Economic Policy (NEP). The policy reflected the state's perception of development as an instrument of social change, and it equally reflected in its implementation.<sup>203</sup> The new goals were the eradication of poverty, reduction of inequality between rural and urban areas in general, and Malays and non-Malays in particular. The policy shifted emphasis from rural agricultural production to urban non-agricultural development, and redistributed state resources to cater for Malays. Consequently, public expenditure rose from M\$4.6 billion in the First Malaysia Plan (1966-70) to M\$10.3 billion in the Second Malaysian Plan (1970-1975), and M\$31.1 billion in the Third Malaysia Plan (1976-1980).<sup>204</sup> The state established various enterprises, regulatory and statutory authorities, and promoted export-oriented industries

<sup>198</sup> Noore Siddiquee, "Public Accountability in Malaysia: Challenges and Critical Concern," *International Journal of Public Administration* 28, (February 2005):118.

<sup>199</sup> Ibid., 115-118.

<sup>200</sup> Gomez and Jomo, *Malaysia's Political Economy*, 41.

<sup>201</sup> Ibid., 18.

<sup>202</sup> Mohammed Yusoff, Fauziah Hasan and Suhaila Jalil, "Globalization, Economic Policy, and Equity: The Case of Malaysia," <http://www.oecd.org/dataoecd/54/49/2682426.pdf> (accessed January 24, 2008).

<sup>203</sup> Martin Rudner, "Changing planning Perspectives of Agricultural Development in Malaysia," *Modern Asian Studies* 17, no. 3 (1983): 417.

<sup>204</sup> Gomez and Jomo, *Malaysia's Political Economy*, 31.

by encouraging foreign investments in those sectors. The interventions were driven by the Industrial Coordination Act and the Capital Issues Committee established at the end of the decade.

### **1. Public Sector**

Direct involvement in production in some industries strengthened the government's role in the economy. Interventions in the public sector were made through the Capital Issues Committee established in 1968, as well as newly established development and statutory organizations, and through the Industrial Development Act of 1974. Three categories of SOEs were established; department enterprises, statutory bodies and limited companies. Department enterprises provided public services, while statutory bodies enhanced Malay participation in the economy through institutions like the Malaysian Industrial Development Authority (MIDA) and Muda Agricultural Development Authority (MUDA). The managers of these businesses were Malay elite from the royalty or former civil servants.<sup>205</sup>

The government participated in the economy primarily through a national corporation, Perbadanan Nasional Bhd (Pernas). The Ministry of Finance established Pernas as a trust holding company for Malays. Pernas acquired equity in publicly listed companies in partnership with foreign investors focusing on export manufacturing industries, resource-based industries, banking and some high technical industries.<sup>206</sup> By 1975, Pernas' fully-owned investments were in excess of M\$100 million, while its associate companies (partnership ventures) had about M\$380 million.<sup>207</sup> By the end of the decade, it had stakes in major investments with a peak profit of M\$179 million.<sup>208</sup>

The Industrial Coordination Act of 1975 represented the height of efforts to promote industrialization and empower Malays. The act provided for 30% equity participation reserved for Malays in unexempted companies and segregated economic development along ethnic/race lines due to the preferential treatment. In addition to using Pernas to acquire equity in companies, the government repealed or relaxed laws

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<sup>205</sup> Snodgrass, *Inequality*, 221.

<sup>206</sup> Gomez and Jomo, *Malaysia's Political Economy*, 32.

<sup>207</sup> Snodgrass, *Inequality*, 218.

<sup>208</sup> Gomez and Jomo, *Malaysia's Political Economy*, 33.

that had prevented state economic development corporations (SEDC) from participating in direct production and borrowing funds from overseas. The corporations which had hitherto limited their activities to providing infrastructural facilities in line with previous policies now embarked on direct production in manufacturing enterprises and acquired equity on behalf of the Malays. The dominance and hegemony of UNMO, increasing intervention of the state in the economy, profitability of industries and tacit advancement of the Malay participation led some investors to lobby politicians and bureaucrats for access to state rents. In addition, others sought protection from foreign competition, allocation for licenses, subsidies and monopoly rights in return for offers of discounted stock options and directorship on boards of companies.<sup>209</sup> This saw the introduction of rent-seeking and patron-client networks in the polity.

Given the increased involvement of the political class in policy making, concern about Chinese domination of the economy and the need to redistribute wealth, patronage, corruption and cronyism soon became prominent. The state's more direct involvement, as opposed to its indirect influences in previous years, had created avenues for rent-seeking that had previously been absent. For instance, Pernas bought a 40% stake in the third largest bank, United Malaysia Banking Corporation, from the Minister of Finance under questionable circumstances following the recession of the 1980s.<sup>210</sup> Likewise, the company sold some of its stake in a profitable enterprise under questionable circumstances to a protégé of the minister.<sup>211</sup> In another regard, ethnic Chinese elites began to use Malay-owned fronts to protect their investments from government take-over. The net effect of these interventions was the introduction of patronage, rent-seeking and cronyism in economic development.

