Savings Mobilization, Financial Liberalization and Economic Adjustment in Africa: Issues, Theory and Policy Consequences

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Résumé: Cet article analyse la complexité étonnante ainsi que l'existence de lacunes dans la recherche et de politiques contradictoires sur des problèmes relatifs à la mobilisation de l'épargne et à la libéralisation économique en Afrique. Plus d'une décennie de croissance lente ou négative dans nombre d'économies de la région n'a pas conduit à une plus grande élaboration analytique et une meilleure compréhension des processus d'épargne et leur importance dans le développement économique. Les pays développés ont connu à la même période, un développement économique sans précédent; des études plus approfondies sur l'épargne ont globalement confirmé les thèses de Lewis. Les partisans les plus acharnés d'un taux d'épargne national élevé ont montré à partir de preuves historiques que l'épargne augmente le capital investible per capita. Ainsi non seulement il détermine la croissance mais également l'augmentation de la productivité, la compétitivité et le niveau de vie.

> The central problem in the theory of economic development is to understand the process by which a community which was previously saving and investing 4 or 5 per cent of its national income or less, converts itself into an economy where voluntary saving is running at about 12 or 15 per cent of national income or more. This is the central problem because the central fact of economic development is rapid capital accumulation. W. Arthur Lewis (1954).

Aspects of Savings Mobilization in Africa

The objective of this paper is to explore the surprising complexity, prevalence of research gaps and policy ambivalence on issues relating to savings Mobilization and financial Liberalization in Africa. More than a decade of slow or negative growth in many economies of the region has not elicited a greater analytical exposition and understanding of the savings process and its importance in development and economic recovery. The

same period in the developed countries has coincided with both an unprecedented economic recovery and further study on savings, reaffirming Lewis's proposition in more general terms. The strongest proponents of increased national savings rates, (Summers, 1986) show from the analysis of historical evidence that savings increases investable per capita capital stock and thereby determines not just growth but also increases in productivity, international competitiveness and standards of living.

In an economy with a low savings rate, the stock of capital will decline if consumption levels rise towards production levels. Zero growth of living standards itself requires gross saving to be mobilized towards at least a level equal to economic depreciation in order to maintain the existing level of capital stock. Incremental rates are needed to achieve other objectives: to ensure that capital grows in proportion to population growth; to raise the capital/labour ratio, thereby increasing per capita output; to match or exceed living standards achieved beyond the national borders.

In most African countries, savings rates have not risen to meet the above objectives, and they have declined in recent years. In addition savings behaviour has local particularities which hinder savings Mobilization. This paper points out the seasonality of incomes, the absence of old-age incomes, the financial support transferred by income earners to the unemployed and old-aged, and government deficit financing, as some of the factors which hinder savings performance in accordance with economic theory. In most countries, the difference between national savings and gross investment typically shows a resource gap which has to be financed with foreign savings.

Furthermore, even where financial savings and their Mobilization have a high potential, Africa's financial systems operate in a highly rigid and segmented environment which further diminishes the Mobilization of what potential savings there is. There are three characteristics most illustrative of the segmentation and financial impediments to savings in the region. One is the system of direct controls under which the financial systems operated until the recent changes towards indirect controls. The second is the rural/urban dichotomy of the financial sectors found in all countries: The financial systems concentrate their activities in the urban centres and shun potential business that can be generated via the Mobilization of savings in the rural areas.

Third, there is an observed stratification of financial services - acceptance of deposits, lending facilities, access to banking and insurance services, share ownership etc.,- by levels of incomes for potential clients. In their deposit liabilities and lending, the financial systems cater to medium and high income earners, broadly discouraging transactions with low-income earners. This is an outstanding paradox in economies where the latter are

broadly the majority of income earners. Although financial liabilities towards low-income earners are viewed as unattractive in terms of profitability, (on the perception that individual transactions are small and thus elicit relatively high transactions costs), it would be far better to devise financial policies which ameliorate the problem than to rely on the financial institutions to apply their profitability schedules as a means of avoiding business with the majority of income earners. The lack of financial services tailored to the saving requirements of local economic activity implies that society loses welfare in the cycle of un-mobilised savings, lower investment and lower output growth.

Lending to lower income groups is shunned for the same reasons and, in addition, for the perceived insufficiency of security of loans. One research project, Nissanke (1990), has gone as far as to suggest that, far from suffering the credit gap predicted under the theory of financial repression, many African financial systems are marked by a clubby conservatism and persistent "excess liquidity". This implies the holding of deposit liabilities over and above statutory requirements. It also implies a lack of motivation to attract new deposits and an unwillingness by financial institutions to mop up liquidity by committing new loans.

Financial repression, an aspect of direct controls in the financial system for the last few decades, has further acted to lower savings, particularly financial savings. The condition describes an environment where interest rates are officially set at levels below the inflation rates. To protect their wealth, income earners respond to the suppressed rates of return on financial savings by shifting their savings to inflation-hedged assets: Physical assets such as animal wealth, precious stones, jewellery, real estate etc., become more attractive (and their prices are raised by demand) than financial savings. Bank lending is squeezed by low profit margins relative to transactions costs.

The current departure from the traditional orthodoxy of direct controls in the financial sector towards "financial deepening" relies heavily on a shift to market-determined interest rates. Theoretically, this should induce a shift in the composition of savings from inflation-hedged savings to financial savings. Savings, investment and general economic activity are strengthened by improved linkages between a country's financial superstructure and its real infrastructure. The triple aggregates of saving-investment-growth are thereby promoted and the efficiency of resource allocation is enhanced. These propositions have been widely acknowledged since Goldsmith (1969, p. 400) put it simply: the financial superstructure of an economy "accelerates economic growth and improves economic performance to the extent that it facilitates the migration of funds to the best user, i.e., to the place in the economic system where the funds will yield the highest social return".

If national saving and restructuring of financial systems are to become key catalysts for growth and rising standards of living, the recent record of performance in the Africa region begs many questions of analysis and application some of which will be highlighted in this paper with quantitative illustrations from Kenya, Cote d'Ivoire and Cameroon. The economies of the region have been characterized by low to negative growth rates, high population growth rates and zero or near-zero growth in per capita incomes. Financial Liberalization has uncovered many paradoxes of the old orthodoxy which hinder the effectiveness of reforms. High financial liquidity co-exists with unfunded development needs. As highlighted above, sizable savings potential and Mobilization of domestic resources are seriously hampered by structural impediments which are partially the offshoots of the era of financial repression. Financial intermediation remains weak and inefficient. In short, the situation calls for more study, a thorough review of the issues and a reformulation of appropriate policy stances for economic recovery.

