

# International Monetary Fund

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February, 2011

## Macroeconomics of Inclusive Growth

Victor D Lledó, *International Monetary Fund*

Rodrigo Garcia-Verdu, *International Monetary Fund*



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# Macroeconomics of Inclusive Growth

Victor Lledó and Rodrigo Garcia-Verdu  
February 2011

# Outline of Presentation

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1. Definition and Rationale of Inclusive Growth
2. How Inclusive has Growth Been in Mozambique?
3. Inclusive Growth Strategies
4. Policies and Institutions for Inclusive Growth
5. Conclusion and Next Steps

# Definition and Rationale of Inclusive Growth

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- ▶ Inclusive growth is defined as growth that is sustained over several years, is broad-based across economic sectors, and creates productive employment opportunities for the majority of the country's population

## Elements of Economic Growth

- ▶ **Macroeconomic stability:**
  - ▶ Moderate fiscal and current account deficits
  - ▶ Low debt to GDP ratio
  - ▶ Low and stable inflation
  - ▶ Adequate level of reserves
- ▶ High investment and savings rates
- ▶ Openness to trade
- ▶ Enforcement of property rights
- ▶ Good governance
- ▶ Declining population growth rate

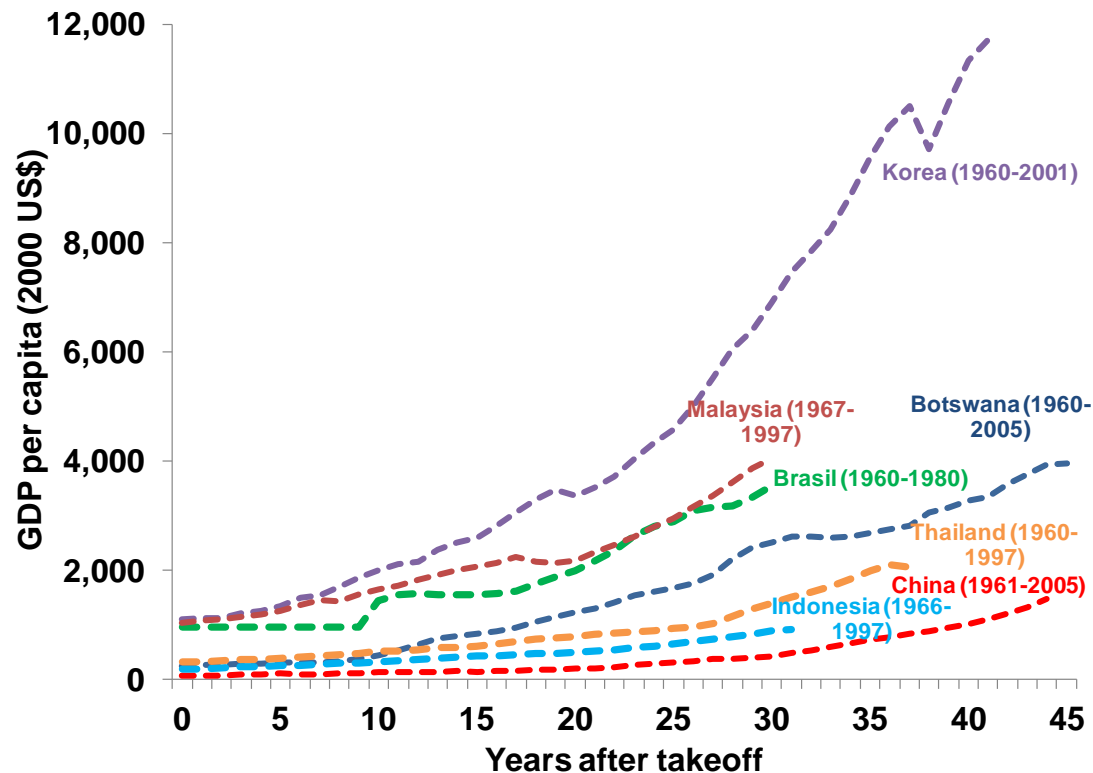
## Elements of Inclusive Growth

- ▶ High growth rates for several years
  - ▶ Sustained growth accelerations
  - ▶ Avoid growth collapses
- ▶ Structural transformation:
  - ▶ Output and export diversification
- ▶ Broad-based productive employment
- ▶ Significant reduction in poverty
- ▶ Propitious business environment
- ▶ Efficient natural resource management
- ▶ Equality of opportunity through basic education, health and infrastructure

Sources: own definition based on Commission on Growth and Development (2008), The Growth Report. Strategies for Sustained Growth and Inclusive Development, and Ianchovichina and Lundstrom (2009), "Inclusive Growth Analytics. Framework and Application," World Bank.

# Definition and Rationale of Inclusive Growth

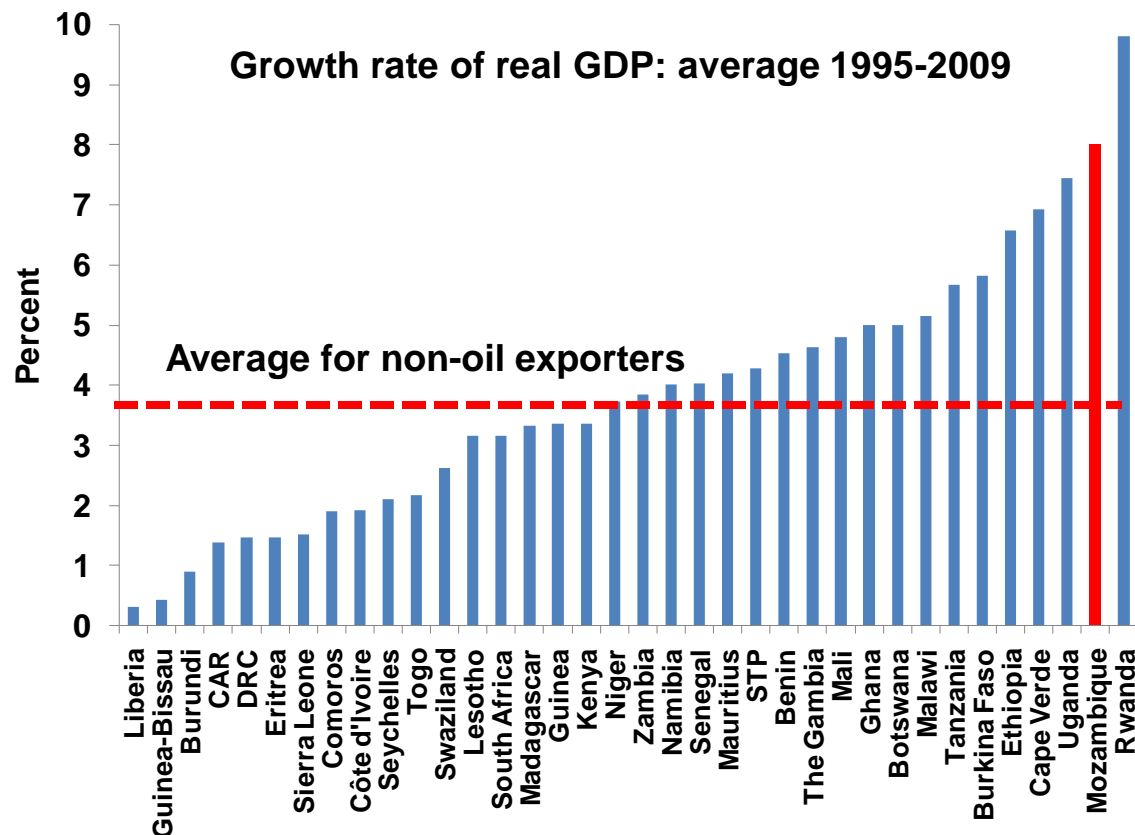
- ▶ How long should growth be sustained for? All countries considered by the Growth Commission as successful cases of Inclusive Development have sustained high growth rates for at least three decades