Unlike Nigeria, however, the SOEs were profitable and the performance of manufacturing increased from 13% share of GDP in 1970 to 26% in 1989.<sup>212</sup> This result provides further insight into how and when patronage impacts negatively on the economy, considering the circumstances and origin of its establishment in both countries.

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<sup>209</sup> Gomez and Jomo, *Malaysia's Political Economy*, 41.

<sup>210</sup> *Ibid.*, 33.

<sup>211</sup> *Ibid.*

<sup>212</sup> *Ibid.*, 41.

In Nigeria, patronage predated the state intervention of the 1970s and was facilitated by inherent traditional practices and the decentralized state structure.<sup>213</sup> For instance, the colonial administration ruled through the traditional chiefs in Northern Nigeria, while it adopted relative higher level of direct rule through very few expatriate staff in a greater part of Southern Nigeria, resulting in very weak government institutions. Traditional chiefs were used to extract taxes through a system of rewards by the colonial administration rather than through formal institutional mechanisms, thus, encouraging a patron-client relationship. In addition, the institutionalization of weak central and strong regional governments (along ethnic lines) prior to independence deepened the inherent weaknesses and created pull on the centre.

In Malaysia, on the other hand, patronage was introduced by state intervention but the complimentary relationship between the political and bureaucracy class and the nature of the state as a whole reduced any negative effect it could have had. Malaysia was a federal state with a strong central government prior to and after independence unlike Nigeria. Most importantly, the first generations of political leaders in Malaysia evolved from the bureaucracy unlike Nigeria where it evolved as a different institution independent of the bureaucracy. In addition, though the bureaucracy was relatively weak, it received tutelage from the colonial administration through a slow system that ensured requisite skills and competence are imbibed by Malays. Furthermore, indigenization of the bureaucracy was gradual lasting about 13 years unlike Nigeria which indigenized the institution on attainment of independence. This suggests that patronage does not have dire consequences on an economy if the bureaucracy is relatively strong and the political structure of the state does not facilitate regional or ethnic divides. Pursuant to the goals of OPP, additional statutory and regulatory bodies were established, including the Urban Development Authority (UDA) and the Credit Guarantee Corporation (CGC).<sup>214</sup> These organizations also sought to empower Malays pursuant to the NEP. The consequence of the interventions was an increase in public

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<sup>213</sup> Kohli, *State-Directed Development*, 301-309.

<sup>214</sup> Snodgrass, *Inequality*, 214.

expenditure from M\$137 million between 1966 and 1970 to M\$564.6 million between 1971 and 1975, and M\$1.16 billion between 1976 and 1980.<sup>215</sup>

## **2. Promotion of the Private Sector**

The state continued with the policy of the private sector driving economic development and increased its involvement in shaping the economy. However, preference was still given to foreign capital due to ethnic Chinese dominance of domestic capital. This bias continued to reinforce the dominance of foreign capital and limit the contribution of local capital. The driving policies of the period include the Capital Investment Committee (CIC) established in 1969, Labor Utilization Relief of 1971, and Industrial Coordination Act (ICA) of 1975.<sup>216</sup> While CIC promoted local capital and Malay entrepreneurship, ICA was targeted at foreign capital. The Labor Utilization Relief promoted labor-intensive industries and Malay empowerment in the midst of economic growth, in an effort to limit capital intensity of EOI industries.

The Pioneer Industrial Act established a fair number of new enterprises. However, while the state targeted labor-intensive investment, the majority of the industries established were capital-intensive, providing limited employment opportunities.<sup>217</sup> Moreover, most were situated in urban areas, while the target of the act was the rural populace. This formed the basis of the adoption of the Labor Utilization Relief. The relief encouraged labor-intensive rather than capital-intensive industries through its incentive structure. The most significant policies during the era were the Industrial Coordination Act of 1975 and the establishment of export processing zones. The Industrial Coordination Act introduced the issuance of licenses as a mechanism of coordinating and organizing the manufacturing sector in the economy.<sup>218</sup> Although the act was vague on conditions for issuance of licenses, indications were that location, market arrangement, equity structure, use of local professionals, and employment potential were key criteria for issuance.<sup>219</sup> Just like its predecessor, the act sought to enhance Malay participation in industrial development. However, it exempted some

<sup>215</sup> Snodgrass, *Inequality*, 215.

<sup>216</sup> Karunaratne and Abdullah, "Incentive Schemes," 269.