For progress to be made, it is important to understand the scope of national savings effort that the situation calls for and why. Second it is important to focus critically on the African context in which the assumptions of the theory of saving as well as the current theories of finance applied to raise savings rates and financial intermediation, apply only imperfectly. Third, it is essential to understand what obstacles these conditions imply for the region's policy capacity for incentivising savings, particularly under a climate of economic reforms. The rest of this section deals with the first aspect of the problem, with illustrations from Kenya, Cot d'Ivoire and Cameroon. The second section deals with the second and third aspects, and a concluding section discusses policy factors likely to strengthen savings and financial liberalization in the region.

National savings in this paper conforms to the conventional definition, which includes private sector saving and government saving. It is measured by subtracting the current account deficit, which is foreign saving, from gross domestic investment. The latter is defined to include gross fixed capital formation and changes in stocks. The national savings rate is calculated by dividing national saving by national income, defined as GNP plus net foreign transfers. Symbolically, the definitions may be set out as follows:

(1) $CAB = X - M + NPI$

(2) $GNP - GDP + NPI$

Where CAB is the value of the current account balance, X is the value of exports, M the value of imports, GNP is the Gross National Product, GDP is the Gross Domestic Product and NPI is the net property income from overseas, which is suppressed for convenience of exposition.

The definition of the GDP can be written in the usual way as,

(3) $GDP = C + I + G + X - M$

Disposable income of the private sector is spent on consumption or saved:

(4) GNP - T = C + S

Substituting (3) into (4) yields overall national saving as the sum of gross investment and the current account balance:

(5) (S + T - G) = CAB + I

In (5), national saving is defined as the sum of private saving plus government saving. The current account of the balance of payments is also shown to be the difference between the two categories of saving on the one hand, and investment on the other. National saving, as defined[1], indicates it's open-economy aspects. If the public sector dissaves, either the private sector must make up the difference or it will show up in the form of an increased current account deficit. The latter constitutes capital inflow, the medium-to-long-term perspective of which seems precarious for the Africa region. In recent years, developments in world capital flows have worsened the prospects for access to foreign saving, putting a sharp focus on measures to invigorate the process of domestic savings mobilization in African countries. In any case, the evidence on the impacts of foreign saving has been found to be inconclusive and controversial (Griffin and Enos 1970, Papanek, 1973 and Frimpong-Ansah, 1987). The controversy has varied aspects, but the central questions centre on two issues: the so-called "substitution hypothesis" raising the question whether the national economy applies foreign saving to augment consumption or whether the inflows supplement investment; and the measurement problem surrounding national saving in the literature. The latter has been elucidated by Papanek (1973) in an interesting contribution showing, among other things, that the results obtained by Griffin and Enos (1970) and Rahman (1968) (showing that foreign capital inflows increase permanent income, leading to both increased saving and consumption) were based on rigid accounting definitions and had no sound basis in theory of savings behaviour[2]. In spite of the debate,

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1   In this paper it is anticipated that the usual measurement problem with national savings affects the results. Independent and desegregated estimates of national saving hardly exist in African countries. Little can be done about this within the scope of an exposition such as this paper although the criticisms, especially from the point of view of the application of econometric methods, are serious (see World Bank, 1975).

2   The usual question in the literature has been whether foreign capital is used to substitute for domestic savings (thereby increasing consumption) or whether it supplements domestic savings to raise investment, leading to an increase in permanent income and consumption, in that order. Apart from issues raised by Papanek, this approach of the "decreased saving effect" of foreign resources has recently been theoretically questioned in the specification and estimates of Levy (1987). In the relation of savings-investment balances to the current account deficit, (S + T- G) - I = CAB, if the point of interest is to assess whether foreign resources are indeed applied to growth, the estimate to obtain is that of how much of the inflow is applied to investment directly. Levy's estimates, using flows of concessional

investment and growth in Africa in the 1970s, but have weakened in recent years.

Two main influences seem to have contributed to the decline in foreign saving and the access of African countries to it. First, the total supply of saving in the major sources, the industrial countries, seems to have fallen, with much of the decline being associated with the slackening of private saving, particularly personal saving. Second, because of the debt crises in Africa, as in the rest of the developing world, there has been a substantial erosion of confidence and therefore financial inflows. Saving has thus been retained in the industrial countries due as much to reduced supplies as to a tendency to be risk-averse with respect to developing countries.

Recent research seems to cast further doubt as to the extent to which national economies should generally rely on world capital markets to fill the domestic gaps between savings and investment. For the major industrial countries, Feldstein and Harioka (1980) suggest that so far, the massive growth of world capital markets and capital flows in the past few decades has not necessarily moved to dissipate world differentials in rates of return to investments. Their finding of a strong correlation between the levels of saving and investment in the national economies of individual countries has an implication for developing countries: in spite of the dynamism of world capital markets and their allocative criteria (such as creditworthiness) and however attractive the domestic investment climate may be in a developing economy, the link between national savings performance and domestic investment may remain unbroken by foreign capital inflows alone. The lower the national savings levels the lower will be the corresponding investment levels and vice-versa[3].

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assistance to the least developed countries, indeed found overwhelming support for the position that the flows were applied to investment and growth. However, even this approach does not settle the question. It leaves out a variety of flows which may be resorted to in financing the current account: draw-down of foreign reserves, workers' remittances, suppliers' credits, etc. This paper can add little to the controversy although estimates of the role of foreign capital will be derived in the appropriate equations for a few countries. Of greater relevance, we will assess the capacity for internal savings of the selected countries to meet domestic investment needs. The results should thus show both · the gap that is likely to be left by the curtailment of foreign resources and the domestic savings mobilization effort that will be needed to fill it.

3   Indeed, by the arguments of the factor-price equalization theorem, the burden of equalization of differentials in world rates of return on capital need not fall on capital flows. Free trade can drive an adjustment process where real returns to factors of production are equalized via the flow of goods and services alone. Trade raises the price of the relatively abundant factor in each trading country while reducing the return on the scarce factor.