Source: World Development Indicators 2010. World Bank.

# How Inclusive has Growth Been in Mozambique?

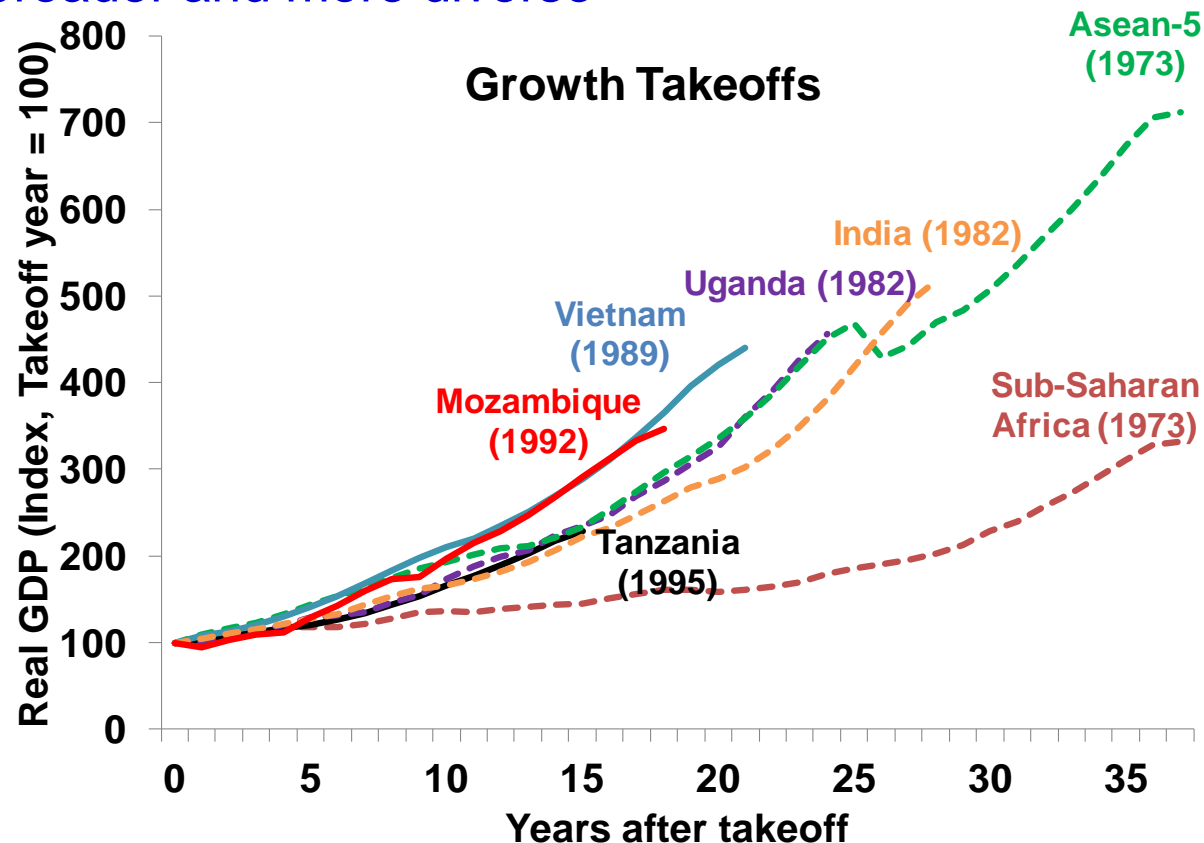
- ▶ The growth rate of real GDP in Mozambique over the period 1995-2010 has been the second highest among non-oil exporting countries in the Sub-Saharan Africa region



Source: Crispolti (2010), "Economic Growth in Mozambique. Experiences and Policy Challenges," IMF presentation.

# How Inclusive has Growth Been in Mozambique?

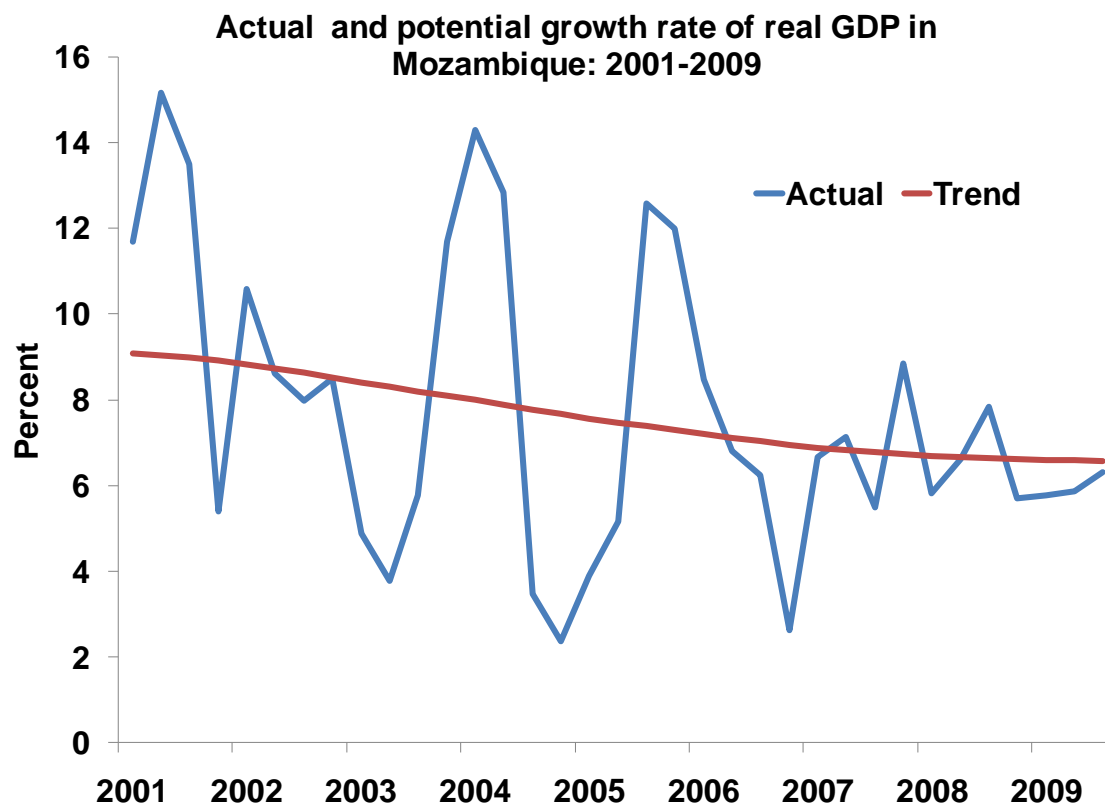
- ▶ Despite Mozambique's impressive performance over the past two decades, growth still needs to be sustained for several more years, and be broader and more diverse