<sup>217</sup> *Ibid.*, 268.

<sup>218</sup> Snodgrass, *Inequality*, 220; and Gomez and Jomo, *Malaysia's Political Economy*, 42

<sup>219</sup> *Ibid.*

industries from adhering to earlier policy reserving 30% employment positions to Malays. The export promotion incentives included the establishment of ten export promotion zones offering free trade, tax-free operation, export insurance schemes, elimination of the NEP and Industrial Coordination Act, and offer of cheap labor through reduced wages.<sup>220</sup>

Given the discriminatory objectives of the IC Act, CIC and the statutory and regulatory authorities, most Chinese investors either patronized/established business ties with Malay elites or concealed their investments.<sup>221</sup> At the extreme, some relocated overseas, thus reducing the contribution of local capital in the economy. At the same time a new Malay entrepreneur class assisted by the state through rents, emerged in various sectors of the economy. The equity participation of Malays in the manufacturing sector rose from 41.8% in 1975 to 54.4% in 1985, while foreign ownership declined correspondingly from 27% to 17.8%, respectively.<sup>222</sup> However, just as some invested the rents positively, some abused or wasted such opportunities.<sup>223</sup> The net effect of these policies was the tacit introduction of cronyism between the political class and business class. The success of the indigenous Malays reflects some of the arguments of the development state on the use of rents. This, however, contrasts with what was obtained in Nigeria. One major difference is that while advancement of Malay interest was seen as a means to balance Chinese economic strength, a different picture was painted in Nigeria, where rents were seen as a means of sharing proceeds of state revenue. Moreover, the inherited political structure in Nigeria, rather than foster national interest or unity, entrenched the divisions along ethnic and regional lines. Furthermore, while patronage was introduced by state intervention in Malaysia, it predated state intervention in Nigeria. This suggests that it is the circumstances and origin of patronage rather than patronage itself that determines its effect on economic development.

Quite unlike the preceding development plans, the Third Malaysian Plan (1976-80) saw an increased role for private sector funding and focused on poverty alleviation of

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<sup>220</sup> Ritchie, "Politics and Economic Reforms," 13.

<sup>221</sup> Gomez and Jomo, *Malaysia's Political Economy*, 48-53.

<sup>222</sup> *Ibid.*, 43.

<sup>223</sup> *Ibid.*

all Malaysians.<sup>224</sup> It was a tacit recognition of security implications of fostering ethnic advancement in a multi-ethnic society.<sup>225</sup> The increased allocation to agriculture from M\$2.3 billion to M\$4.74 billion represented an increase from 21.7% of allocations in the Second Malaysian Plan to 25.5% in the Third Malaysian Plan.<sup>226</sup> Correspondingly, the allocation to utilities rose from M\$931 million in the Second Development Plan to M\$2.14 billion representing 9.5% and 11.9% of allocations, respectively. Of note was the lack of any increase in allocation to statutory bodies such as Pernas, UDA and MARA.<sup>227</sup> The expected contribution of domestic capital to fund the plan was M\$26.5 billion.<sup>228</sup>

For the most part, the policy remained consistent in the agricultural sector, largely because the majority of Malays resided in rural areas and the efforts of FELDA enhanced them economically. The Third Malaysian Plan increased productivity through infrastructural development like irrigation and drainage schemes for rice and increased allocation to rubber replanting from 1.6% to 3.6% in total spending.<sup>229</sup> The establishment of a commodity exchange in 1980 facilitated trade in oil palm and linked the local market more effectively to global trade to the benefit of local producers.

The new plan sought to reduce exploitation of producers by middlemen and protected consumers by introducing price controls and direct involvement in rice production in 1974. Unlike elsewhere, the prices were set above the global price to boost local production. By the 1980s, the state liberalized the agriculture sector with the First National Agriculture Policy (NAP) and extended subsidies to rural farmers. The policy sought to develop new lands while using subsidies to encourage rice farming by reducing the cost of production. This was achieved by the government bearing the cost of milling to reduce costs to consumers without reducing income to farmers. These costs were then

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<sup>224</sup> Colin MacAndrew, "The Politics of Planning: Malaysia and the New Third Malaysia Plan (1976-1980)," *Asian Survey* 17, no. 3 (March 1977): 298-301.

<sup>225</sup> *Ibid.*, 299.

<sup>226</sup> *Ibid.*, 302.

<sup>227</sup> *Ibid.*, 303.

<sup>228</sup> *Ibid.*, 304.