The implications of the above developments for African countries need to be understood by policy-makers. In the foreseeable future, prospects for the availability of foreign financing to augment gross domestic investment will remain poor. Furthermore, if the Feldstein Harioka findings are true for the region, a change in prospects may not necessarily raise national savings-investment levels. To buttress current levels of domestic investment and forestall a future sequence of falling capital stock, stagnation and falling standards of living, African economies largely have to fall back on a strategy of raising their own resources to fill the gap in financing economic development. This challenge can only be met through efforts to increase national savings rates to even higher levels than hitherto anticipated.

The urgency to raise savings rates is reinforced by current indications that there has been a widespread failure to match reductions in foreign resources with increased domestic savings (Aghevli et al, 1990). Compared to the 1970s, national savings in the developing countries fell sharply in the 1980s, in tandem with foreign saving and gross domestic investment. In relative terms, the declines in the Africa region ranked among the steepest in the developing world. These declines, unless reversed by counterbalancing changes, can be expected to negatively affect prospects for income formation and standards of living in the future. The following analyses show the results of trend developments in savings rates, investment ratios and resource gaps in Kenya, Cote d'Ivoire and Cameroon. Simple savings and investment functions are used to illustrate the problems of savings Mobilization using annual data for the 1970s and 1980s.

Table 1 presents a trend analysis of the national savings rate, S/Y, domestic investment rate, I/Y and foreign capital inflow, $S/Y-I/Y$, in Kenya. As seen in the table the savings rate fluctuated within the range of 11 percent and 24 percent between 1970 and 1987. The savings rate was consistently higher than 15 percent for most of the years cited, and reached a peak rate of 24 per cent at the height of the coffee boom in 1977. However, in spite of the seemingly high national savings rate, it has not been possible to finance Kenya's gross domestic investment entirely from national savings efforts. This is clearly indicated by the substantially higher gross investment rates which also show that foreign savings have been applied to close the gap. All three columns of the table bring out these trends quite convincingly. The investment rate has reached above 20 per cent for most years during the period cited, considerably exceeding the savings rate. The savings-investment gap in Kenya reveals that foreign savings have generally been lower than 10 per cent. In recent years, the gap seems to have been narrowed. However, since the savings rate has not changed dramatically, this narrowing might reflect a combination of lower economic performance and a slowdown in inflows. It is also noted that the indirect effect of improved export performance, as evidenced by the coffee boom of 1977, has the effect

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of raising savings substantially. During that year the savings rate exceeded
the investment rate by over half a per cent.

**Table 1: Trend Movements in Savings Rate Investment Rate and
Resource gap: Kenya**

	S/Y	I/Y	S/Y-I/Y
1970	0.189	0.219	-0.030
1971	0.190	0.253	-0.062
1972	0.187	0.221	-0.034
1973	0.147	0.199	-0.053
1974	0.177	0.285	-0.108
1975	0.113	0.182	-0.069
1976	0.166	0.202	-0.036
1977	0.243	0.237	0.006
1978	0.172	0.297	-0.124
1979	0.145	0.227	-0.082
1980	0.175	0.300	-0.125
1981	0.200	0.284	-0.084
1982	0.176	0.225	-0.049
1983	0.203	0.211	-0.008
1984	0.213	0.234	-0.021
1985	0.172	0.201	-0.029
1986	0.216	0.225	-0.010
1987	0.185	0.246	-0.061

Sources: Computed from i) International Financial Statistics;
ii) World Bank *World Tables*

Equation (1) shows the impact of foreign capital inflows on national
savings in Kenya. The results indicate that foreign capital inflows have not
necessarily been detrimental to national savings effort in Kenya, a reflection
of the possible use of foreign savings to complement gross investment rather
than consumption. The influence of foreign capital inflows on national
savings has generated considerable debate in the theoretical and empirical
literature with some researchers finding a positive impact while others could
only find a negative impact. Our result is in line with those who consider
foreign investment not to be detrimental to national savings efforts. The
coefficient of foreign capital inflows was not statistically significant
however. From equation (1) it is would seem that a 10 percent increase in
foreign savings rate may lead to a nearly 2 percent increase in national
savings rate, all things being equal. However, the constant is significant at
the 1 per cent level, indicating that there are missing variables in the
equation. The overall fit of the equation is consequently poor.

Equation 1: Dependent Variable: SR

variable	Estimated Coefficient	Standard Error	T-statistic
C	0.19591*	0.01442	13.585
FS/GDP	0.19701	0.17566	1.1215
$R^2 = 0.0729$, D.W. = 1.9706, n = 18			

Notes: SR= savings rate, FS/GDP= trade balance as ratio of GDP.
  * = significant at 1 per cent level.

Equation 2 considers the responsiveness of the gross domestic investment rate to national savings efforts in Kenya. It can be seen that the savings rate variable bears the correct sign. It is however, not statistically significant. The result for Kenya would seem to indicate that a 10 per cent increase in the savings rate constitutes a 4 per cent impetus for investment, or about two fifths of each unit of investment. This is a fairly low figure indicating lack of financial depth and weak financial intermediation. Similarly, domestic credit growth seems to support gross investment, but with the same constraints. However the fit of the equation is poor, and a constant which is significant at the 10 per cent level shows that there are other major determinants of gross investment in Kenya not included in the simple specification.

Equation 2: Dependent Variable:GIR

variable	Estimated Coefficient	Standard Error	T-statistic
C	0.14097**	0.05958	2.3661
SR	0.39889	0.29109	1.3703
GDC	0.00110	0.00091	1.2123
SER = 0.0348, R^2 = 0.172449, D.W. = 1.7497, n = 17			

Notes: GIR= gross investment as ratio of GDP, SR= savings ratio, GDC = growth
  of domestic credit.
  * = significant at 1 per cent level

For Cote d'Ivoire table 2 indicates that the savings rate has been lower than that of Kenya for the nearly two decades analyzed. Whereas the savings rate in Kenya varied between 11 percent and 24 percent of GDP, that of Cote d'Ivoire varied between 6 percent and 19 percent with a mean savings rate of 11.1 percent. However, the savings rate in Cote d'Ivoire shows substantial fluctuation. The coefficient of variation or the instability index for Cote d'Ivoire is 0.324. The table further reveals that, as in the case of Kenya, sharp increases in national savings occur during commodity booms such as in the 1970s. In periods of recession as in the 1980s, savings rates should tend to fall, in theory. While this trend was not observed for Kenya,

the national savings rate of the Ivory Coast seems to have undergone a secular decline in the 1980s.

