Chapter 8
Aid, Debt, and Foreign Direct Investment

When African countries achieved political independence in the late 1950s and 1960s, their citizens had high expectations. They had been promised by the nationalists and the emerging political class that the departure of the “colonial masters” would herald a new era of economic prosperity, opportunities, and better future. Prime Minister Kwame Nkrumah of Ghana proclaimed in 1959 that “We shall achieve in a decade what it took others a century…and we shall not rest until we demolish these miserable colonial structures and erect in their place a veritable paradise” (Nkrumah, 1957, quoted in Ayittey, 1999, p.7). Chief Obafemi Awolowo, a leading Nigerian nationalist and frontline politician, said that if elected Nigerian president, he would build a Disney World in Nigeria. The new political leaders were very resolute about what they intended to accomplish: an industrial economy, educated population, and modern society. In their attempts to promote economic development, postindependence African leaders faced the onerous task of mobilizing development finance, without which their aspirations would be a mirage.

This chapter discusses some of the challenges and opportunities encountered by African countries in their attempts to promote economic development in the postindependence era. It focuses on the process of mobilizing financial resources in support of development projects, as well as the recent emphasis on private capital flows.

Although the postindependence ruling class in Africa genuinely intended to deliver on their promise to build a strong economy, they faced a number of challenges. One of those challenges was the nonexistence of an indigenous business class that would serve as the linchpin for private-sector-led growth and development. Consequently, a “statist” approach, whereby the government became the major initiator of economic development, was adopted. The postindependence government took on the role of an entrepreneur, mobilizing capital, taking risks, and investing in business enterprises. But a bigger problem in postindependence Africa was the existence of what development economists refer to as the “dual-gap” problem. A dual-gap problem exists when a country’s level of domestic savings is less than its desired level
of investment. In addition, foreign exchange earnings are below the amount required for economic development. To close these two gaps, postindependence governments in Africa resorted to foreign aid, external borrowing, and foreign direct investment (FDI). The expectation was that aid and borrowing would help close the foreign exchange gap, while FDI would close the savings-investment gap.

Aid and Economic Development

Foreign aid has been central to Africa’s economic development since the 1960s. Africa has been the largest recipient of aid in the world, though aid to the region has been on the decline recently (see figure 10.4 in chapter 10). In 1990, overseas development assistance (ODA) to Africa was about $41 billion, but that amount fell to about $24 billion in 1999. ODA has begun to rise since then, reaching a peak of $51 billion in 2012. The largest recipients of aid in Africa include Egypt, Ethiopia, Tanzania, Mozambique, the Democratic Republic of Congo (DRC), and Nigeria (see table 2.2 in chapter 2). Aid to Africa has taken various forms, including the following:

**Bilateral aid**: This is a type of aid that flows from one country to multiple countries and organizations. It is usually channeled through agencies established by donor countries (see table 8.1). It was very common for a newly independent African country to receive bilateral aid from its former colonial master. Almost 85 percent of France’s ODA goes to its former colonies (Martin, 1995, p.11). It recently pledged to provide about $540 million in support of Cote d’Ivoire’s (a former colony) economic recovery (McClanahan, 2011). Bilateral aid usually has “strings” attached to it. For instance, a donor may require an aid recipient to import goods, equipment, and services from the donor country. Bilateral aid recipients are expected to formulate foreign policies that are consistent with the interests of the donor countries. Bilateral donors are quick to withdraw their aid whenever the recipient country acts in ways that are deemed to be detrimental to the donor’s values and strategic interests.2

**Multilateral aid**: A group of countries, or an organization representing several countries, may channel multilateral aid to recipients. Multilateral aid is mostly project-based, as opposed to direct cash transfers to the receiving countries. It has been used to support water projects, irrigation, education, health, research, agriculture, capacity-building, and so on. Multilateral aid agencies include the African Development Bank, World Health Organization and the World Food Program.

**In-kind versus in-cash aid**: Aid may be given “in-kind,” as when a donor country or organization sends teachers, doctors, nurses, engineers, and other professionals to African countries. When the US government sent its military to construct hospitals for the treatment of Ebola patients in Liberia in late 2014, it was offering in-kind aid. In-kind aid could also be in the form of food, clothing, and equipment donations. A rationale for this type of aid is that it helps to build the capacity of African countries to take control of their economic development. Proponents of in-kind aid argue that “in-cash” aid is