<sup>229</sup> *Ibid.*, 303.

off-set by the profits made from the state's monopoly on importation.<sup>230</sup> In spite of these gestures, the system was corrupted by middlemen who stifled profit to the rural farmers through illegal practices.<sup>231</sup> For instance, rice grades were mixed, price subsidies were manipulated to benefit traders and millers instead of farmers, and there are under-the-counter payments between producers and marketers.<sup>232</sup>

The effects of policies and the result of the agricultural sector support the arguments of the neo-liberals and development state alike. While the avenues for corruption meets the arguments of neo-liberals that state involvement breeds grounds for exploitation of farmers and an eventual decline in performance, the governments role in shaping and directing agricultural production justifies the development state school. It is doubtful that the success achieved in oil palm and rice production could have been made without government support. However, the choice of commercializing the project right from inception and ensuring communal buy-in reduced its exploitation for rents. Thus, it is not necessarily state intervention that ensures policy failures, but the nature of its design. State intervention (in rice, oil palm and rubber production) in this instance is market-oriented providing direct price benefit through the global price to farmers. Furthermore, it avoided (oil palm and rubber) dependence on the state by relinquishing to private investors in the shortest possible time.

### **3. Monetary and Financial Regulations**

The adoption of a fixed and predictable exchange regime by the state enhanced the EOI. The currency was pegged to a basket of hard currencies such as the U.S. Dollar, the Japanese Yen and the Euro, which invariably tied the performance of the economy to the value of these currencies.<sup>233</sup> The Plaza Agreement of 1985 between the U.S. and Japan, which led to the devaluation of the U.S. currency against the Yen, benefited the Malaysian economy because production and exports became cheap compared to Japan. This resulted in an increase in foreign direct investment (FDI) from M\$325 million in

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<sup>230</sup> James Pletcher, "Public Intervention in Agricultural Market in Malaysia: Rice and Palm Oil," *Modern Asian Studies* 24, no. 2 (May 1990): 335.

<sup>231</sup> *Ibid.*, 336.

<sup>232</sup> *Ibid.*

<sup>233</sup> Charette, "Malaysia," 11.

1986 to MR6.2<sup>234</sup> billion in 1990, and a reduction in the government's deficit budget.<sup>235</sup> Although the monetary regime boosted production and FDI in the short-term, it later became a hindrance to economic development. The economy became dependent on the relative values of the hard currencies in the international market. For instance, an agreement between the U.S. and Japan on review of their exchange rate in the mid 1990s resulted in an appreciation of the Malaysia currency, making the economy less attractive. This led to the pegging of the currency against only the dollar.

#### **4. Effects of State Activism on the Economy**

The number of SOEs increased from 22 in 1960 to 1,010 in 1985.<sup>236</sup> Within the first ten years of OPP, the average annual growth rate of the manufacturing sector was in excesses of 10%, declining to 4.9% between 1981 and 1985. By 1985, the sector contributed 19.7% of the GDP, up from 13% in 1970.<sup>237</sup> Agriculture declined from 40% to 20.8% in the corresponding period.<sup>238</sup> The relative success in state intervention was due to the limiting of the state's involvement to the shortest possible time, commercialization of such projects early in the scheme and a focus on exports. Furthermore, success was guaranteed by the competency of the bureaucracy, the complimentary relationship of the bureaucracy and the political class, and the political structure of the state which did not facilitate fractionalization

#### **G. THE 1986 -2000 ERA**

Between 1986 and 1996, the state reversed of some of the policies of NEP in favor of more neo-liberal approach, marking a tacit end to the development state policies of OPP. Some SOEs were privatized while the Investment Promotion Act was adopted in 1986 to further encourage foreign investment. The reversal was in response to the economic recession of the early 1980s and the attendant capital flight, which exposed the economy's weaknesses: vulnerability to the world market price of oil and other commodities, uncompetitive local industries, and high government expenditure due to

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<sup>234</sup> The dollar and its sign "\$" were dropped in place of Ringgit Malaysia and "RM" in the 1990s.

<sup>235</sup> Charette, "Malaysia."

<sup>236</sup> Ibid., 31.

<sup>237</sup> Ibid; and Tengku Ahmad and Ariffin Tawang, "Effects of Trade Liberalization on Agriculture in Malaysia: Commodity Aspects," (working Paper no. 46, CGPRT, Bogor, Indonesia, September 1999), 5.

<sup>238</sup> Ibid.

inadequate private sector contribution to the economy.<sup>239</sup> The exercise was based on the belief that privatization would promote competition, enhance efficiency, stimulate private entrepreneurship and reduce abuses inherent in SOEs.

