Aid dependency: how can Rwanda move toward self-sustained growth in coming years.

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Professor Collier is the co-director of IGC and the director for the Study of African Economies at the University of Oxford. From 1998-2003 he was the director of the Development Research Group of the World Bank. He is the author of three books; 'The Bottom Billion: Why the Poorest Countries are Failing and What Can Be Done About It', published in 2007; 'Wars, Guns and Votes: Democracy in Dangerous Places', published in March 2009; and his most recent book, entitled 'The Plundered Planet: How to reconcile prosperity with nature', which was published in May 2010. His research covers the causes and consequences of civil war, the effects of aid and the problems of democracy in low-income and natural-resource rich societies. Professor Collier is currently Advisor to the Strategy and Policy Department of the IMF and advisor to the Africa Region of the World Bank.

Rwanda is serious about national development; there is a "smell of success" in Rwanda which is easy to build on. Often, the hardest thing in Africa is lack of self-belief which is vital in the process of economic growth. Growth in Rwanda depends crucially on two factors: investing wisely and breaking away from isolation. Professor Collier highlighted how various sources of funding can be used and the associated disciplines they bring with them and the how the idea of 'connectedness' is necessary to transform Rwanda into a middle income country.

Linking sources of money to their uses

No country wants to be dependent on aid. However, the question "how can Rwanda overcome aid dependency?" is ill-posed. "Asking such a question is equivalent to asking someone if he has stopped beating his wife" – no answer

will leave a clean record. The issue therefore is not how can Rwanda overcome aid but rather how can Rwanda utilize the various resources available to the country to sustain its economic growth; "At what stage should aid become a less important source of finance in Rwanda's development?". The answer lies in understanding the various sources of money and the associated disciplines they bring with them.

Natural Resources: Natural resources like oil bring maximum freedom to the government in terms of its uses. It is like "manna from heaven" except that it has the potential to be "money from hell" because it brings with it plenty of room for abuse, especially if the government is not disciplined. There are various examples of such cases in Africa where oil money has resulted in corrupt governments instead of economic growth and poverty reduction. However, Botswana serves as a good example of a country which has managed its natural resources well and achieved spectacular rates of economic growth.

Taxes on citizens: Taxes are a good source of revenue and bring with them two main advantages. One is the relationship it creates

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between government and its citizens which allows citizens to scrutinize their governments and hold them accountable for the money. The second is the direct interest the government has in growing the economy in order to increase tax revenue. "We should all learn to love taxes more"

Commercial borrowing: The standard theory in commercial borrowing is to lend money only if it is going to be used well. In practice this has frequently not been the case, as evident from the Greek crisis. It hasn't provided the kind of discipline it should. Rwanda still has plenty of fiscal space for borrowing, with a low debt to GDP ratio, but in taking on additional debt it is the rate at which this borrowing occurs that is important. The key thing to note about commercial borrowing is that the perceived riskiness is what determines the rate of interest and the government needs to put in every effort at reducing the perceived riskiness of the country. This can only be done through concrete actions by the government to send the right signals to lenders.

Foreign aid: Foreign aid usually comes with interference but "the sort of interference you get is the sort that you deserve." The best way to minimize interference is to collect good evidence and be fully transparent on how the money has been spent so far. This will enable the government to have more control over this source of finance and minimize interference from donors. "Evidence is your friend" if you want more independence in managing aid money, successes should be celebrated and failures revealed with their associated lessons.

Public risk bearing capital: Examples of which include the IFC, FMO, COC, Abu Dhabi, China etc. These are all attractive sources of money as they represent a halfway house between commercial borrowing and development assistance: they offer more freedom than development assistance at a lower cost than commercial borrowing. Rwanda should also try and break into the IBRD if possible.

PPPs: This is a popular source of finance that should be handled with caution. Common problems with PPPs include: (1) contractors can change their terms once the project has begun, driving up the cost substantially; (2) incentives for corruption are high because amounts of money are large and technical details make public oversight difficult; and (3) PPPs are an expensive source of finance when compared to concessional financing or other alternatives. Chile, one of the countries with the most technically qualified public sector and lowest corruption rankings in the world and at the forefront in PPPs, was hit by a major corruption scandal that ended with a Minister in jail. Having good legislation with clear rules, a technical team with legal and economic expertise during contract bidding and negotiation, and ensuring maximum transparency for public accountability are key.

FDI: The key to attracting foreign direct investment is in sending the right signals to potential investors. This involves bragging about what you have done so far and why your country is an attractive place for investment.

Domestic savings: Savings can be hard when the population is largely poor but there are many instances of high savings among poor people (eg, China). Rwanda needs to create clean and simple institutions that ordinary people can access in order to encourage more savings. Building societies in the UK served that purpose whereby ordinary people came together to form cooperative savings groups instead of having to deal with commercial banks. Building societies are particularly well suited because of their simple operations that both clients and employees could easily understand.

Understanding these sources of money and linking them to their various uses will help Rwanda manage its finances better and tap into the potential that these sources provide.

Moving to an integrated economy – 'connectedness'

Rwanda at present is a small isolated economy. The isolation comes from a lack of good transport linkages with its neighbours. The problems of isolated economies are different and a large part of the writing on growth is often not relevant to Rwanda. There is not a single small isolated economy in the world today that is middle income. What is required then to transform into a modern economy are (a) economies of scale and (b) interdependence of activities.

Rwanda is doing a good job of growing its current set of activities but it needs to break into new activities which have both economies of scale and are interdependent. With a small national market, achieving scale economies requires stepping up exports. For this to be achieved, Rwanda needs to radically lower its transport costs through improving its rail, road and air links. Most cost-benefit analyses will not pick up the long term benefits accruing from such investments and this needs to be taken into account while evaluating such investments. There is tremendous potential for Rwanda to develop an integrated regional transport network with its neighbours.

The IGC in Rwanda

The IGC is directed and organized from hubs at the London School of Economics and Oxford University and is funded by UKaid from the Department for International Development (DFID). The IGC was created to provide demand-led policy advice based on frontier research.

The IGC's Rwanda country office was established in November 2010, and the core team includes Country Director, Richard Newfarmer, Lead Economist Mans Soderbom and Country Economists Jonathan Argent and Michele Savini. The IGC's activities in support of government programmes focus on four core thematic areas: trade and diversification; agriculture; infrastructure; and finance.