

# **Governance and Economic Growth in Cameroon**

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# 1. Introduction

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The socioeconomic conditions in sub-Saharan African countries deteriorated sharply during the 1980s, a decade that is widely regarded as Africa's "lost decade" of development opportunities (Iyoha, 1999). During this period, the economies of most countries in the region collapsed, in spite of the agenda for action the World Bank and other concerned organizations and donors had come up with (World Bank, 1981). Two reasons have been given for the collapse of these economies: (a) external—oil price shocks, economic slowdown in the Organisation for Economic Co-operation and Development (OECD) countries and the collapse of world commodity prices; and (b) internal—poor management and the failure or inability of many of these countries to adapt to the changed external environment. The countries of the sub-region could not realign their domestic policies to meet the changing situation of the world, driven by the forces of globalization.

Many countries in the sub-region, including Cameroon, responded with structural adjustment programmes (SAP) supported by the World Bank and the International Monetary Fund (IMF). These measures were aimed at inducing growth, restoring price stability and reducing external imbalances. However, the SAP measures have not produced the intended results. Whether this is because they were introduced somewhat brutally without adequate preparation or because of socio-cultural and socio-political reasons or both, they have led to the rapid accumulation of debts, leading to heavy indebtedness, and exacerbating the poverty in many of the countries. The yoke of debts—debt burden—has crowded out investments in many instances, and reduced most of these countries to heavily indebted poor countries (HIPC). This is the situation Cameroon finds itself in today.

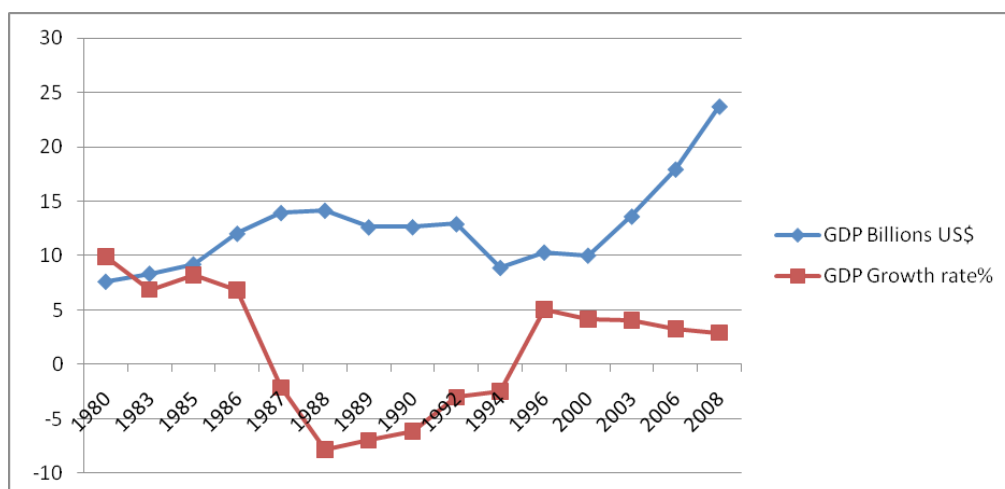
In the 1980s, development assistance shifted to a large extent from financing investment projects (roads, dams, etc) to promoting policy reform. This reorientation arose from a growing awareness that developing countries were held back more by poor policies and even a lack of goodwill to implement the policies than by a lack of financial resources for investment. Poor policies breed poor governance and create an appropriate environment for rent-seeking. Today, donors are putting more emphasis on governance. This has become topical, and the New Partnership for Africa's Development (NEPAD) has embraced it as one of its main initiatives. To reinforce this, the African Peer Review Mechanism (APRM) was introduced.

## Problem statement

Cameroon has the potential to become one of the fastest developing countries in sub-Saharan Africa. It is endowed with a significant resource base—petroleum, forests, mineral deposits, a rich agricultural base and sufficiently skilled human resources. It is also one of the few countries in Africa that has not had any serious political turbulence. Unfortunately, this has not translated into economic progress: instead, the country has retrogressed in the past couple of decades, and today Cameroon is among the few African countries under observation for having reached the heavily indebted poor countries initiative completion point. Until 1985–1986, the country’s economic growth was strong, by conventional measures, resting on the production and export of natural resources and later on the expansion of the petroleum sector. However, in 1985–1986, petroleum revenues dropped owing to the simultaneous reduction in prices and dwindling number of exploitable sites. At the same time, the terms of trade for crop exports declined. The slowing down of the economy brought to the fore serious structural and mismanagement problems that the economy had been facing.

Three major shocks after 1986 exposed Cameroon’s weaknesses in economic structure and policies. First, the external terms of trade declined by 60% through 1993 as the prices of coffee, cocoa, and oil fell sharply. Second, oil output dropped, and thirdly, the real exchange rate appreciated by about 54% over the period 1986–1993.

**Figure 1: GDP (billion US\$) and GDP growth rate (%), 1980–2008**



The government embarked on a series of economic reform programmes supported by the World Bank and IMF beginning in the late 1980s. By 1993, no significant improvements were apparent. The economy had deteriorated significantly: continuous public finance deficits were generated, as falling revenues were not matched by expenditure cuts. The burden of public finance was exacerbated by a large inefficient and corrupt public enterprise sector. In addition, the growing economic decline was accompanied by increasing poverty. The government decided to take the draconian, but unfortunate, measure of slashing nominal civil service salaries by over 60% in 1993.

This was followed by a 50% devaluation of the CFA franc—the currency used in the franc zone—in 1994.

All these measures did not move Cameroon out of its demise because: (a) governance issues were not included in the measures; (b) the government failed to meet the conditions of the first four IMF programmes or implemented some of the measures late and therefore out of synchronization; and (c) slashing civil servants' salaries led to rampant rent seeking, as the civil servants tried to maintain consumption at the same level as before the salary cuts and devaluation. Workers were also generally demoralized and no longer productive. The situation deteriorated as the debts (external and internal) accumulated even after the country had rescheduled its loans a number of times. Eventually Cameroon qualified as a heavily indebted poor country, and was enlisted to benefit from the HIPC forgiveness programme in 2006. Added to the economic situation was the growing corruption in the public sector, political repression and limited liberties. In 1998 and 1999 Transparency International classified Cameroon as the most corrupt country in the World. From 1976 to 2006, Freedom House classified Cameroon as a country that was not free, based on its political right and civil liberty indices. These two organizations underscored issues of bad governance in the country.

Pressure from international donors and civil organizations led the government to accept that without tackling the governance issues along with implementing the structural adjustment measures, no positive results could be expected. In 1992, the American Embassy said that while Cameroon's long-run development potential was great, "it will require political and economic liberalization to be realized, greater transparency and accountability in government, an independent judiciary, and improved definition and enforcement of contracts and property rights" (American Embassy in Cameroon, 1992). It is now fairly well known that since economic management is hampered by a lack of transparency and political accountability rooted in a still incompletely democratized political system, further democratization would facilitate recovery. In 1998, the government reluctantly adopted a National Governance Programme, with a mission to fight corruption, ensure the rights and liberties of the citizens, etc. In his New Year message to the Cameroon nation in 2005 and 2006, the President of Cameroon recognized that governance was at the root of the problems the nation was facing. On New Year's Eve in 2005, he said that the principal cause of the mitigated economic growth Cameroon was facing was inertia, which had perverted the Cameroonian bureaucracy: it was not the lack of resources—human or financial. On New Year's Eve 2006, the President acknowledged that without fighting corruption, the nation was unlikely to enjoy the economic growth needed to alleviate the poverty rate, currently 40%.