Table 2: Trend Movements in Savings Rate, Investment Rate and Resource Gap: Cote D'ivoire

	S/Y	I/Y	S/Y-I/Y
1971	0.14679	0.21789	-0.07110
1972	0.13519	0.20815	-0.07296
1973	0.11932	0.23184	-0.11252
1974	0.16779	0.22016	-0.05237
1975	0.09832	0.22422	-0.12590
1976	0.12657	0.22980	-0.10323
1977	0.19532	0.27336	-0.07804
1978	0.13382	0.29759	-0.16377
1979	0.08190	0.27969	-0.19779
1980	0.09991	0.28218	-0.18227
1981	0.06808	0.25922	-0.19114
1982	0.08425	0.23205	-0.14780
1983	0.06692	0.20604	-0.13912
1984	0.10770	0.10910	-0.00139
1985	0.12046	0.12588	-0.00542
1986	0.10912	0.11054	-0.00142
1987	0.06811	0.13026	-0.06215
1988	0.07099	0.14507	-0.07409
Mean rate	0.111	0.210	
Instability index	0.324	0.291	

Sources: Computed from i) International Financial Statistics;
ii) World Bank *World Tables*

When the national savings rate in Cote d'Ivoire is compared with the gross investment requirements, it is seen that it has been inadequate, a fact which led to the recourse to foreign savings to breach the savings-investment gap. The problem of inadequate savings indicated in the results for Kenya is again evident in the case of Cote d'Ivoire but to a substantially greater degree. The savings-investment gap in Cote d'Ivoire reveals that throughout the period, savings consistently lagged behind gross investment needs. When the recession of the 1980s appeared to affect domestic savings adversely, the resource gap narrowed at the same time. From the trend in the investment rate, it is evident that this diminished reliance on foreign savings did not reflect a substitution of domestic resource Mobilization for foreign savings, but occurred at the expense of a steep decline in the investment ratio. This must negatively affect medium to long-term growth and living standards. The poor savings record of Cote

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d'Ivoire casts serious doubts on the usefulness or effectiveness of the well-known Abidjan stock exchange in mobilizing savings for investment, when compared with the record of Kenya which has a similar stock exchange. In addition, the general decline in savings rates in the 1980s shows that the macroeconomic adjustment programme launched in the country in 1981 is yet to seriously address the issue of domestic resource mobilization.

Equation 3: Dependent Variable: SR

variable		Estimated Coefficient	T-statistic
C		0.15337*	9.9504
FS/GDP		-0.048474*	-4.1033
SER = 0.024	R = 0.606	n = 18	

Equation (3) shows the impact of foreign capital inflows on national savings in Cote d'Ivoire. The results indicate that foreign capital inflows have had a possibly detrimental effect on national savings effort in Cote d'Ivoire, a reflection of the possible use of foreign savings for consumption. In contrast to the case of Kenya, the coefficient of foreign capital inflow was not only negative, it was also statistically significant at the 1 percent level. A ten percent increase in the foreign savings rate may lower the savings rate by about half a percent. This finding is consistent with the views of the proponents of the position that foreign savings act as a disincentive for domestic savings effort by possibly being diverted to consumption instead of complementing investment, growth and development.

Equation 4: Dependent Variable: GIR

variable	Estimated Coefficient	Standard Error	T-statistic
C	0.18381*	0.0396	4.6387
SY	-0.28713	0.4066	-0.7061
GDC	0.00315*	0.0011	2.9947
SER = 0.050, R^2 = 0.409, D.W = 0.8268, n = 18			

Equation (4) considers the responsiveness of gross domestic investment rate to national savings efforts and to the growth of domestic credit. As can be seen from the table, the savings rate variable bears the wrong sign. Although it is not statistically significant, it does suggest that a ten per cent increase in the savings rate may lead to a 2.9 per cent decrease in gross investment. Although the result is not easily explained, it may imply, taken with equation (3), that foreign savings substitute for domestic savings and vice versa. Furthermore, the magnitude of the impact suggests a lack of

financial intermediation. The other variable, growth of domestic credit, seems to have similar supportive impacts on gross investment as in Kenya and the coefficient is significant. It should be remembered that the Cote d'Ivoire is in the UMOA zone where there are relatively strict guidelines on the expansion of domestic credit. In Kenya however, the restraints are not similarly strict, and domestic credit expansion may have overshot appropriate levels such that the price-increasing impacts of the expansion may have dominated the output effects, thereby producing the negative impacts on investment.

Table 3 presents a trend analysis of national savings rate, domestic investment rate and foreign capital inflow in Cameroon. As seen in the table the savings rate fluctuated within the range of 4 percent and 26 percent between 1971 and 1988. The savings rate was considerably higher than 15 percent between 1982 and 1986 with a peak rate of 26 percent in 1984. The mean average savings rate between 1971 and 1988 was 12.2 percent with an instability index of 0.552. In spite of the seemingly high and fluctuating national savings rate, it was not possible to finance gross domestic investment entirely from national savings efforts. This is clearly indicated by the substantially higher gross investment rates which again replicate the positions in Kenya and the Cote d'Ivoire. Columns 1 and 2 of the table bring out these trends quite convincingly. The mean investment rate during the period had been 0.213 which exceeded the mean savings rate by 9.1 percent. The savings-investment gap in Cameroon reveals that it was generally higher than 10 percent between 1977 and 1981. Between 1982 and 1988 the gap has been narrowing. Until 1985, the narrowing of the gap reflected the growing capacity of national savings to meet rising investment requirements. In 1986 however, the saving rate begun to fall, so that the continuing narrowing of the gap began to reflect a fall in the gross investment ratio. It is remarkable that the national savings rate of 26 percent in 1984 exceeded gross domestic investment rate by 4.7 percent.

It is important to emphasize that Cameroon is known to have a substantial network of informal savings mobilized from small savers. However, we had no access to information to analyze the informal financial sector whose very substantial savings are thus not represented in the savings figures presented and analyzed in this section.