### **1. Public Sector Reform**

The privatization exercise entailed the restructuring of the public sector, commercialization, privatization and deregulation of SOE and some social services. For instance, services such as packaging and garbage disposal, which hitherto were public services, were contracted out under the program.<sup>240</sup> Furthermore, telecommunications, air and road transport, and power generation were deregulated to allow private sector participation. The privatization of Pemas and management buy-out of MARA were the high points of the privatization effort and an indication of the government's commitment to the exercise. The instruments of privatization included management buy-outs, sale of government equity, and build, operate and transfer (BOT). BOT entailed private sector conception, building, and operation of some services or projects for a number of years to recover their expenditure after which ownership is handed over to the state.

The reform of the civil service was premised on weaknesses and corruption in the bureaucracy. Incidences of bribery of state officials, kickbacks and award of contracts to the politically connected and kiths and kin were rampant. This was in spite of measures to strengthen the civil service through inculcation of ethical practices and universal values and anti-corruption measures of ACA and AGO.<sup>241</sup> The ACA and AGO undermined the effort focusing primarily on petty corruption, leaving the elite and politically connected relatively free from investigation and prosecution. For instance, of the 939 arrests made by ACA between 1996 and 2000, 13 were politicians, 77 top management personnel while 810 were support personnel.<sup>242</sup>

By 1994, the work force of the state had been reduced by about 97,000 personnel while about RM10.8 billion was generated from the sale of government equity in

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<sup>239</sup> Gomez and Jomo, *Malaysia's Political Economy*, 79.

<sup>240</sup> *Ibid.*, 82.

<sup>241</sup> Siddiquee, "Public Accountability," 118.

<sup>242</sup> *Ibid.*, 119.

SOEs.<sup>243</sup> Similarly, the private sector expended RM8.2 billion on infrastructural development under the BOT, while the state reduced its debt burden with the transfer of about RM7.45 billion to the private sector.<sup>244</sup> One of the most significant outcomes of the program was the number of investments and quality of services provided by the private sector in the telecommunication and transport sector. For example, the average turn around time at the Kelang Port Container Terminal (KCT) declined from 11.7 hours to 8.9 hours within two years of its privatization. In addition, the efficiency gains of KCT increased by 53% while the revenue of Malaysia Airlines Bhd (MAS) and Sports Toto (former SOEs) rose by 22% and 11% respectively.<sup>245</sup> The privatization effort contributed to the growth of the Malaysian capital market and the strength of the Kuala Lumpur Stock Exchange, which became the largest stock market in South East Asia and the fourth largest in Asia.

While privatization enhanced the profitability of most of the companies and the country at large, the privatization process also transferred state monopolies to politically connected private investors.<sup>246</sup> Thus, a serving finance minister acquired a 10% stake in TV3, a privately owned television company granted license to operate, the gaming company Sports Toto came under the control of protégés of the royal family, and Pan Malaysian Sweeps Sdn Bhd was awarded to a close associate of the prime minister. State ownership remained high as well. As of 1995, the state held 77% of Tenaga Nasional Bhd (TNB), and a 75% stake in Syarikat Telekom Malaysia Bhd (STM), a telecommunication enterprise and Petrolia Nasional, a petroleum enterprise. It is obvious in this case that profitability and patronage resulted in growth, in contrast to what was obtained elsewhere.

Unlike in SSA, the government had conceived privatization of SOEs before the BWI encouragement. This was premised on the prime minister's belief that privatization would eliminate the subsidy mentality among Malays and his desire to make the Malaysia enterprise internationally competitive. Given this desire and the UNMO

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<sup>243</sup> Gomez and Jomo, *Malaysia's Political Economy*, 86.

<sup>244</sup> Ibid.

<sup>245</sup> Ibid., 87.

<sup>246</sup> Ibid., 87- 98.

hegemony and previous practices, it suggests that SOEs were sold to investors capable of achieving this goal. Moreover, the antecedents suggest that the goal of balancing the Chinese economic strength served to ensure the investments remain profitable.

## **2. Private Sector Promotion**

The enactment of the Investment Promotion Act in 1986 signified a renewed effort to encourage foreign capital. This followed the adoption of multi-national company-led export-oriented manufacturing prevalent among the South East Asian countries. The Act eliminated the application of the NEP and ICA requirements for industries involved in exports, and domestic investments with less than RM1 million shareholder capitals.<sup>247</sup> The high point of the effort was the liberalization of ownership and tax regulation of all firms, both foreign and domestic. This resulted in average growth of 6.4% by 1992, and achievement of full employment in 1993.<sup>248</sup>

With the economy at full employment, the New Development Policy of 1993 shifted the focus to capital-intensive manufacturing to facilitate competitiveness of local industries and reduce the cost of production. The policy sought to increase the amount of local content in foreign-owned export manufacturing, while advancing the level of technology of local and foreign firms. These objectives were facilitated by organizations like the Human Resource Development Corporation. The corporation enhanced local manpower development through the establishment of vocational and industrial training centers. Furthermore, the Malaysian Industrial Development Authority (MIDA) restructured the tax system, reducing tax exemption from 100% to 60% for firms meeting stringent requirements on technology content and sharing as a means of improving linkage between foreign and local firms.<sup>249</sup> The requirement included a minimum capital investment per employee of RM55,000, research and development expenditure of 1% of sales within three years of production, and 7% of employees with certificate or diploma in technical fields.