A number of studies on Cameroon have concentrated on examining socio-economic factors affecting economic performance, with very little emphasis on the institutional dimension and particularly the role good governance plays (Amin, 1998; Kobou, 2000; Doh, 2000). This study was conceived on this background and has examined those elements embodied in governance, relating them to economic performance in Cameroon. Specifically, the study is structured to provide answers to some basic questions:

- How is governance affecting the economic performance of the nation?
- What should be done to improve the governance and ensure sustainable economic growth for the country?

## Objectives

The main objective of this study was to determine how governance has affected economic growth in Cameroon. The specific objectives of the study, therefore, were to:

1. Establish that there is a relationship between governance and economic growth;
2. Identify the obstacles to good governance and how these impede economic growth; and
3. Make proposals on the way forward.

## Justification for the study

Good governance is indispensable in enhancing the effectiveness of government operations and in stimulating private investment, and therefore, growth. The government is aware that it is critical to proceed vigorously to tackle issues of economic governance and transparency as a core component of the reform programme being carried out in the country. Thus the promotion of good governance is at the centre of many of the reforms being undertaken by the government, particularly in the areas of public expenditure management, the liberalization of markets, and the introduction of transparency and accountability into public life.

The interest in this topic, therefore, arises from the apparent interest indicated by the state through the adoption of a National Governance Programme in 1998. As part of its activities, the programme has ensured that anti-corruption notices are posted in all public buildings. Furthermore, the programme holds seminars to educate Cameroonians on their rights. Also serving as motivation for this study is the enormous potential Cameroon has to get out of poverty and onto a sustained growth path: the country has yet to achieve this, mostly because of poor governance in the management of state affairs. Research by Freedom House has determined that for the past 30 years or more, political and civil liberties have been very restricted in Cameroon. Since 1966, Cameroon has mostly been a one-party state, with nearly all the powers concentrated on the President. The population has not had any real opportunities to change leadership. With a rapidly changing environment, the status quo cannot continue to prevail, so this study is timely. The findings should provide some sense of appreciation of the impact of governance issues on the welfare of Cameroonians, and should also contribute to the debate on governance and economic growth.

## 2. Review of literature

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Reformers in many governments, the civil society and investors increasingly view governance as key to development and a conducive investment climate, which in turn has increased the demand for monitoring the quality of governance in a country over time (Kaufman et al., 2005). Good governance is “epitomized by predictable, open, and enlightened policy making (that is, transparent processes); a bureaucracy imbued with a professional ethos; an executive arm of government accountable for its actions; and a strong civil society participating in public affairs, and all behaving under the rule of law” (World Bank, 1994a). Recent work has addressed the impact of institutions on the level of GDP per capita (Knack, 2002; Edison, 2003). These authors established that the quality of governance has a strong and unequivocal impact on economic performance.

McNab and Everhart (2002) argue that “a functioning private sector requires the rule of law; enforcement of property rights and contracts; an independent, strong judiciary with transparent and effective bankruptcy procedures; transparent tax systems; effective bank supervision; and the strict enforcement of bank prudential regulations.” These are the hallmarks of good governance, regardless of the formal definition. Fostering such an environment not only reduces opportunities for corruption, but, more importantly, the returns from corruption. Each of these, in turn, stimulates investment, lowers transaction costs, and facilitates economic growth.

Donors have realized that aid flows have a stronger impact on development in countries with good institutional quality, and thus increasingly utilize measurable performance indicators (governance) for monitoring, evaluation and decision-making at country level. On foreign aid and governance, McNab and Everhart (2002) state that foreign aid that is subject to conditions, such as that offered by the large multi-lateral international donor agencies, may create sufficient incentives for receiving governments to improve institutions, governance and economic efficiency. This is because a government that wishes to reform but lacks the political will to do so may be able to move forward with reform by accepting foreign aid. Collier and Gunning (1997), and Easterly and Lavine (1997), however, argue that attaching conditions to foreign aid does not improve governance. The conditions attached to foreign aid may also not be static, that is, they may be adjusted over time in response to economic conditions in the recipient country.

Improving governance is a difficult but necessary task in increasing efficiency and promoting economic growth. McNab and Everhart (2002) found that a 1% change in the quality of governance appears to induce a 4% change in the rate of economic growth. For a country currently growing at 2% per annum, a 10% increase in the governance score would raise the growth rate to approximately 2.9% per annum.

Countries that ignore the rule of law, let red tape interfere with free-market commerce, and let corruption run rampant cannot improve the rate of economic growth without first addressing the problems of governance. As governance improves, the marginal return to improving governance eventually falls. A monotonic relationship, therefore, does not exist between good governance and economic growth. Past some point, resources will enjoy a higher rate of return when invested in human and physical infrastructure, but without improvements in governance, these returns cannot occur.

Gradstein (2003) uses a household model to show that enforcement of property rights (proxy for governance) will lead to growth. His paper shows that for countries with poor governance and high levels of corruption, investments in physical and human capital will not produce the same rate of return as investments in governance and anti-corruption efforts.

The transmission channel from corruption to growth is clear. Corruption lowers the quality of governance. As the quality of governance declines, economic growth declines at a faster rate. The policy prescription is clear: actions to combat corruption and enhance the quality of governance are likely to enhance economic growth. The efficiency of government institutions cannot easily be quantified. Corruption, the most important variable in governance, is by its very nature difficult to measure. Although indices to measure corruption are typically based on standardized questionnaires designed by consultants, and are therefore somewhat subjective, they are indicative of the extent to which corruption may permeate economic interactions. Corruption arises when distortion in the economy creates a shortage, raising the value of a desirable good. For example, quantitative restrictions on imports make import licences very valuable; importers may then be willing to bribe the relevant official to obtain them. Protection of domestic industries from international competition generates rents that local entrepreneurs may be willing to pay for in the form of bribes (Mauro, 1995). Greater openness in an economy as measured by the sum of imports and exports as a share of GDP is significantly associated with lower corruption.

Government subsidies, price controls, multiple exchange rate systems and foreign exchange allocation schemes also cause rent-seeking (Mauro, 1995). When civil servants are poorly paid, they may be obliged to use their positions to collect bribes, especially when the expected probability of being caught and punished is low (Kraay and Van Rijckeghen, 1995; Haque and Sahay, 1996). In 1993, civil service salaries in Cameroon were slashed by about 60%. Corruption immediately became the order of the day, leading to the country being classified as the most corrupt nation in the world by Transparency International in 1998 and 1999. Since then, Cameroon has continued to be among the most corrupt nations in the world. This action by the Cameroonian authorities proved the IMF Fiscal Affairs Department right: the IMF had warned that across-the-board civil service wage cuts could lead to a rise in corrupt behaviour.

Bardham and Mookherjee (2000) state that corruption in the delivery of public services in developing countries has frequently been argued to result from over-centralization and lack of suitable information systems required for the effective oversight of the behaviour of bureaucrats. They suggest the devolution of power to local authorities better informed about local conditions. In Cameroon, the President has ultimate power and is practically above the legislature and the law.

A few empirical studies present empirical evidence that the quality of governance has a robust effect on growth. Early contributions include Barro (1997), Knack and Keefer (1997a, b), Mauro (1995) and Svensson (1998). More recent and detailed supportive evidence is provided in Chong and Calderon (2000) and in a working paper by Kaufmann et al. (1999a), whose authors find that a one standard deviation increase in any of their governance indicators causes between a two-and-a-half and fourfold increase in per capita incomes. This relationship can be manifested through several channels. Knack and Keefer (1997b) and Mauro (1995), for example, find that poorly protected property rights affect physical investment. King and Levine (1993) and Demirguc-Kunt and Maksimovic (1998) present similar evidence with regard to investment in financial assets. Evidence on the reverse relationship, from income to corruption, can be gauged using Kaufmann et al. (1999b), who provide a data set on the quality of governance across more than 150 countries, exhibiting six measures of the quality of governance.