Source: Clément and Peiris (2008), Post-Stabilization Economics in Sub-Saharan Africa: Lessons from Mozambique, IMF.

# How Inclusive has Growth Been in Mozambique?

- Growth also needs to be accelerated to counter a declining downward trend of potential output growth

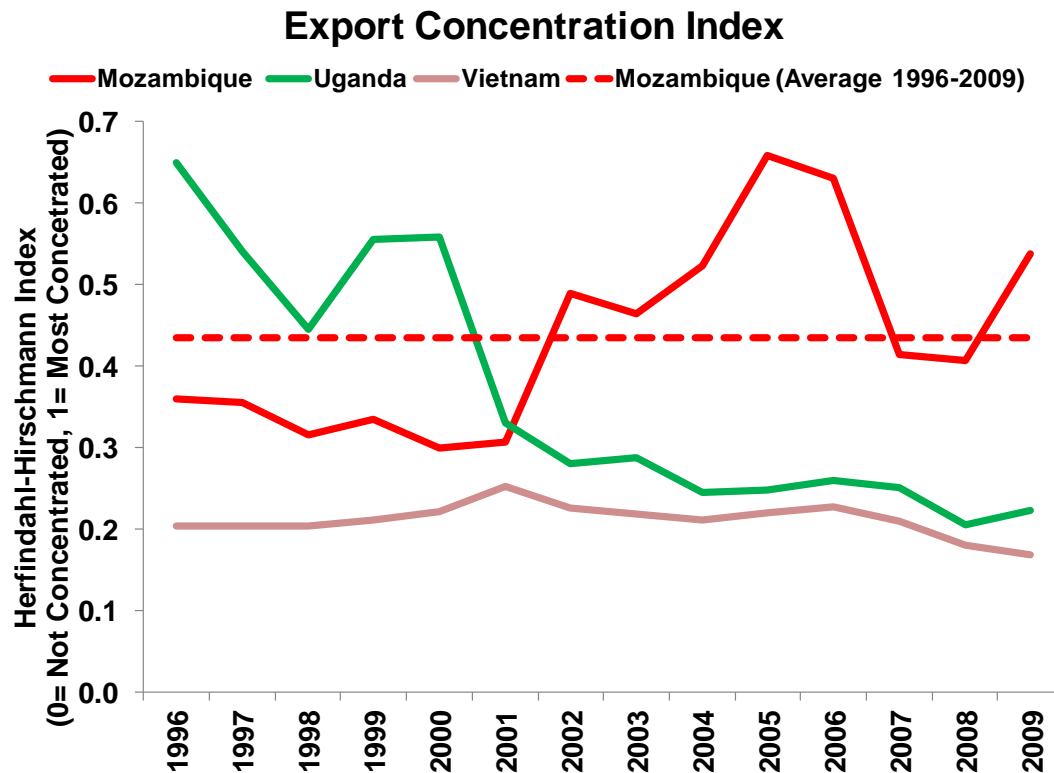


Source: Crispolti (2010), "Economic Growth in Mozambique. Experiences and Policy Challenges," IMF presentation.



# How Inclusive has Growth Been in Mozambique?

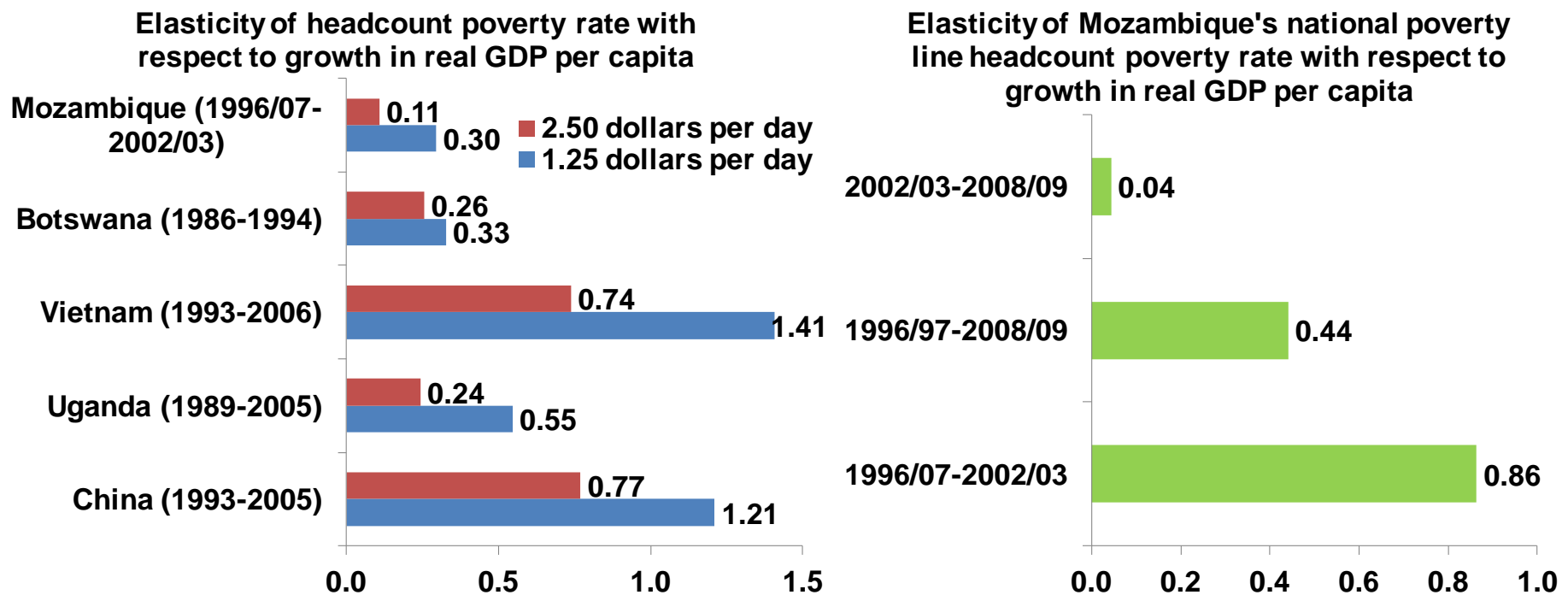
- ▶ Unlike other successful cases, Mozambique growth takeoff has not been accompanied by significant export or economic diversification. In fact the export base has become more concentrated



Source: UNCTAD-STAT, United Nations Conference on Trade and Development (UNCTAD).