Equation 5 shows the impact of foreign capital inflow on national savings in Cameroon. The results indicate that foreign capital inflow has a negative impact on national savings, as in the case of the Cote d'Ivoire. However, the coefficient is statistically insignificant even at the 10 percent level. One explanation for this may be the application of foreign savings for consumption purposes, an indication of myopic behaviour. The fact that the responsiveness of national savings to foreign capital inflow is negative

suggests that Cameroon should examine more carefully the nature and quality of foreign assistance provided to the country.

Table 3: Trend Movements in Savings Rate, Investment Rate and Resource Gap: Cameroon

	S/Y	I/Y	S/Y-I/Y
1971	0.05109	0.17664	-0.12555
1972	0.04045	0.19354	-0.15309
1973	0.07925	0.21075	-0.13150
1974	0.11287	0.18006	-0.06719
1975	0.08876	0.21079	-0.12203
1976	0.04915	0.18533	-0.13618
1977	0.12456	0.23013	-0.10557
1978	0.12841	0.24669	-0.11829
1979	0.07286	0.23787	-0.16501
1980	0.06270	0.20993	-0.14723
1981	0.13853	0.27171	-0.13318
1982	0.16730	0.24793	-0.08063
1983	0.22804	0.25974	-0.03170
1984	0.26000	0.21315	0.04685
1985	0.24616	0.20344	0.04272
1986	0.15134	0.20189	-0.05054
1987	0.09258	0.18327	-0.09069
1988	0.09469	0.16658	-0.07188
Mean rate	0.122	0.213	
Instability index	0.552	0.143	

Note: Instability index is computed as coefficient of variation.
Sources: Computed from i) International Financial Statistics (IMF);
ii) World Bank *World Tables*

As is clear by now, the results from simple savings functions are not overly reliable and can not be taken literally for the three countries. Even so, the available interpretations suggest that the impacts of foreign inflows on national savings encompass the debate in the theoretical and empirical literature where some researchers find a positive impact while others find a negative impact. Our result for Cameroon is in line with those who consider foreign investment to be detrimental to national savings efforts.

Equation 5: Dependent Variable SR

variable	Estimated Coefficient	T-statistic
C	0.13545*[a]	6.5168
FS/GDP	-0.21351	-1.0244
SER 0.0669, R = 0.06 n = 18.		

Equation 6 considers the responsiveness of gross domestic investment rate to national savings efforts and to the growth of domestic credit. As can be seen from the equation, the savings rate variable is statistically significant and has the expected sign. A 10 percent increase in the national savings rate may lead to a 2.2 percent increase in the investment rate, or approximately a fifth of each incremental unit of the investment ratio, all other things being equal. This result is unlike that for the Cote d'Ivoire which, like Cameroon, is in the Franc zone. It underlines the importance of national savings in promoting investment, although the levels of financial intermediation for the two countries would seem to be lower than in Kenya. Although the coefficient on the growth of domestic credit has the correct sign, it is not statistically significant. The significance of the constant term at the one per cent level further points out to the importance of other determinants of the investment ratio not included in the simple equation.

Equation 6: Dependent Variable GIR

variable	Estimated Coefficient	Standard Error	T-statistic
C	0.16811*	0.01868	8.9965
SY	0.22153**	0.10024	2.2101
DCG	0.0008	0.00048	1.7274
SER = 0.0270, R^2 = 0.302, D.W. = 1.1634, n = 18			

In summary, with the possible exception of Kenya, savings rates have fallen in recent years in the three countries selected to illustrate the savings Mobilization problem. All three countries have persistent resource gaps, and in some cases, where these resource gaps are filled with foreign savings, the latter is presumably applied to consumption rather than to investment. Furthermore, the capacity for national savings to make an impact on domestic investment requirements is fairly low and, in the case of the Cote d'Ivoire, curiously negative.

To conclude this section, the required national savings efforts in the medium and long-term perspectives in the region have four counterparts, each calling for cumulatively higher orders of resource Mobilization:
- a savings counterpart required for replacement of depreciation in capital stock;
- a savings counterpart required for maintenance of capital per worker as an offset for population growth;
- a savings counterpart required for the replacement of shortfalls in net inflows of foreign saving, to permit the maintenance of current levels of gross investment;
- a savings counterpart required for increments in gross investment in order to underpin economic growth.

In the current understanding of the savings Mobilization problem, there are two main sources of policy formation as to how savings on the above scale can be raised in African economies. One is the theory of consumption and the other is the analysis of the structural impediments which discourage the flow of national savings to investment and which must be removed to achieve the appropriate degrees and efficiency of financial intermediation.

General and Specific Factors in Savings Mobilization and Financial Liberalization in Africa

In the literature on developing countries, much of the concern with savings relates to its central position as a pillar of economic development, but whose potential stimulus is curtailed by inadequacy (Deaton, 1989). Recently it has been recognized that adjustment programs in developing countries have important direct and indirect impacts on saving, and that the directions of causation among savings, growth and investment may play a complex role in the final outcomes, not necessarily in a supportive stance for progress in any of the three aggregates (Aghevli et al, 1989)[4]. This section first discusses the general issues on savings and then presents other issues which are specific to policy thinking in the area.

The theory explaining savings was for long dominated by the Keynesian perspective that consumption is determined largely by disposable income. Fiscal spending was seen as a major stimulus for economic expansion and

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4   In a simultaneous equation model using the savings rate and the growth rate of GDP as endogenous variables, an estimation of the savings rate for Kenya yielded the following results; SR = -0.112 + YG 0.004 + YPG 0.0003 + DRI 0.0395 - MR 0.010 +
(-0.764) (1.942) (1.380) (2.455) (-0.116)
SRL 0.272
(0.920),   R-SQUARED =   0.512
                         DW =   1.82
                          N =   17
In the equation, SR is the national savings rate, YG is the growth rate of real GDP. The result for the latter has the correct sign and is significant at the ten percent level. YPG is real per capita income growth. DRI is a "dummy" variable for real interest rates constructed to capture the impacts of recent reforms in interest rate policy. The coefficient is significant at the five percent level. Each unit increase in the real rate of interest would seem to increase the savings rate by approximately 0.04. Like GDP growth, positive real rates of interest would seem to give a moderate impetus to the national savings rate. As seen below however, this does not seem to necessarily imply a deepening of the financial system via a shift towards financial savings. MR was constructed as a principal component to represent macroeconomic reforms reflected in movements in a list of variables; the real exchange rate, the budget deficit to GDP ratio and a "dummy" representing prices decontrol. The variable has a negative sign which seems to concur with a view of negative impacts of non-financial structural adjustment reforms on the savings rate. If austerity imposes a major burden on real wages and incomes in particular, this should tend to lower the private savings component of national savings while diminishing the negative impacts from public saving. SRL is lagged SR.