Because of the data problems, most studies recognize that different observable measures of the quality of governance can be construed only as proxies for the variable of interest, and all studies are aware of the simultaneity of the relationship between these measures and growth. A study by Hall and Jones (1999) is rooted in growth accounting and focuses on cross-country differences in income per capita arising in a steady state. It employs subjective evaluations of aspects of governance, such as bureaucratic efficiency, corruption, and maintenance of law and order, supplemented by the degree of openness to international trade. The authors use various geographic and linguistic measures of the effect of Western culture as instruments. Using cross-sectional evidence for 127 countries, the paper presents robust findings on the positive effects of good governance on growth, which significantly supplements the effect of physical and capital accumulation. The extent to which a country was exposed to Western influence plays a crucial role in its ability to design proper institutions for good governance (Hall and Jones, 1999). The study by Kaufmann et al. (1999a) is similar in many respects. It uses an enlarged data set and constructs a much wider battery of measures of governance quality based on a variety of (subjective) sources. This study's conclusions generally reinforce the results from the study by Hall and Jones (1999). Chong and Calderon (2000) explicitly test for the mutual causality between good governance and growth, suggesting "multiple institutional equilibria", whereby good institutions promote growth, which then leads to the adoption of good institutions. They conclude that causality runs in both directions, providing tentative support for the theoretical claim they make. Kaufman et al. (2005) have used a large data set to construct governance indicators based on a broad definition of governance.

In their study of foreign direct investments in Cameroon, Khan and Bamou (2005) found that a number of reasons appear to explain the poor performance of the country in terms of FDI attraction despite the generous incentives offered by the regulatory and institutional framework, especially from the 1984 Investment Code and the Free Trade Zone regime. These reasons are: the state's non-respect for tax and customs commitments created an atmosphere of suspicion and loss of confidence between it and interested economic operators; the limited autonomy and resources of the body set up to manage the free trade zone; the socio-political instability within the Central African sub-region, including in Cameroon, in the early 1990s; corruption; poor governance; administrative

bottlenecks; and finally, the silence observed by the government regarding the setting up of accompanying structures and the texts of application to the Investment Charter. Governance, whether bad or good, is the result of a combination of factors, some of which may not be measurable. Nevertheless, the progress of nations is greatly affected by governance.

## 3. Methodology

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### Conceptual and analytical framework

**B**efore looking at the governance situation in Cameroon, we present four sequences via which different dimensions of the interactions between economic and governance dynamics might interact and evolve over time: (1) state capacity-building provides a platform for accelerated growth via improved public sector performance and enhanced credibility for investors; (2) reshaping the country's political institutions to enhance accountability and reduce the potential for arbitrary discretionary action will shift expectations in a positive direction; (3) not seeking to anticipate and address in advance all possible institutional constraints, but addressing specific capacity and institutional constraints as and when they become binding; and (4) engaging the civil society, which should give the state a stronger capacity to fight corruption, ensure better public services, improve political institutions more broadly and subsequently unlock the constraints on growth.

Because of data constraints, we looked at the governance situation of Cameroon, vis-à-vis other countries with similar characteristics. In this study, we used Botswana and Senegal. Botswana is a resource-rich (diamonds) sub-Saharan African country that at independence had about the same GDP per capita as Cameroon (which is also a resource-rich country with petroleum and timber). Senegal is also a sub-Saharan African country and is French-speaking like Cameroon, but has relatively fewer resources than Cameroon. Being French-speaking is also important because the colonial policies of France and Britain were different, and these differences continue to be reflected in the behaviour of the former colonies. Next, we looked at studies that have been carried out to show the impact of governance on economic performance. Because time series data on governance cover a short period, we were unable to carry out any time series model estimation. Rather, we took cross-country estimations by other authors and fitted data from Cameroon, Botswana and Senegal to determine the performance of Cameroon in comparison to these two countries over time. We therefore used a cross-country approach to produce a time series outcome. To examine the relative importance of governance as a determinant of economic performance, we adopted the econometric frameworks of Knack (2002), Edison (2003), Baliaoune-Lutz (2005) and Easterly et al. (2006). These are the studies we found most appropriate for our work. We also estimated a growth model using the International Country Risk Guide's (ICRG's) Cameroon data, based on an adaptation of the Knack model to support findings of the comparative cross-country models.

The most ambitious attempt to handle the data issue posed by governance variables that are based on perceptions, and therefore are qualitative, is that of Kaufmann et al. (2006). They have identified indicators that measure six dimensions of governance: (1) voice and accountability; (2) political instability and violence; (3) government effectiveness; (4) regulatory quality; (5) rule of law; and (6) control of corruption. The construction of these six aggregate governance indicators was motivated by a broad definition of governance as the traditions and institutions by which authority in a country is exercised. This includes: (1) the process by which governments are selected, monitored and replaced; (2) the capacity of the government to effectively formulate and implement sound policies; and (3) the respect of citizens and the state for the institutions that govern economic and social interactions among them. This classification of indicators into clusters corresponding to this definition reflects their views of what constitutes a consistent and useful organization of the data that is concordant with prevailing notions of governance.

The first two governance clusters are intended to capture the process by which those in authority are selected and replaced. Kaufmann et al. (2006) refer to the first of these as “voice and accountability”, and included in it are a number of indicators measuring various aspects of the political process, civil liberties and political rights. These indicators measure the extent to which citizens of a country are able to participate in the selection of governments. Also included in this category are indicators measuring the independence of the media, which plays an important role in monitoring those in authority and holding them accountable for their actions.

The second governance cluster is labelled “political stability and absence of violence”. In this index, Kaufmann et al. (2006), combine several indicators which measure perceptions of the likelihood that the government in power will be destabilized or overthrown by possibly unconstitutional or violent means (including domestic violence and terrorism) or both. This index captures the idea that the quality of governance in a country is compromised by the likelihood of wrenching changes in government which not only have a direct effect on the continuity of policies, but also, at a deeper level, undermine the ability of all citizens to peacefully select and replace those in power.

The next two clusters summarize various indicators of the ability of the government to formulate and implement sound policies. In “government effectiveness” Kaufmann et al. (2006) combine responses on the quality of public service provision; the quality of the bureaucracy; the competence of civil servants; the independence of the civil service from political pressures; and the credibility of the government’s commitment to policies. The main focus of this index is on “inputs” required for the government to be able to produce and implement good policies and deliver public goods. The second cluster, which they refer to as “regulatory quality”, is more focused on the policies themselves. It includes measures of the incidence of market-unfriendly policies, such as price controls or inadequate bank supervision, as well as perceptions of the burdens imposed by excessive regulation in areas such as foreign trade and business development.

The last two clusters summarize, in broad terms, the respect of citizens and the state for the institutions which govern their interactions. This is captured by “rule of law.” In it, they include several indicators which measure the extent to which agents have confidence in and abide by the rules of society. These include perceptions of the incidence of crime; the effectiveness and predictability of the judiciary; and the enforceability of contracts.