The most ambitious incentives were offered by the Multi-media Development Corporation (MDC), established in 1996, which created and managed a multimedia

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<sup>247</sup> Ritchie, "Politics and Economic Reform," 17.

<sup>248</sup> Ibid.

<sup>249</sup> Ibid., 20.

corridor consisting of the university and incentives to firms located in the corridor. However, the impact of these measures has not redressed the gap between available labor and requirements of foreign enterprises. These efforts to increase the skill of human capital to meet the challenges of capital-intensive enterprises have been limited by earlier failure to invest in primary and secondary education. This was due to the pursuit of Malay traditional-centered education, which does not stress mathematics, science and English education. Moreover, gains in the education sector have favored a small number of elite at the expense of the majority of the populace.<sup>250</sup>

The long-term effects of the First NAP on agriculture began manifesting during this period. The policy continued to aim at maximizing income from agriculture through efficient utilization of the state's resources and increasing productivity through land development and support services.<sup>251</sup> The most important hindrances to the attainment of the goals included labor shortages, increasing wages and the state's preference for manufacturing.<sup>252</sup> Consequently, the policy was reviewed and the Second NAP adopted a new focus on competitiveness, efficiency and linkage between agriculture and the manufacturing sector. It primarily focused on small-scale farmers. Import taxes on agricultural products were reduced while export of value added was encouraged.

### **3. Effects of the Policy on the Economy**

Manufacturing share of GDP increased from 25% in 1990 to 35% in 2000, while agricultural share declined from 18% to 8% within the same period.<sup>253</sup> Foreign direct investment increased initially from \$2.332 million in 1990 to \$5.136 million in 1997, before declining to \$1.552 million in 1999.<sup>254</sup> The decline was due to the financial crisis of 1997 which resulted in capital flight. In addition, the vulnerability of the economy, corruption, controls on capital and inadequate technical skills resulted in the loss of

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<sup>250</sup> Ritchie, "Politics and Economic Reform," 24.

<sup>251</sup> Ahmad and Tawang, "Effects of Trade Liberalization," 8.

<sup>252</sup> *Ibid.*, 9-11.

<sup>253</sup> Mun-Chow Lai and Su-Fei Yap, "Technology Development in Malaysia and the Newly Industrializing Economies: A Comparative Analysis," *Asia-Pacific Development Journal* 11, no. 2 (December 2004): 64.

<sup>254</sup> Ritchie, "Politics and Economic Reform," 31-32.

competitive attractiveness and investor confidence. Efforts to redress the shortcomings in skill capabilities and investment drive were barely adequate to sustain the achievements of earlier years.

## **H. CONCLUSION**

Malaysia adopted a predominantly liberal economy with limited state intervention after independence. The economy successfully transitioned from a producer of primary goods to an exporter of intermediate products driven by foreign capital. The government encouraged ISI initially and later adopted EOI to boost industrialization and developed a rural infrastructure to boost agricultural production. The policies resulted in substantial growth in the agricultural and industrial sectors. However, the dependence of the economy on foreign capital and its exposure to swings in the prices of primary produce in the international market resulted in greater state intervention to promote diversification of the economy. This was facilitated by the accrual of sufficient public capital in the previous period. The implementation of the policies in the immediate years of independence reflected a relative absence of patronage, while intervention led to the introduction of patronage. The state adopted a mix of neo-liberal and development state policies in steering the economy. Between 1956 and 1970, its intervention in the economy was indirect providing the relevant infrastructure to encourage private sector participation, while it took active direct intervention in the next period. This broadened the productive base and resulted in tremendous growth. This was facilitated by EOI which reduced its dependence on the export of agricultural produce, as this proved successful in the interim. Although, the intervention introduced patronage and patron-client networks into the polity, it did not undermine economic development.

The broadening of the productive base was facilitated by state-led mechanisms in the agricultural and industrial sectors. In particular, the diversification of agricultural production to include oil palm production was only attainable by virtue of state intervention given the fact that the market would most logically exploit the advantages in rubber production. Likewise, the inherent weaknesses in skills and domestic capital would certainly have favored agricultural production rather than manufacturing. This, however, became the reverse as state intervention resulted in the development and growth of the manufacturing sector. These successes were dependent on the design of the

mechanisms which were market friendly, and reduced the burden of dependence on the state. Concern on competitiveness and efficiency of erstwhile SOEs led to the adoption of neo-liberal policies. While this was successful, the Asian financial crisis exposed the dependence of the economy to international shocks and inherent weaknesses in the domestic capabilities. Within the three distinct periods, none of the approaches in and of itself was adequate to grow the economy; rather, growth was facilitated by the right mix of both approaches.