employment. The impacts of real rates of return on savings as a stimulus for savings Mobilization received little attention until the 1970s. In the Absolute Income Hypothesis, consumption is held to be a positive function of income, and since savings is a residual from income after consumption, it is also positively related to income. The neglect of the role of real rates of return on savings, which is at the heart of current thinking on financial liberalization programs, may have stemmed from a theoretical ambiguity regarding their impacts on savings. Despite the current emphasis on reducing financial repression to strengthen the savings-investment-output cycle, the ambiguity remains.

Higher real interest rates incentivise savers to increase current saving and postpone consumption via substitution effects. In developing countries where financial repression has traditionally driven savers to inflation-hedged savings such as animal wealth, gold and other physical assets, the closing of the gap between the nominal deposit rates and inflationary expectations may also induce a certain amount of substitution of financial savings for savings in these assets. Forgoing a unit of current consumption will yield a larger amount of future consumption when the real rate of interest becomes positive. On the other hand the rise in real interest rates also implies an increase in future income and wealth from current financial assets. To achieve a given level of future consumption, it is no longer necessary to save as much. It is even possible to consume more, both in the present and in the future. The net effect of an increase in interest rates- the so called interest elasticity of saving- thus depends on the interplay between the substitution and income effects, working in opposite directions.

Not surprisingly, the experience and empirical literature from testing the interest elasticity of saving proposed à la McKinnon, Shaw and Fry hypothesis, gives conflicting evidence (Le Fort, 1989). To show a positive net effect of increased interest rates on saving, one would have to hypothesize that the substitution effect is greater than the wealth effect.

Although there have been other theoretical approaches to consumption and saving analyses, such as the Relative Income Hypothesis (à la Duesenberry, 1968), it is the Permanent Income Hypothesis and the Life Cycle model, due to Milton Friedman and Franco Modigliani, respectively, which have done the most to enhance the understanding of modern saving behaviour. The Life Cycle Hypothesis posits that consumption is smoothed over individuals' lifetimes, while income earnings are low in early life, high in mid-life and low in retirement. Saving thus follows the same pattern in order to smooth consumption. The hypothesis predicts that the rates of saving and consumption will be affected by the rate of growth in per capita income, the stock of wealth, and various demographic factors such as life expectancy, the normal age of retirement, age distribution, family size, and

the share of the population that is of working age and is employed. Policies affecting any of the above factors also affect the saving rate.

The foregoing general factors, and questions surrounding them, could be modeled for any modern economy. However, the conditions of income formation and consumption are sufficiently different in the Africa region as to warrant the study of the savings problem distinctly from its manifestations in the developed industrial countries (Deaton, 1989). Africa has deeply-embedded problems in savings Mobilization that appear to fall into two broad categories.

First, there are problems related to the real sector. The feedbacks on savings in this case arise principally from low economic activity and the structure of the private and public domains of the savings process. Second there are problems related to the rigidities and segmentation of the financial systems, which act to further diminish savings. Both categories of the problem have unique features whose complexity, policy implications and interactions are still insufficiently studied or understood. In an era of financial and other macroeconomic reforms which further complicate the objectives of savings Mobilization the need for further study is greater.

The starting point in understanding the nature of the real sector problems of savings Mobilization is to examine Africa's processes of private sector income formation and expenditure. Private sector saving is made up of household saving and corporate saving. However household saving in Africa is usually the major source of not only private sector saving but national saving as well. It usually comprises a third of the latter. By composition, however, household saving also has its principal sources in the rural sector. In a striking example from Kenya, one estimate showed rural household saving to exceed total estimated gross national saving[5].

In line with the mainstay of much of the population in Africa in agricultural and non-agricultural economic activity in the rural sector, personal incomes derives principally from this sector and also from mining

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5   The Kenya Economic Survey (1988) summarizes the main findings of the 1981/82 Rural Household Budget Survey whose comprehensive information covered about 2.8 per cent of rural households nationally. The survey found rural households to have an average propensity to save of 36.6 per cent. The average monthly net income was Ksh 829 and average monthly expenditure was Ksh 526. With an estimated rural population of 2.4 million households, the rural sector thus surprisingly generated an estimated Ksh 8.73 billion in 1981/2, a figure higher than that for the gross national savings estimated for that year from the national accounts. Both results perhaps reflect the data problems and measurement errors arising from factors such as the seasonality of agricultural incomes, the difficulty of measuring the flow of non-monetized incomes and expenditures, well known issues of measurement in the national accounts, etc. The survey must nevertheless serve as confirmation that the real savings potential of the rural sector that can be exploited to finance national investment is quite large and it is usually underestimated.

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activity to some extent. Although households are also relatively large and poor, even by third world standards, it is clear that policies for economic recovery which induce even marginal increases in economic activity and income in the rural sector must also elicit very substantial Mobilization of resources. It can thus be hypothesized that the greater the impact of recovery, including enhanced financial services and credit, on rural agricultural and non-agricultural activities, the greater the Mobilization of resources that can become available as the foundation for enlarged gross investment and future economic growth.

An estimate for Kenya in equation 7 shows clearly that relatively to well known determinants of the ratio of financial savings to GDP, such as the real rate of interest, income growth is highly significant. Although the coefficient is low, it is far higher than that on the actual real rate of interest which is insignificant. Macroeconomic reforms similarly seem to raise the ratio but the coefficient is insignificant. The equation, taken together with another estimation which showed interest rates to be ineffective in boosting financial savings as a ratio of gross national savings, suggests that the emphasis on moving interest rates to market-determined rates as an engine for savings Mobilization and deepening of the financial system may be misplaced[6].