Together, these indicators measure the success of a society in developing an

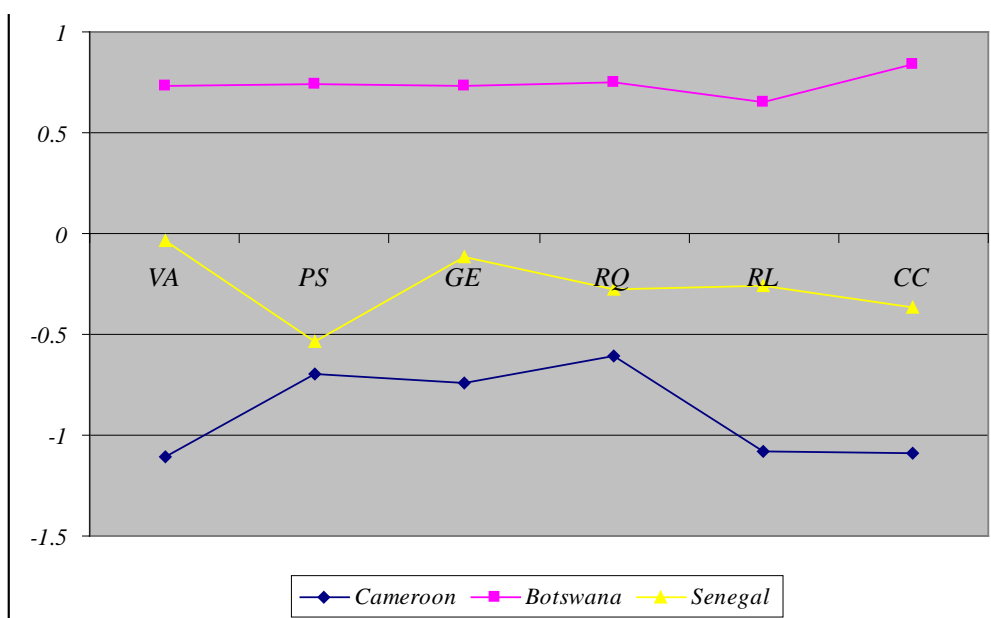
environment in which fair and predictable rules form the basis for economic and social interactions, and importantly, the extent to which property rights are protected. Kaufmann et al. (2006) refer to the final cluster as “control of corruption”. This measures perceptions of corruption, conventionally defined as the exercise of public power for private gain. The presence of corruption is often a manifestation of a lack of respect of both the corrupter (typically a private citizen or firm) and the corrupted (typically a public official or politician) for the rules which govern their interactions, and hence represents a failure of governance according to their definition.

## 4. Results: Situational analysis

Figure 2 shows the six governance indicators for Botswana, Cameroon and Senegal. The table depicts the percentile rank on each governance indicator as developed by Kaufman et al. (2006). Percentile rank indicates the percentage of countries worldwide that rate below the selected country (subject to a margin of error): higher values indicate better governance ratings. Percentile ranks have been adjusted to account for changes over time in the set of countries covered by the governance indicators.

Cameroon performs consistently worse than the other two countries in all the categories and over the years. Considering all countries in the data set, Cameroon falls within the bottom 20% in governance matters, while Botswana falls within the top 20%.

**Figure 2: A profile of the quality of governance**



Key for acronyms: VA –Voice and Accountability; PS- Political Stability; GE – Government Effectiveness; RQ Regulatory Quality; RL – Rule of Law; CC – Control of Corruption

Cameroon fares worse than Botswana and Senegal in all six indicators, with wider disparities in voice and accountability, rule of law, and control of corruption.

Since 1972 Cameroon has been a *de facto* one-party state, meaning that the citizens have not been free to choose leaders of their choice. Since Transparency International classified Cameroon as the most corrupt country in the world for two years running in the late 1990s, it is no surprise that the level of corruption continues to be very high. Corruption and lack of respect for the rule of law are mutually reinforcing. In recent times, governance deficiencies such as problems with the rule of law, corruption and ineffective provision of public services have accounted for a large proportion of the difference, not only in income inequality but also in voter turnout and civil participation, with civil participation undermining the very foundations of civil society.

**Figure 3: International Country Risk Guide (ICRG) governance measures**

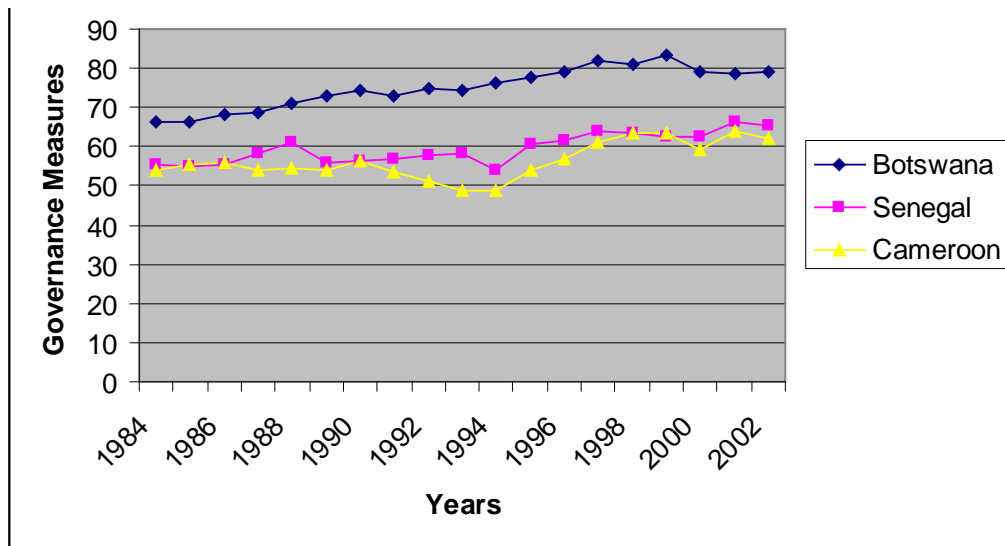


Figure 3 presents another measure of governance, based on scores that capture political, economic and financial risk. This governance measure (ICRG) is produced by Political Risk Services (PRS)<sup>1</sup> and is derived from scores given by a panel of international investors. The scores range from 0 (the worst case) to 100 (the best case). Cameroon again fares worse than Botswana and Senegal on this governance measure.

As can be seen from Figure 2, Cameroon fares worse than Botswana and Senegal in a Freedom House ranking of countries pertaining to political rights and civil liberties.

## The impact of governance on economic growth

The above analysis shows that governance has been generally poor in Cameroon. We will now try to show the impact of governance on economic performance in the country. We first looked at the model by Easterly et al. (2006). In their study of social cohesion, institutions, and growth, they specified the following two models which enabled them to verify a two-stage hypothesis that more social cohesion leads to better institutions, and better institutions in turn lead to higher growth:

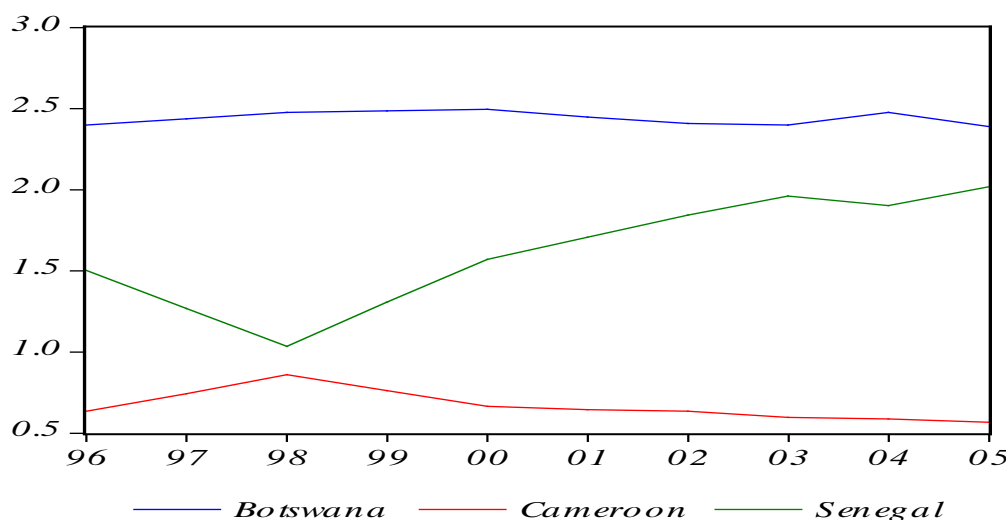
$$\begin{aligned} \text{Institution} = & \alpha_0 + \alpha_1(\text{Ethno-linguistic Fractionalization}) \\ & + \alpha_2(\text{Middle-class Share}) + \varepsilon \end{aligned} \quad (1)$$