# How Inclusive has Growth Been in Mozambique?

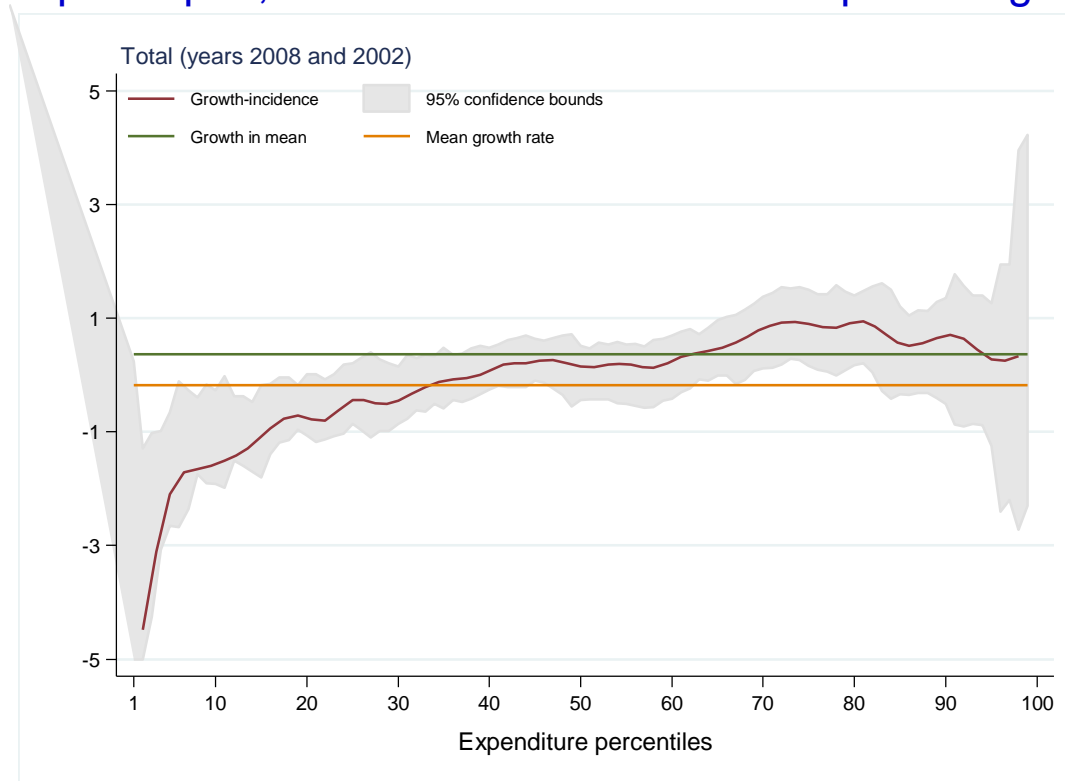
- Critically, growth in Mozambique has been less pro-poor than in other successful countries, and such pro-poor characteristics appear to be declining over time



Source: Own estimates based on data from the World Development Indicators 2010. World Bank.

# How Inclusive has Growth Been in Mozambique?

- ▶ The growth incidence curve for Mozambique also confirms that growth was not pro-poor between 2002/03 and 2008/09
  - ▶ Households in the first three deciles experienced negative growth in expenditure per capita, while others benefited from positive growth

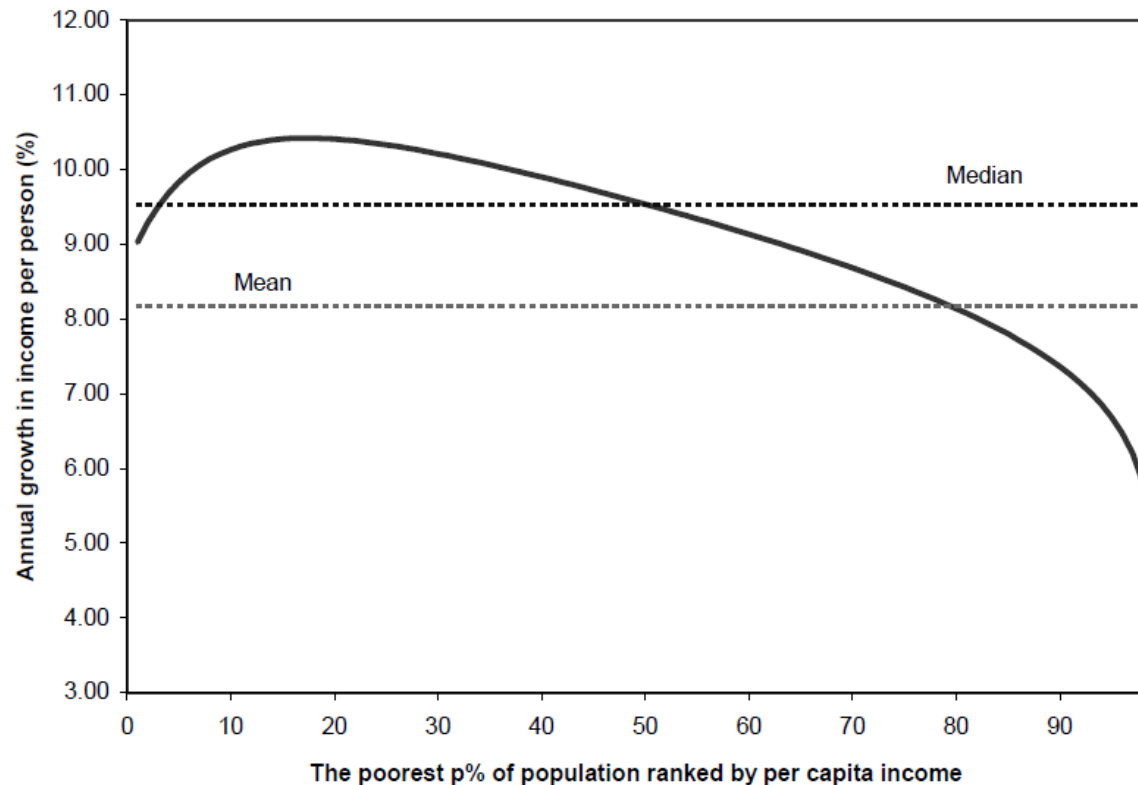


Sources: own estimates using ADePT based on data from IOF 2008-09 and IAF 2002-03.