Equation 7: Determination of Financial Savings in Kenya: Dependent Variable FINS/GDP

variable	Estimated Coefficient	Standard Error	T-statistic
C	-0.12729	0.099864	-1.2747
GDPG	0.00377*	0.001189	3.1678
ARRI	0.00004	0.001129	0.0387
PAC	0.00002	0.000020	1.1347
PCM1	0.00602	0.006950	0.8659
S.E.R. = 0.02084, R^2 = 0.503, D.W.		= 2.13, n = 17	

FINS = financial savings represented by change in M2, GDPG = real growth of GDP, ARRI= actual real rate of interest, PAC = per capita income, PCM1 = principal component representing macroeconomic reforms.

6   It should not be forgotten that the preoccupation with the shift to market-determined interest rates ignores other well-known difficulties of savings MOBILIZATION: income needs to be boosted to increase the volume of savings: financial services need to be expanded and transformed to meet the needs of low-income earners and small enterprises. In fact the freeing up of interest rates alone faces conceptual limits set by the inability of investors to pass on their financing costs indefinitely to consumers of goods and services: Beyond levels where the price mark-ups eliminate border-price differentials, there will be a substitution of imports for domestic goods and services.

The predominance of rural personal incomes in the determination of national saving also implies another aspect of savings behaviour which is given little attention. It is symptomatic of agricultural and commodity-based income that it is unpredictable due to factors such as climatic changes and the variations in world market volumes and prices for unprocessed agricultural and mineral products. This implies that in Africa, the hump saving of the Life Cycle Hypothesis is "dented" in many places since savers must smooth their consumption in the face of substantial income volatility and risk (Deaton, 1989). Consequently, volatile incomes must imply that there is substantial probabilistic saving in the region. Policies relating to investment should thus be engendered with the flexibility and risk appropriate not only for volatility of aggregate savings but also of savings rates.

In addition, many rural household incomes have a diversity of sources, ranging from purely farming activities to an assortment of very significant non-agricultural activities, including incomes from salaries and wages. The common thread among many rural household incomes is that many have a semi-subsistence character and are also in part the result of exchanges in kind. In effect, the levels of income are sometimes so low that postponement of consumption to the future has close to zero elasticity with respect to higher real interest rates. In the Kenya survey for example, it was shown that non-financialised incomes and expenditures were 42 and 36 per cent, respectively. Monetised savings were only 32.1 per cent of the total savings. Furthermore the composition of the financialised savings showed that it is non-agricultural rural economic activities which dominated the monetised part. At least for Kenya, this engenders the latter type of household income with a greater capacity to respond with higher Mobilization of savings induced by market incentives in the financial system than is the case with household incomes from purely farming enterprises.

In general however, the considerable savings potential which the rural sector can yield in the context of economic recovery requires a wider range of policy approaches than would be the case if the highly monetised personal saving from urban households dominated total national savings. In the current setting of low access to banking services and low levels of monetisation of incomes and expenditures in the rural sector, the usual financial incentives for higher savings, such as higher real interest rates, (notwithstanding the theoretical ambiguities discussed above) can only elicit weaker responses than would be the case in high income countries. Policy actions on the supply side in the rural sector, could possibly be effective. In this context, interest rates are only one item in a list of production considerations which need to be ameliorated in the enhancement of household incomes, and thus the underlying base for national savings Mobilization. There is considerable scope for other actions such as increased

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access to input supply and the stabilization of producer and consumer prices, all of which may be of greater importance to production efficiency than the investment discipline of market-oriented credit costs. It should be remembered that one way of increasing real interest rates is to increase supplies and thus dampen inflation rates rather than simply manipulate nominal interest rates.

Another aspect of real sector problems of savings Mobilization is the tradition of income earners to finance substantial transfers to family members in the ranks of the unemployed, disguisedly unemployed and old-aged persons who are in retirement but are uncovered by retirement benefits. Regardless of other merits of the practice, the personal savings rates of workers in the Africa region are necessarily depressed (by income transfers and remittances) below the levels which their own observed personal consumptions would warrant. Transfers and remittances thus constitute a fraction of disposable income which goes to neither the savings of income earners nor to their expenditures.

The corporate component of private saving has similar idiosyncrasies. Although we have little information on this aspect of national saving, own-financing appears to be a major source of overall financing although the rates of corporate saving vary significantly among enterprises.

Public sector saving is another aspect of the real sector problem of savings Mobilization differentiated by a number of important factors. In the past two decades, the most important has been the role of non-financial public enterprises in productive activity. These enterprises were mostly set up after independence with public policy objectives, (such as indeginization of economic activity), rather than the profit motive. In the event, they have not strengthened public sector revenues, and their performance (in efficiency, productivity and managerial terms) often called for transfers from the central government, raising both the primary and total budgetary deficits and reducing public sector savings at a rate which became unsustainable by the 1980s. Their social impacts have not been properly assessed however.

The second category of problems of savings Mobilization relate to the rigidities and segmentation which permeate virtually every financial system in Africa and which act to depress the volumes of financial savings. In section I of this paper, we mentioned the observed segmentation of financial services and policies along the lines of the rural/urban dichotomy and also by the income levels. The latter problem is evident for example whenever a financial institution, including insurance firms, requires minimum deposits and/or minimum income levels. The outcome is the virtual exclusion of low-income earners from the formal financial system giving added vibrancy to the growth of informal financial sectors in most of the region's economies. These activities arose to mitigate the adverse financial conditions

faced by rural and low-income savers in the formal financial systems, and continue to operate out of the reach of financial policies.

At the macroeconomic level, one facet of financial sector constraints to savings Mobilization is the practical point of interaction between the private and public components of national saving in the domestic financial systems in Africa. In Africa, the interaction brings up many unresolved issues which affect the financial sector and progress in financial Liberalization. Relative to the private sector, governments in the region have traditionally predominated in the disposition of total financial savings (commercial bank deposits, Post Office Bank deposits, life insurance premia, National Social Security Funds and other pension funds, etc.) Governments are typically the major debtors to the financial system, and have maintained interest rates at below equilibrium levels as much to keep public borrowing costs low as to motivate private investment. Loans to government and the public sector usually outweigh loans to the private sector. In Zambia for example the central government is by far the largest beneficiary of domestic credit: in 1986, claims on central government accounted for 80 per cent of total domestic credit and claims on the private sector for 20 per cent.