$$\text{Growth} = \beta_0 + \beta_1(\text{Institutions}) + \mu \quad (2)$$

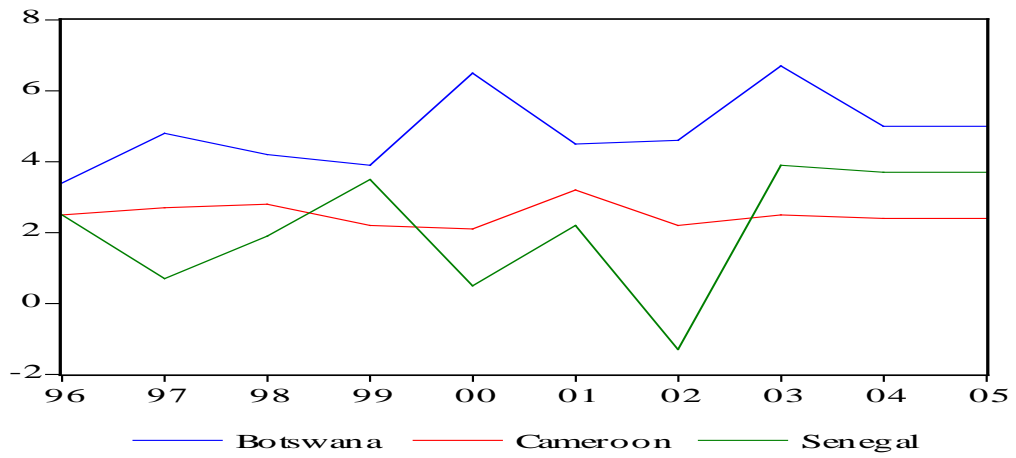
where *Institution* is a composition of various institutional measures comprising mostly perception measures of the governance indicators constructed by Kaufmann, Kraay, and Mastruzzi (2005). *Growth* is the annual GDP per capita growth rate. We found the second specification [2] relevant to our study. Easterly et al. (2006) use the three-stage least squares (3SLS) to take into account the possible endogeneity of institutions: the two indicators of social cohesion (see [2]) make natural instruments that allow them to identify a causal link from good institutions to growth. The instruments pass two over-identification tests for whether they are excludable from the final regression. Using 3SLS regressions, Easterly et al. (2006) obtain the estimated parameters of their model [1] and [2] (see Appendix 1).

Their findings show that all measures of institutional quality are positively associated with growth, which confirms *a priori* expectation. We adapt these results to the data on governance measures (Table 1) for Botswana, Senegal and Cameroon, in an effort to assess the trends of the impact of governance on economic growth in Cameroon. Figures 4 through 9 indicate that Cameroon does poorly in its governance measures vis-à-vis Botswana and Senegal. Control of corruption, government effectiveness and political stability appear to be affecting economic growth negatively in Cameroon.

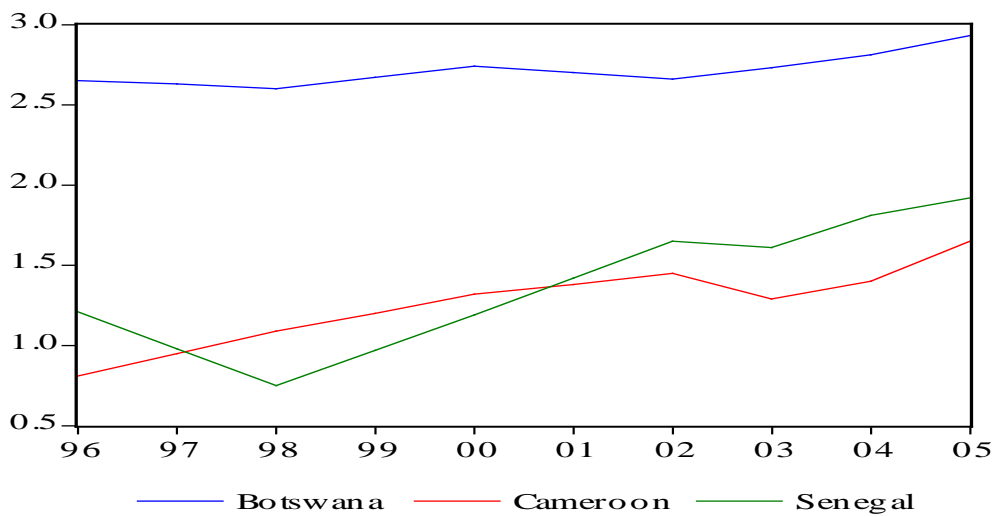
**Figure 4: An impact analysis of voice and accountability on growth**



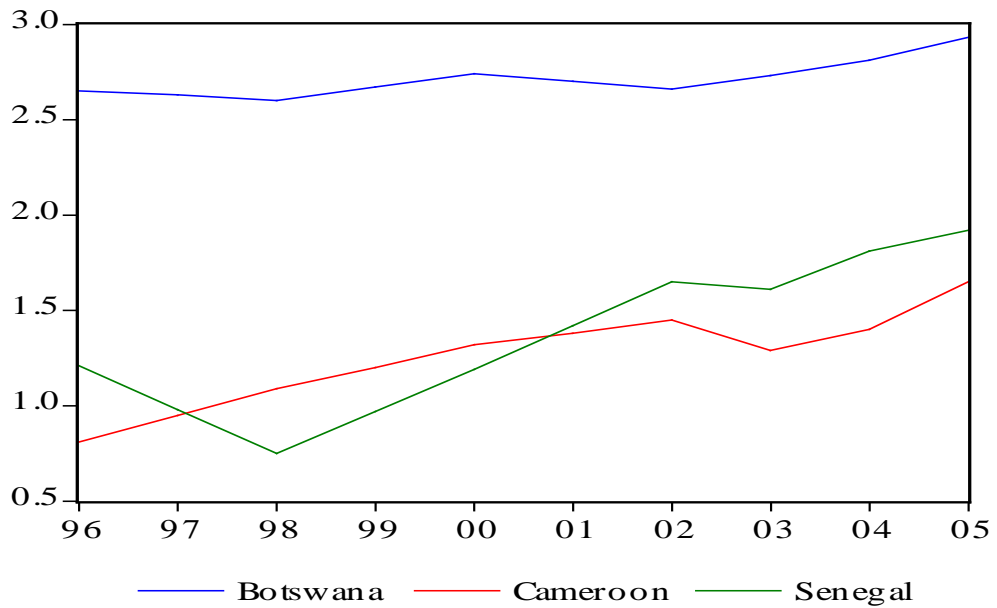
**Figure 5: An impact analysis of government effectiveness on growth**