# How Inclusive has Growth Been in Mozambique?

- ▶ In contrast, China is an example of a sustained growth country that registered a pattern of highly pro-poor growth between 1993 and 1996

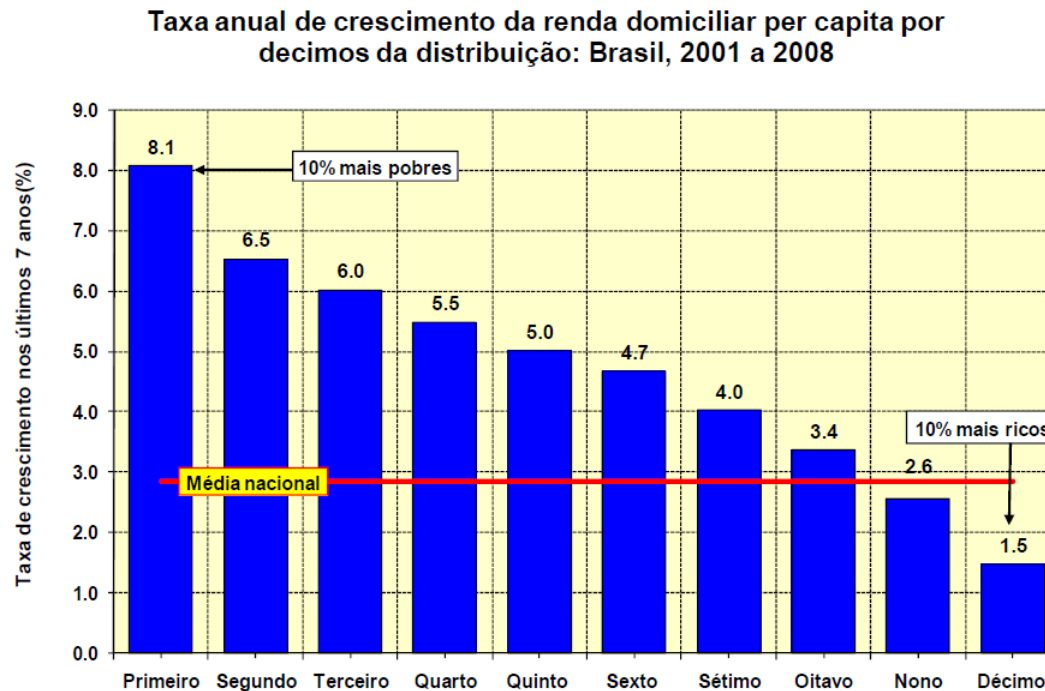
**Growth Incidence Curve for China: 1993-1996**



Source: Ravallion (2004), "Pro-Poor Growth: A Primer," mimeo, Development Research Group, World Bank.

# How Inclusive has Growth Been in Mozambique?

- ▶ Brazil is one of the countries which has registered the most progressive or pro-poor growth pattern, with the poorest households experiencing a growth rate of income per capita nearly 6 times higher than the richest households



Source: Paes de Barros, Ricardo (2009), "Sobre a Evolução Recente da Pobreza e da Desigualdade," Instituto de Pesquisa Econômica Aplicada, based on data from the *Pesquisa Nacional por Amostra de Domicílios* (PNAD), 2001-2008.

# Inclusive Growth Strategies



# Policies and Institutions for Inclusive Growth

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- In all these endeavors, Mozambique should preserve one of its key assets: Macroeconomic stability

## **Preserving Macroeconomic Stability – Key Policies**

- Pursue prudent fiscal policy that preserves debt sustainability and raise country's long-term growth factors.
- Create fiscal space through revenue effort and prudent borrowing to help finance well-targeted spending.
- Pursue prudent monetary policy to keep inflation low -> Inflation hurts the poor
- Monitor, but do NOT manage, the Real Effective Exchange Rate (REER)



## **Element**

- Avoid growth decelerations through bad policies

# Policies and Institutions for Inclusive Growth

## Key Strategies

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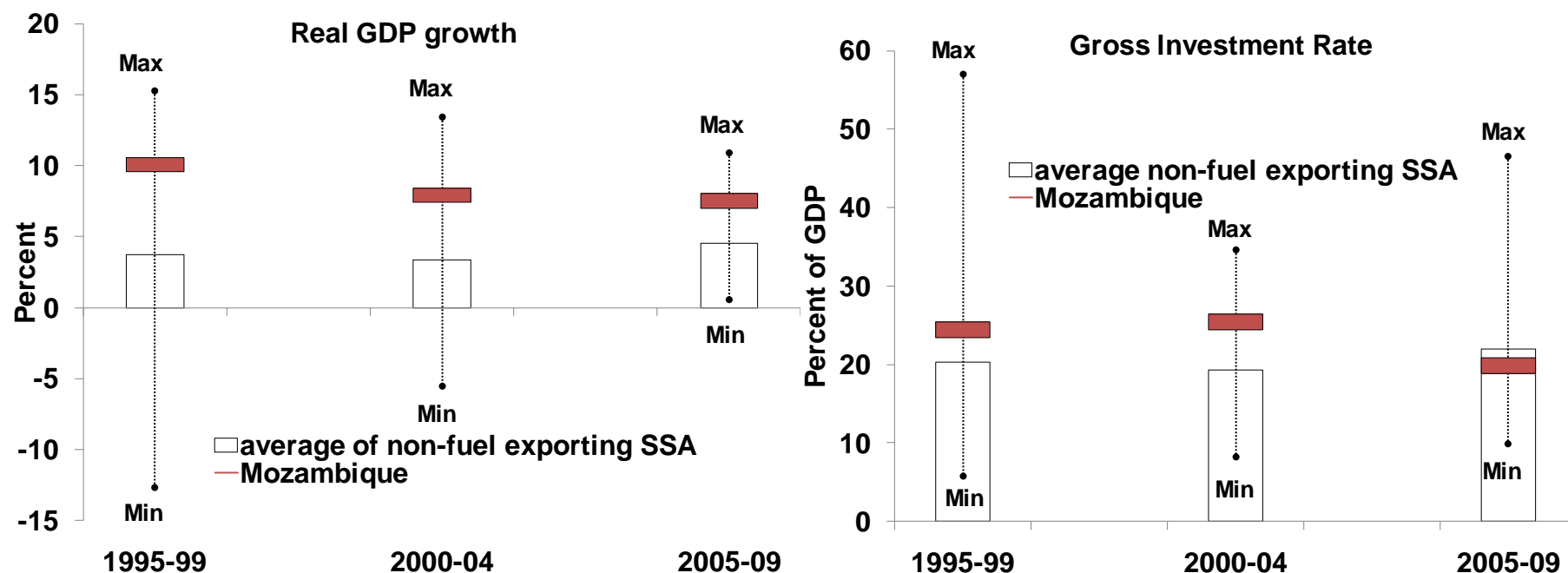