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## V. CONCLUSION

This thesis was motivated by the differences between the BWI and AU/African specialists on how economic policies within the region should be structured in the light of the acceptance of neo-liberalism by African leaders. While the AU/African specialists are more disposed to improved planning and management, the BWI remain favorably disposed to economic openness. This thesis sought to examine if improved planning and management, further opening of the economy, or a nuance combination of both result in sustained economic growth and development. The policies of the state and its effect on the economy in Nigeria, Botswana and Malaysia were examined vis-à-vis the arguments of the two approaches. While, the opening of the market ensures growth, it was unable to diversify the productive base. Likewise, improved planning and management facilitated a broadening of the productive base, but the investments that often resulted were unable to grow substantially without opening of the market. Examination reveals that neither of the two approaches alone resulted in economic development; instead, growth resulted through the adoption of a blend of both.

In Nigeria, ISI and state intervention in agriculture resulted in a decline in the performance of these sectors in the long-term, and neo-liberal policies did not result in balanced growth in Botswana, but rather deepened the dependence on the export of primary products. Conversely, ISI resulted in sustainable growth in Malaysia. In addition, while neo-liberalism deepened the dependence on export of primary export commodity in Malaysia, growth was facilitated by state intervention and not the market. On the other hand, the efficacy of neo-liberalism was uneven in the agricultural and industrial sectors in the three cases. While it resulted in improved performance in the agricultural sector in Nigeria and Botswana, its performance in the industrial sector in all three cases was doubtful. Neo-liberalism ultimately resulted in the market maximizing the short-term potential of the economy, while intervention enabled the state to shape the economy in ways that latent potentials could be created and exploited. It is evident from all three cases that neither neo-liberalism nor state-led development by itself is sufficient to stimulate economic growth and development given the inherent weaknesses in underdeveloped economies thus, necessitating a blend of the two approaches.

From the studies on Nigeria and Malaysia, it is apparent that the involvement of the state in marketing and provision of subsidies breeds avenues for corruption, reduces incentives for rural farmers, and ultimately causes a decline in agricultural production. On the other hand, the provision of infrastructural facilities, extension services and necessary inputs and materials enhanced production during the SAP in Nigeria, facilitated oil palm and rubber production in Malaysia, and boosted cattle production in Botswana. The sustainability of state institutions in Malaysia and Botswana was due to the commercial focus and time limitation on support to private investments. This resulted in shifting the sources of rents away from the state to the market, and guaranteed the sustainability of the institutions and project long-term. Furthermore, state involvement in the establishment of farms facilitated the diversification from rubber to oil palm production, beyond the expectation of the market. Similarly, though relatively successful, Malaysia's intervention in rice production ensured that production for the domestic market and economic empowerment of the Malays were met.

In all three cases, the liberalization of the sector and determination of prices by market forces encouraged rural farmers to boost production. Nevertheless, the success achieved in Malaysia suggests that when the private sector is reluctant or unable to broaden the agricultural base, the state is capable of achieving this through mechanisms that do not encourage dependence on agriculture. Thus, while the analysis suggests that state involvement in production or marketing might hinder increased agricultural production, state involvement might be necessary to direct or shift the productive base to other produce if it absolutely becomes necessary due to risks and cost to private capital. The issue is not just whether or not the state should be involved in the economy, but where and how.

Equally obvious is the fact that increasing production in agriculture is insufficient to ensure that maximum benefits are derived by the state and investors. This was evident in the export of cattle and oil palm in Botswana and Malaysia, respectively, which generated multi-fold profits to investors and significant foreign exchange for the state. In both instances, export was facilitated by the maintenance of a competitive exchange regime, while added value in Malaysia was achieved by the linkage of the agricultural and industrial sectors of the economy through state action. Conversely, in Nigeria

artificially valuing the local currency disincentivized exports. Similarly, pegging the local currency at a low value, though beneficial in the interim, could have negative consequences in the long run as was observed in Malaysia. This calls for a strong state's role when the currency exchange tends to have an opposite effect on exports. However, its prevailing value is best determined by the market, while the state intervenes only when it becomes absolutely necessary.