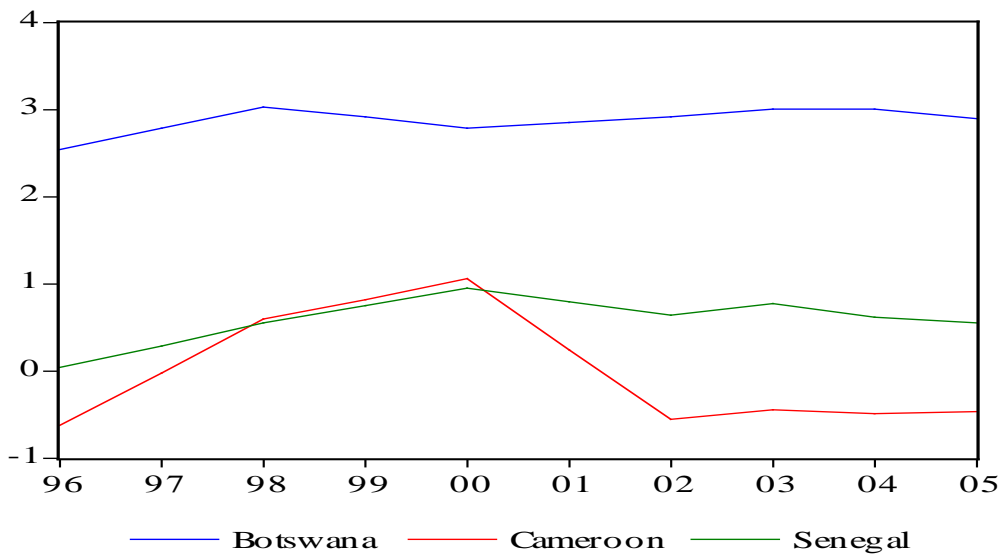
**Figure 6: An impact analysis of the control of corruption on growth**

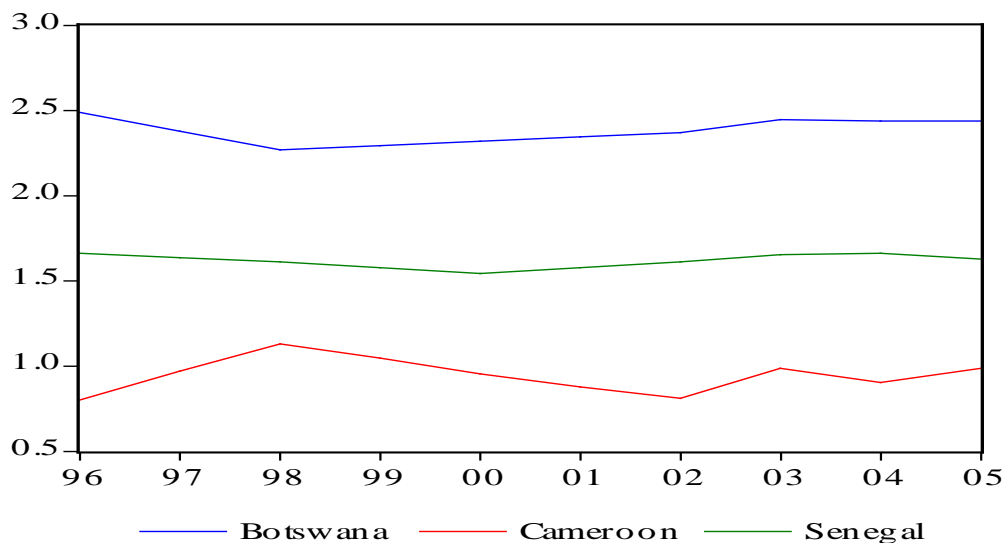


**Figure 7: An impact analysis of political stability on growth**



**Figure 8: An impact analysis of regulatory quality on growth**



**Figure 9: An impact analysis of the rule of law on growth*****The Knack (2002) model***

The dependent variable in this model is the average annual growth in per capita income over the 1980–1999 period. Regressors include: (1) the ICRG quality of governance index, averaged over 1982–1997; (2) initial GDP per capita; (3) average educational attainment of the over-25 population, averaged over 1980, 1985, 1990 and 1995; (4) the log of inflation, averaged over 1980–1998; (5) the year-to-year variability of inflation (coefficient of variation) over 1980–1998; (6) M2/GDP, a standard measure of financial development, averaged over 1980–1998; and (7) exports/GDP, averaged over 1980–1998. Implicitly stated, the model is:

$$Y = f(x_i) + \mu \quad i = 1, 2, \dots, 7 \quad (1)$$

The model is explicitly stated as follows:

$$Y = \beta_0 + \beta_1 x_1 + \beta_2 x_2 + \beta_3 x_3 + \beta_4 x_4 + \beta_5 x_5 + \beta_6 x_6 + \beta_7 x_7 + \mu \quad (2)$$

$\beta_i$ ,  $i = 0, 1, 2, \dots, 8$  are parameters to be estimated.

Knack (2002) obtained the estimates of the parameters of Equation (2) using cross-country data. Hence, the estimated model is stated as follows:

$$\hat{Y} = -3.136 + 0.150x_1 + 0.280x_2 + 0.214x_3 - 0.214x_3 - 0.274x_4 + 0.018x_6 - 0.002x_7 \quad R^2 = 0.47$$

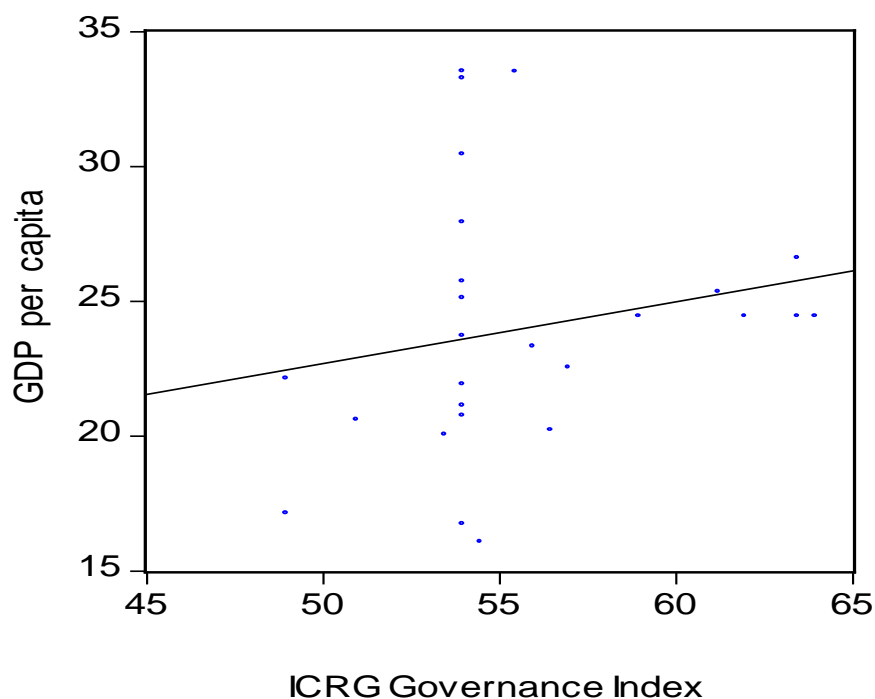
$$(1.114) (0.044) (0.086) (0.116) (0.134) (0.222) (0.009) (0.009) \quad (3)$$