The typical balance sheet of central banks in Africa shows a very substantial growth in assets in the past two decades. However, high proportions of these assets were held as claims on the governments as budget deficits increased. The fact that little is held by central banks in claims on commercial banks indicates the virtual absence of central banks in their traditional roles as "lenders of last resort" and indirect manipulators of monetary policy through money supply changes articulated with the tool of the discount rate. It also lends support to Nissanke's (1990) claim that the region's formal financial systems are marked by "excess liquidity". On the liabilities side, balance sheets are dominated by foreign assets, representing the growth of governments' external debts.

Public borrowing from the financial sector usually involves advances from the central banks and the issuing of liabilities in the form of treasury bills and (longer-termed) government stock which draw on the assets of private sector savers held as deposits in the financial system. However, in the process of keeping borrowing costs low, governments have also distorted the composition and possibly the level of private savings. Furthermore, government borrowing is almost exclusively drawn from financial savings and may have crippled the development of the financial sector in terms of competition, financial intermediation and the development of capital markets over the decades.

In terms of the distribution and efficiency of use of financial savings, economists have pointed out that the borrowing could be accompanied by financial "crowding out" effects (Aghevli et al, 1990). Evidence from Kenya (Mwega et al, 1986) has confirmed that government's share in financial

resources to finance the budgetary deficit was a source of financial "crowding out" of the private sector. Yet, these observations would seem to be contradicted for the region in general by the suggestion cited above that financial systems are marked by excess liquidity.

For the region as a whole, the shares of government in the borrowing of financial savings are sufficiently high that, unless reduced through the lowering of budget deficits, particularly the primary budgetary deficits, they could undermine the financial Liberalization process. Simply put, if high shares of (priority) government financial sector borrowing to finance budgetary deficits persist during the financial sector Liberalization process, the budgetary deficit could exert sharp upward pressures on interest rates. Paradoxically however, even the success of governments in withdrawing from high levels of borrowing from the financial sector in Africa poses new quandaries for banking and investment.

The principal source of the dilemma is the past success of governments in attracting financial savings to budgetary resources. In some cases, such as that of the financial liabilities of the extensive Post Office Savings Banks in the region, colonial and post-colonial financial arrangements ensured that virtually the entire stock of liabilities, other than working reserves, were transformed into Post Office Savings Banks assets held in the form of government stock and treasury bills. An important and geographically wide base for the Mobilization of resources, particularly small-scale savings, was thus assigned to hold assets in government paper with no room for liabilities in the form of loans and investments to develop small-scale incomes.

In Malawi for example, the Post Office Savings Bank network covers 158 post offices and 126 postal agencies. Deposit rates in the 1980s were set competitively at the same level as those paid on time deposits by commercial banks[7]. Other regulations on the investment of National Social Security Funds similarly ensured that the liabilities were invested in government paper. Many other private sector sources of financial savings, such as insurance companies, pension funds and cooperative savings associations also transformed their liabilities into assets in the form of government paper.

In the context of the financial Liberalization and structural adjustment programs in some African countries, a major target has been the reduction of government budget deficits as ratios of GDP, as well as the freeing-up of interest rates. Governments have reduced their claims on financial savings.

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7   When the government exempted taxes on interest earnings from post office savings deposits in the late 1980s, as a measure to increase the availability of financial savings to fund budgetary deficits, a very large influx of savings was attracted to the post office bank savings network. These included corporate savings.

A major investment problem has then arisen in the financial sectors of many adjusting countries concerning the re-orientation of financial savings to new channels of investment that do not emphasize government securities. For example, the problem has created the need to re-visit the underlying role of the post office savings bank institution. While the Malawi post office bank system faced an investment dilemma, an interesting solution to the problem was provided by Ghana's creation of a post office bank with operations similar to those of commercial banks. It is clear that when seen against the traditional neglect of the rural sector by financial institutions in lending policies, a re-orientation of financial savings such as post office savings banks' investments, from government securities to credit for rural economic activities, could underpin substantial output growth and new rounds of savings Mobilization.

Conclusions

In summing up, the requirements for economic recovery in Africa have come up against a changing environment in respect of resource availability. There are constraints on the availability of foreign saving, and the long-term value of a strategy of reliance on foreign resources is also questionable. On the other hand, savings behaviour in Africa seems to be weak and appears to worsen with declines in economic activity as shown for a few countries whose data was analyzed in this paper.

When set against theoretical thinking on savings, it is suggested that there are regional idiosyncrasies which alter the behaviour and outcomes in Africa. However, the most serious constraints to saving seem to emerge from the paradoxes typified by segmentation and fragmentation of the financial mechanisms in relation to the process of savings mobilization. The dualism of the financial sectors in the region seems to exclude probably the greatest potential source of national savings: deposits and lending on the small scales required by rural agricultural and non-agricultural economic activity. The dualism similarly permits a marked preference for the acceptance of business from higher income groups while shunning the majority of potential customers who have lower incomes. Traditionally this behaviour has existed because of low competition and the avoidance of small-scale transactions on the basis of their erosion profitability in financial enterprises. Contrary to the thinking suggested under the theory of "financial repression" many of regions financial systems are probably marked not by the scarcity of loanable funds but by excess liquidity. The latter condition has tended to be exacerbated by the financial liberalizations of recent years. This paper suggests that the paradoxes should be removed by providing financial services to as wide a population as possible.

Furthermore, the burden of savings Mobilization should not be placed too heavily on interest rate reforms which, in isolation, seem to have weak

impacts. Policies which boost income growth could be more important: so are increased access to financial services and the reform of financial policies to cater to local income and investment requirements.

To overcome some of the above structural obstacles to savings mobilization and recovery, some policy remedies are needed: to attune the incentives for recovery to rural agricultural and non-agricultural activities on the basis that the category of economic activity will generate succeeding rounds of increases in savings and investment: to incentivise financial institutions towards the acceptance of small scale deposits and the granting of loans to small and medium enterprises in order to bring the region's financial systems in line with national incomes and savings requirements: to invigorate the movement of loanable funds, (particularly in conjunction with financial Liberalization) to economic activity in order to mop up excess liquidity and to avoid the "bubble" effects of financial reforms which may direct resources towards speculation rather than output growth.

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