Given the poor linkage between the agricultural and industrial sector in all three cases in the years after independence, it is obvious that the market alone is insufficient and incapable of bridging inherent gaps. Although structural adjustment facilitated the utilization of local agricultural resources in the industrial sector in Nigeria short-term, its non-sustainability long-term revealed the inadequacies of market forces due to competing demands for export and local consumption. In Malaysia, however, the tariff regime ensured the gap between the agricultural and industrial sector was reasonably reduced while the EOI guaranteed its sustainability in the long run. To this extent, therefore, both the state and market forces have a role to facilitate agricultural production.

ISI programs proved inadequate and inappropriate to achieve economic growth in both Nigeria and Malaysia, while for Botswana, close proximity to South Africa and the weaknesses of the domestic market hampered industrial growth. However, the adoption of EOI tremendously impacted economic growth and revealed the lapses inherent in ISI. Thus, EOI is a necessity for economic growth, and must be fashioned by the state in ways that it meets its interests as was the case in Malaysia. Considering the effects of SAP on industrialization in Nigeria, the liberalization of the economy based on an ISI strategy would lead to a decline in productivity because of low comparative advantages in the local economy. However, judging from the successes in EOI in Malaysia, there must be a clear-cut objective on what the state seeks to achieve with industrialization. In Malaysia, the state utilized ISI to satisfy local consumption while using EOI to generate foreign exchange for the state. Moreover, efficiency, improved productivity and competitiveness were guiding principles in both strategies. To this extent, tariff regimes must seek to protect those industries under ISI. However, the tariff regime must be dynamic to stimulate a gradual exposure of production of low-end goods and services to competition and gear investors towards moving into the next stage of production. Thus,

it must not protect industries indefinitely. Similarly, given the competing needs for export and industrial use evident in Nigeria and role of the government in facilitating the use of local raw materials in Malaysia, a balance must be struck between these two needs. However, because the private sector is largely involved in both instances, the state is the most appropriate institution to coordinate and regulate the needs of the sectors.

The relative success achieved in Malaysia, and to a lesser extent in Botswana, was due to the direct intervention of each government in specific sectors. However, the differences between the processes in these countries were in the form of the interventions. In Malaysia and Botswana, intervention was market-friendly with measures adopted to enhance inherent potentials which could be exploited maximally by the market within the shortest possible time, while the reverse was the case in Nigeria. Malaysia commercialized such investments from inception, ensured a communal buy-in and sold to the private sector. In Botswana, the state granted loans, entrepreneurial and management training to private investors who chose their investments. Either way, the government avoided prolonged involvement in the projects and shifted the rents from accruing to the government to returning to the investment. In this regard, the state would be necessary to steer industrialization to areas not too unattractive to the private sector, with reasonable chances of successes and sustainability and with short-term public support.

For Botswana, much of the success achieved was dependent on the bureaucracy and its relationship within the polity. While independent in posture, the Botswana bureaucracy was equally competent in its responsibilities to the state. On the other hand, the same cannot be said of the bureaucracy in Nigeria. In Nigeria, the bureaucracy was weak, hijacked and connived with the political class and elite to appropriate state resources for personal benefit, contributing to decline in economic performance. Conversely, the bureaucracy in Malaysia was fairly competent and had a close relationship with the political class in Malaysia which fostered positive accumulation and utilization of rents for national interest. This suggests that the competency and nature of the relationship between the bureaucracy and political class matters. Nigeria's undue preference given to indigenous participation in spite of weak institutional capability and competing ethnic needs and lack of a unifying purpose resulted in patronage. While patronage might be difficult to eliminate and did not undermine growth, as evident from

the result of the privatization exercise in Malaysia, avenues which booster or lend credence to patronage must be reduced substantially as in the result in Nigeria under NEEDS. Furthermore, given the differences in the effect of patronage in Nigeria and Malaysia, a unifying purpose needs to be instituted among the various ethnic groups and business/political class. Equally revealing is the result of the shift of the sources of rents from the state to the private sector. It is certain that privatization does not necessarily reduce patronage.

Finally, given the spate of illegalities that bedeviled the financial and monetary sector in Nigeria and the result of NEED, it behooves the state to be capable of performing supervisory roles efficiently and effectively in the economy. This calls for the institutionalization of a competent civil service, an insight supported by the capacity and professionalism of the bureaucracy in Botswana. Furthermore, considering the effects of tariffs and monetary regulations on the competitiveness of the economy, the role of the state as a facilitator of growth cannot be under-estimated. Also, given that privatization in Malaysia resulted in private monopoly, the seeming connivance between the bureaucracy and the business class can be undermined by resorting to a fully liberalized economy with multiple players in various sectors of the economy.

From all the case studies, neither the state-led development nor neo-liberal policies by itself are sufficient to guarantee growth in the agricultural and industrial sectors in particular, and the economy in general. A blend of the two approaches would certainly stimulate economic growth and development; this suggests that the neo-liberal/development state debate is largely a false one.

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