$$n = 79$$

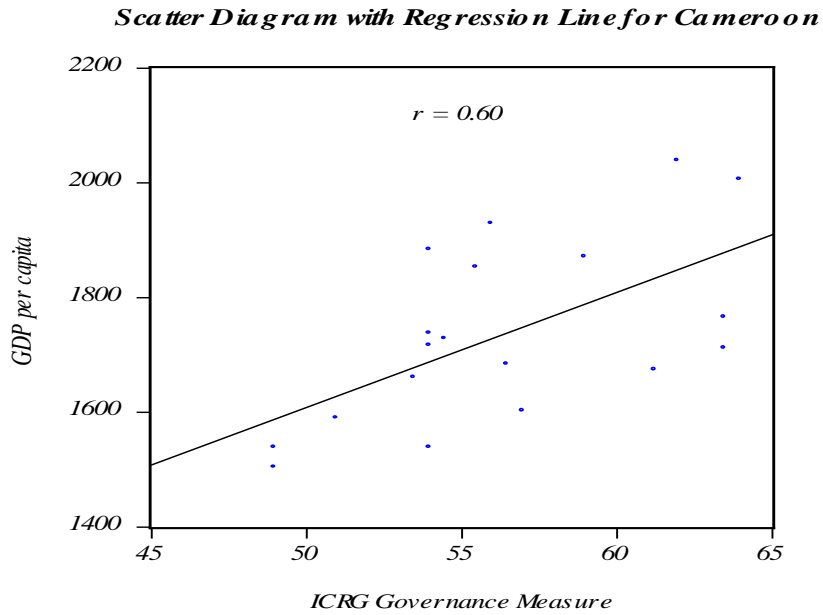
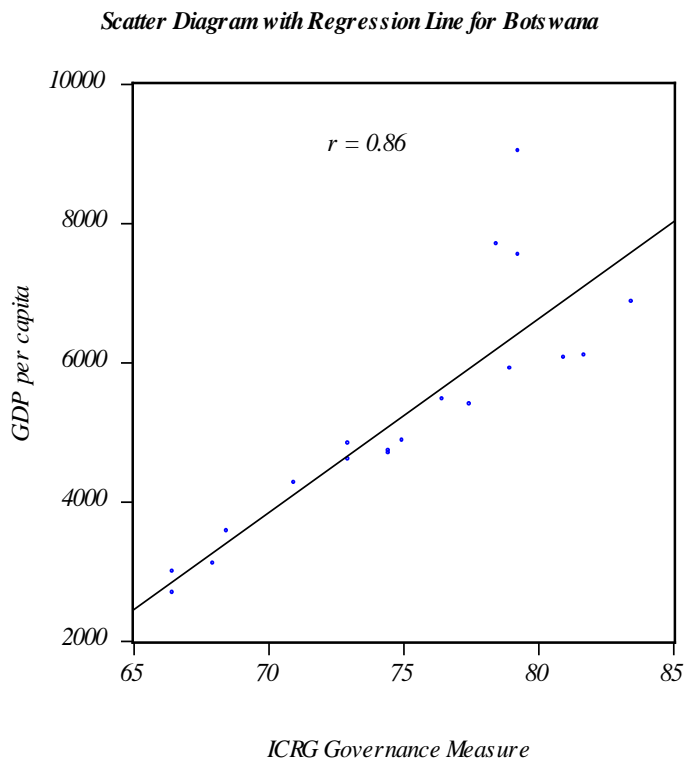
The values in parentheses are standard errors of estimated parameters, and these errors are adjusted for heteroskedasticity.

**Figure 10: The impact of governance on GDP per capita**

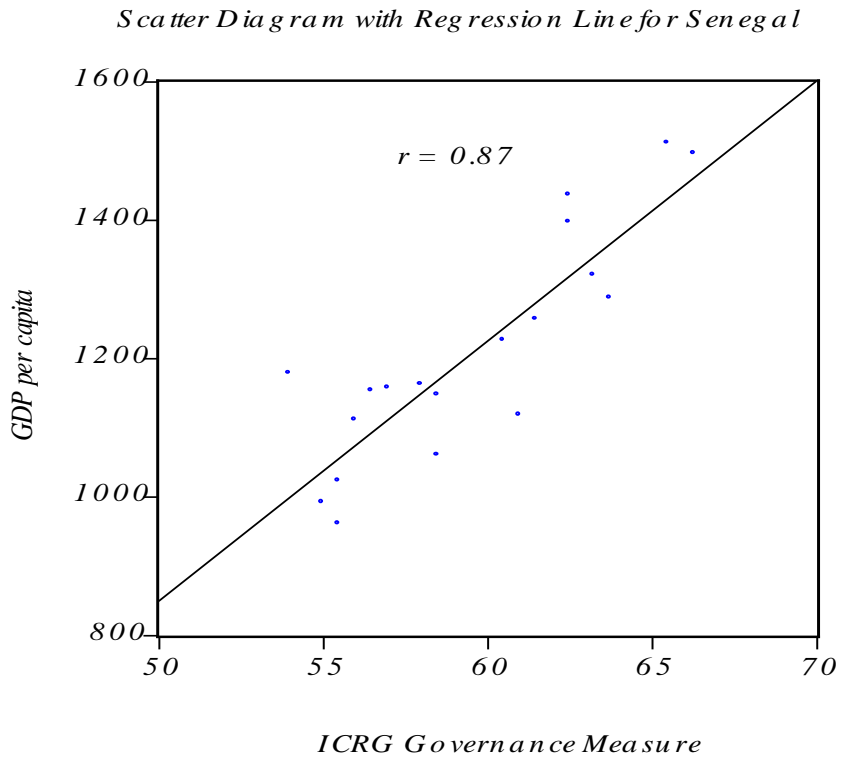
**Knack (2002) Model: Scattergram with Regression Line**



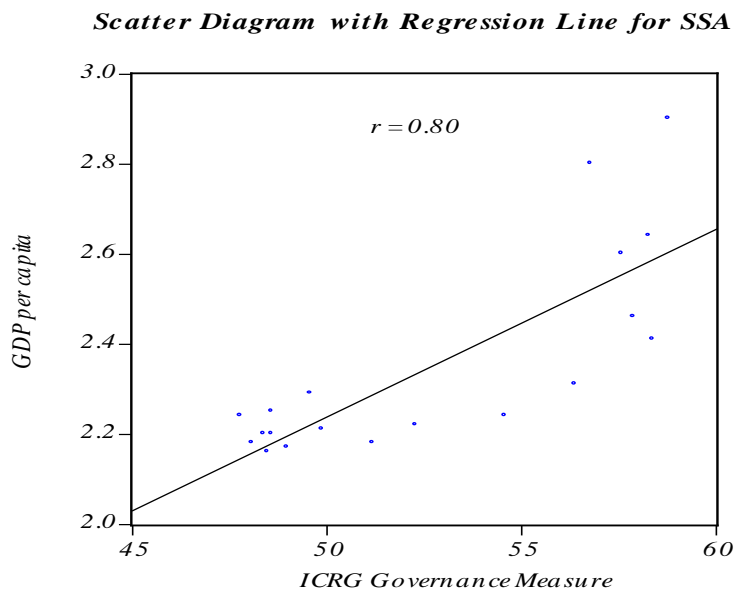
To establish the impact of governance on the growth rate of GDP per capita, we correlated the ICRG governance index with GDP per capita growth rate as estimated by Knack (2002). With this estimation, we observed a weak positive correlation for all the countries (Figure 10), but a relatively strong one for the individual countries (Figures 11–14).