# Policies and Institutions for Inclusive Growth

## Public Investment

- Mozambique's public investment is falling behind the curve



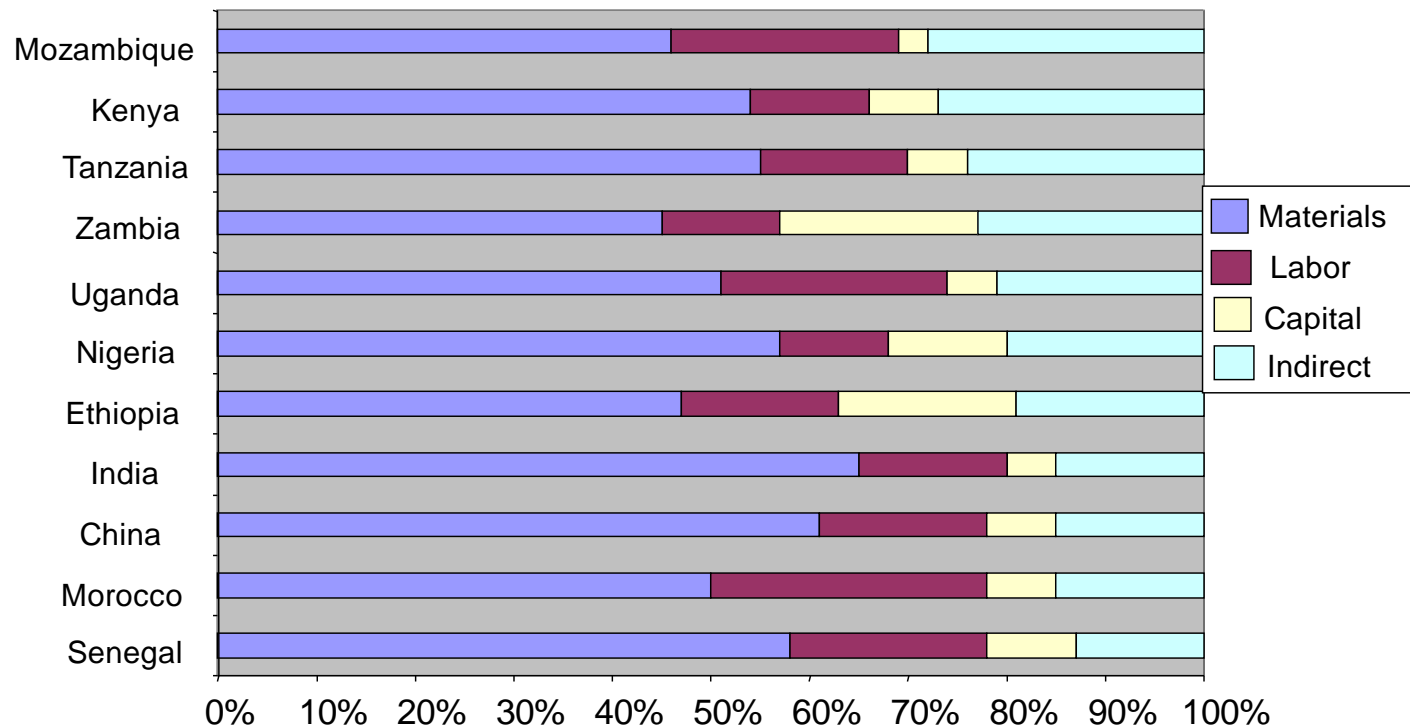
Source: Crispolti (2010), "Economic Growth in Mozambique. Experiences and Policy Challenges," IMF presentation.

# Policies and Institutions for Inclusive Growth

## Regulatory and Labor Reforms

- Diversification into light manufacturing and other labor intensive industries in Mozambique hampered by high indirect costs in the form of burdensome regulations ...

**Cost structure, firm-level average, by country**



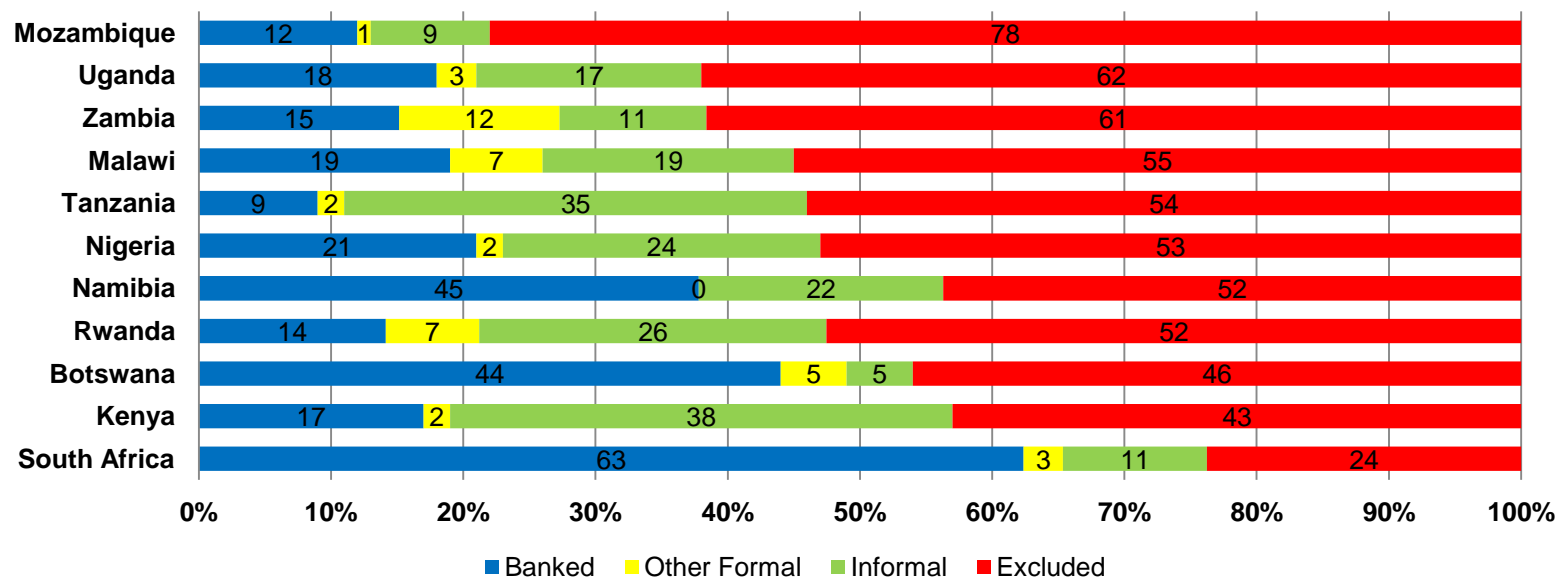
Source: Eifert, Gelb, and Ramachandran (2005) based on World Bank Investment Climate Assessment data.

# Policies and Institutions for Inclusive Growth

## Financial Inclusion

- ... and one of the highest rates of financial exclusion among SADC countries

**FinScope Survey Results:  
Comparative Access to Finance in African Countries**

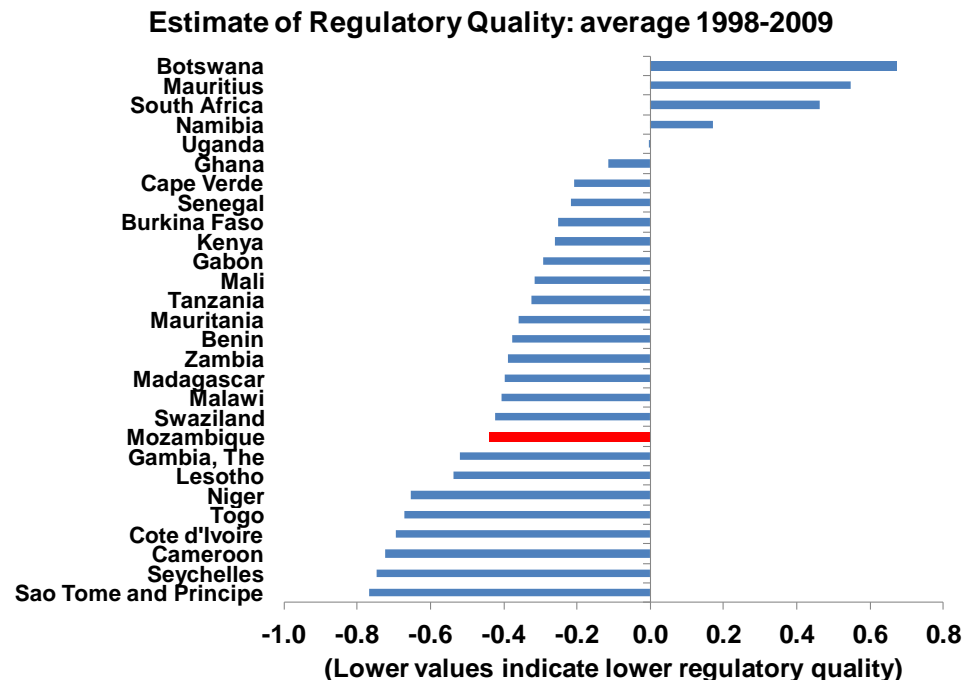


Source: Mozambique Fin Scope.

# Policies and Institutions for Inclusive Growth

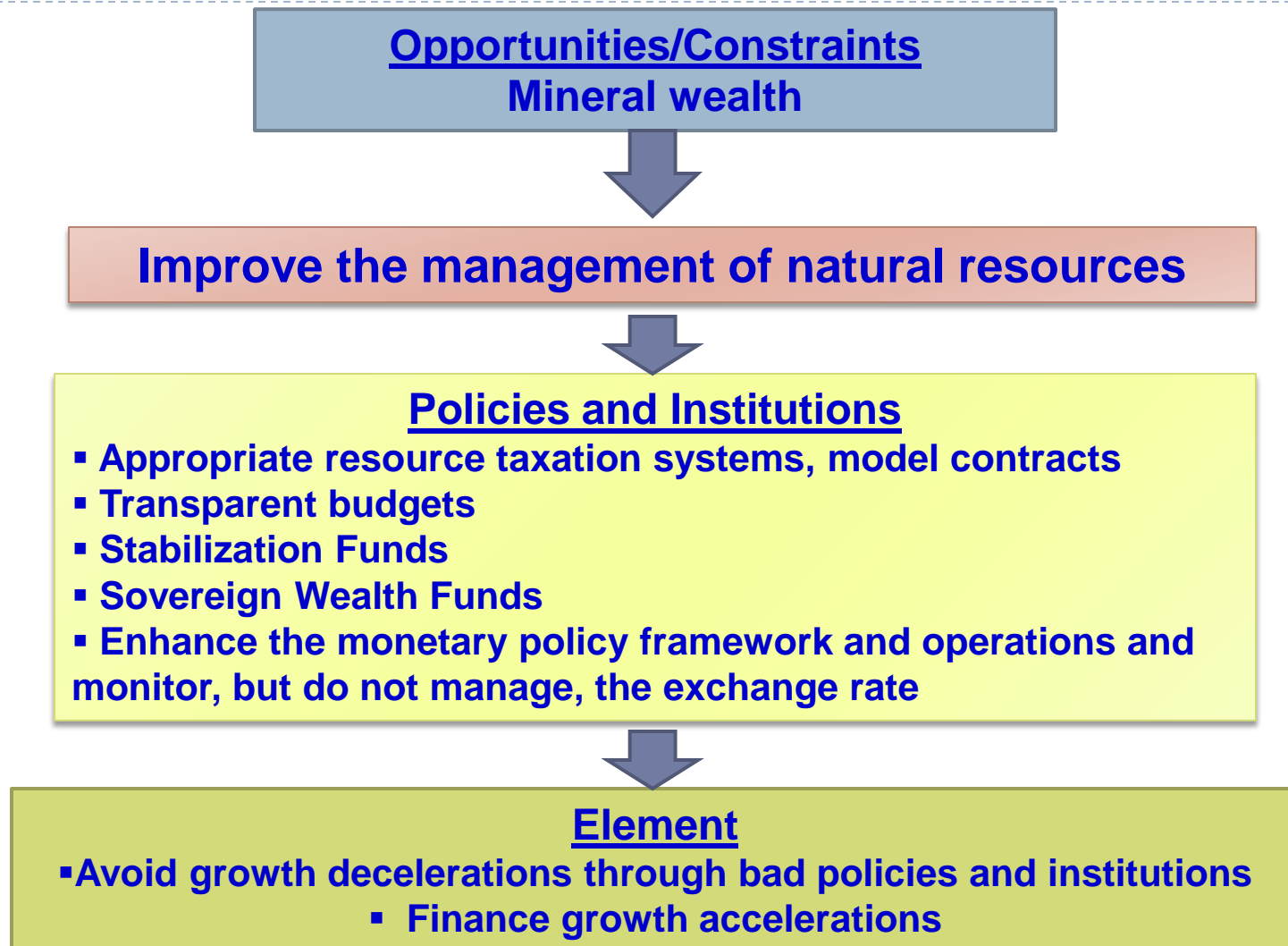
## Economic Diversification in Uganda

- Uganda constitutes a very relevant case study for Mozambique of successful economic diversification:
  - Both countries started their growth takeoffs around the same time after emerging from a protracted civil war
  - Uganda has a more disadvantageous initial condition than Mozambique, since it is landlocked, yet it has been a more aggressive economic reformer



Source: World Development Indicators 2010. World Bank.

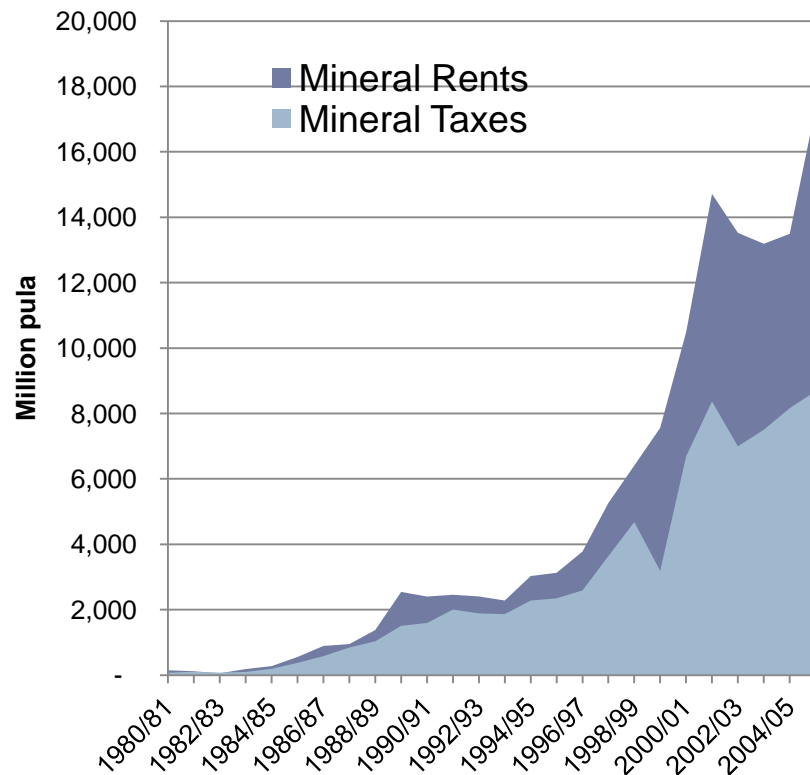
# Policies and Institutions for Inclusive Growth Managing Natural Resources Well



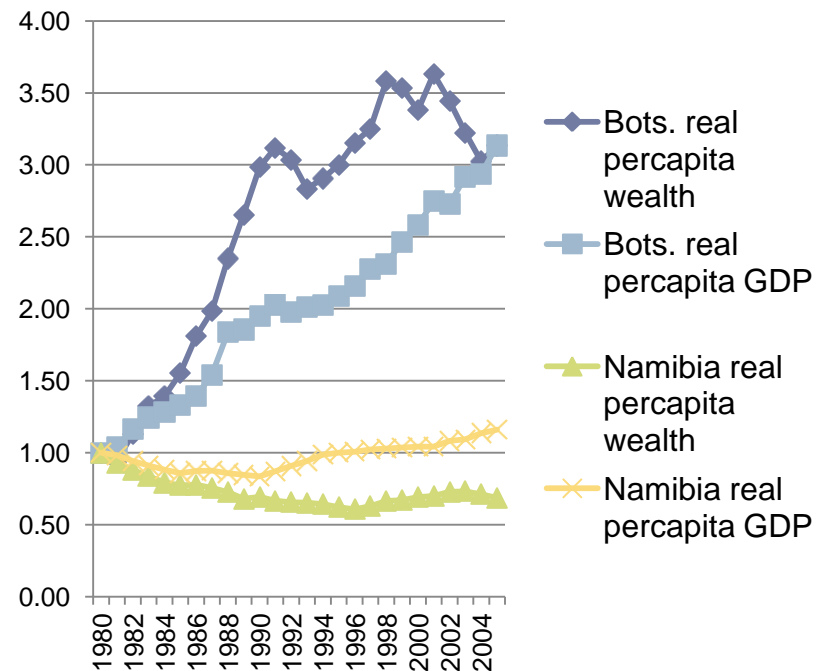
# Policies and Institutions for Inclusive Growth

## Managing Natural Resources in Botswana

**Recovery of resource rent and taxes by state from mining in Botswana, 1980 to 2005**



**Growth of real, per capita wealth and GDP in Botswana and Namibia, 1980 to 2005 (1980 = 1.00)**



Source: Lange (2011), *The Changing Wealth of Nations. Measuring Sustainable Development for the New Millennium*, World Bank.

# Policies and Institutions for Inclusive Growth

## Managing Natural Resources in Botswana

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- ▶ Manage fluctuations in revenues from natural resources rents through the use of stabilization funds and rules for smoothing public expenditure
    - ▶ Government created three funds -the Domestic Development Fund, the Revenue Stabilization Fund, and the Public Debt Service Fund- which have allowed it to avoid the boom-bust cycles in commodity prices
  - ▶ Transform revenue from natural resources into sustained economic growth by effectively reinvesting in additional productive capacity, including education, training, health, and infrastructure
    - ▶ Government limits current expenditure and debt payment and devotes close to 40% of government revenues allocated to infrastructure and human capital expenditures
  - ▶ Fair price for mineral resource use
    - ▶ Government has been able to form stable, long-lasting partnerships with mining companies, leaving company management in the hands of private sector firms. It has effectively negotiated equity and business shares, instead of outright nationalization, and increased its share of equity and revenue
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# Policies and Institutions for Inclusive Growth Strengthening Social Cohesion

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# Conclusions and Next Steps – Thanks !

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- **Mozambique growth needs to become more inclusive to reinvigorate the poverty reduction process.**
- **The country's strong track record of macroeconomic stability needs to be preserved.**
  - **It has provided the country with a sound base for economic development**
    - > **Scaling up public investment in infrastructure is feasible**
  - **Preserving macroeconomic stability will create a framework for private sector activity**
- **A more inclusive growth strategy could rest on two key pillars:**
  - ✓ **Fostering a competitive and diversified export base**
  - ✓ **Boost production and productivity in labor intensive sectors**
    - > **Catch up with faster reformers in Africa and worldwide**
- **Inclusive growth strategies should be supported by policies and institutions that strengthen natural resource management and social cohesion.**