**Figure 11: The impact of governance on GDP per capita, Cameroon****Figure 12: The impact of governance on GDP per capita, Botswana**

**Figure 13: The impact of governance on GDP per capita, Senegal**



**Figure 14: The impact of governance on GDP per capita, SSA**



***Edison (2003) modelling strategy***

This model regresses the macroeconomic outcome for country  $i$  on a measure of its institutions, a measure (or set of measures) of macroeconomic policy, and a set of exogenous variables. It takes the following form:

$$Y_i = a + b[\text{Institutions}] + c[\text{Policy}] + d[Z] + u \quad (1)$$

$$\text{Institutions} = f[Z] + u_o \quad (2)$$

where  $Y_i$  is the macroeconomic outcome of interest; *Institutions* is a measure of institutional development; *Policy* represents measures of macroeconomic policies; and  $Z$  is a set of exogenous control variables, including geographic variables capturing a country's basic endowments.

The parameters that Edison (2003) was interested in identifying are  $b$  and  $c$ , the effects of institutions and macroeconomic policy on economic performance. However, our study limited itself to  $b$ . The simplest strategy would be to estimate Equation (2) using the ordinary least squares method, but since institutions and the policy variables are endogenous, the model is estimated using the two-stage least squares technique, using a set of instruments (discussed below) that are correlated with the endogenous regressors and orthogonal to the random disturbances.

Edison (2003) used three measures of economic performance:

- economic development, measured as the logarithm of real per capita GDP;
- growth, measured as the average growth rate of per capita GDP over the period; and
- volatility of growth (“volatility”), measured as the standard deviation of the growth rate of per capita GDP.

In this study, we used economic development, that is, the logarithm of per capita GDP. For the measure of institutions, Edison (2003) used some broad measures of institutions that included the indicators developed by Kaufman et al. (2005), and a measure of property rights, indicating the degree of protection that private property receives.

The data on governance are those constructed by Kaufman et al. (2005). The aggregate governance measure is the equally weighted average of the six sub-indexes reported in Kaufmann et al. (1999b). The method used to calculate each sub-index gives it approximately a unit normal distribution, and it ranges from -2.5 to 2.5 with an increase always meaning a better quality of institution. The indicators used in the analysis are based on data for 1996 and 2005 collected by the World Bank (2005).

Using the cross-country estimation from the Edison model, we fitted data for Cameroon, Botswana and Senegal to determine the performance of Cameroon in comparison to these two countries over time, to get the following equation:

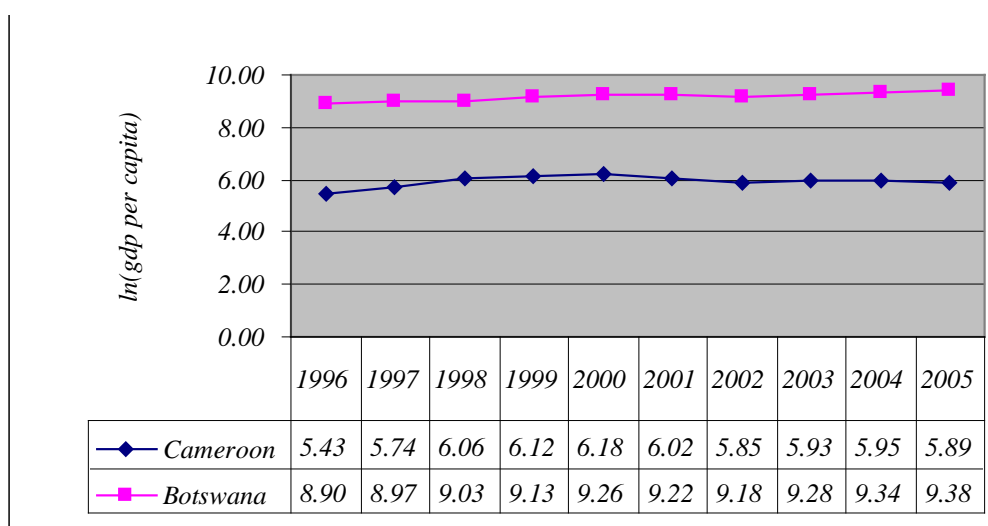
$$Y_i = \alpha + 2.09AGM \quad r^2 = 0.73 \quad n = 93 \quad (3)$$

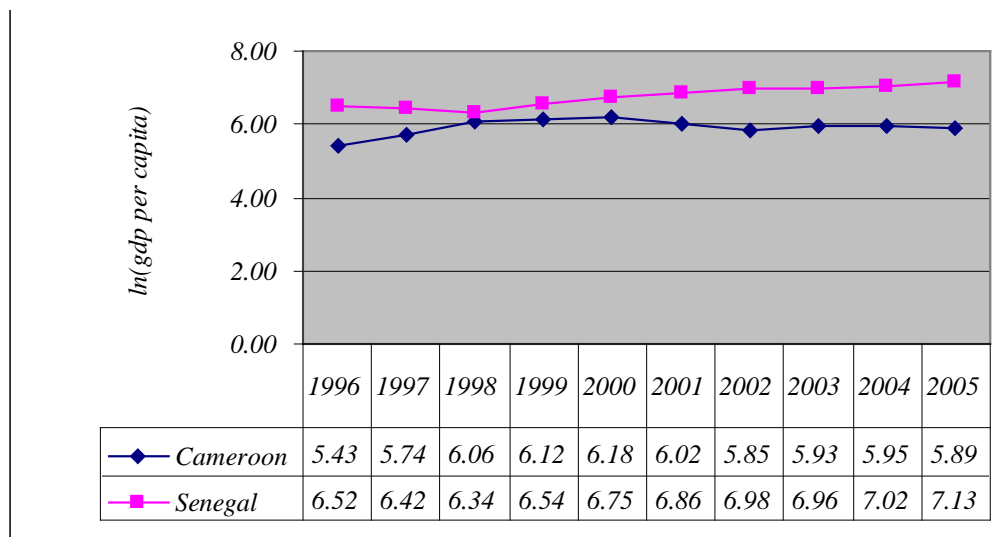
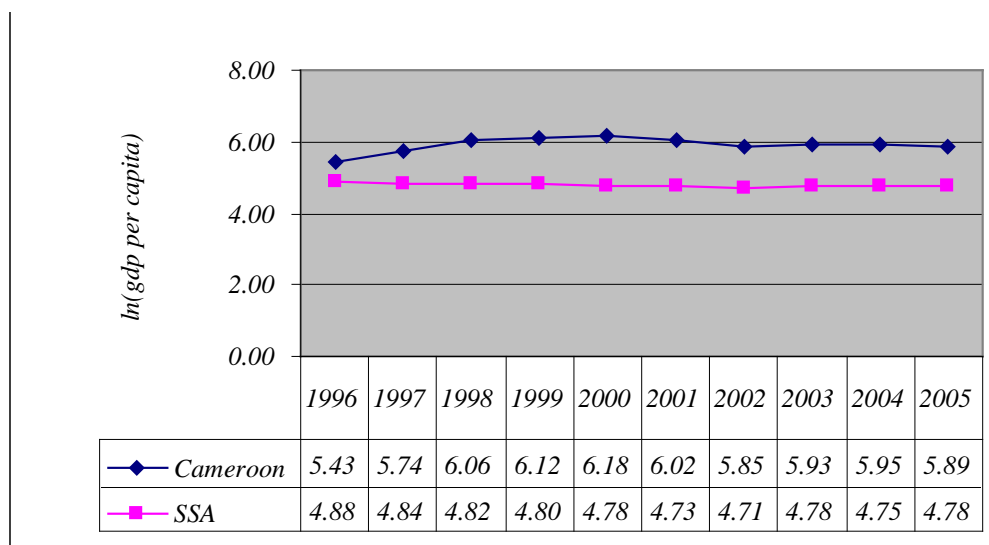
where  $\alpha$  is the average effect of all the variables (such as macroeconomic policies and exogenous control variables) omitted from the model on economic growth, and  $AGM$  is the aggregate governance measure.

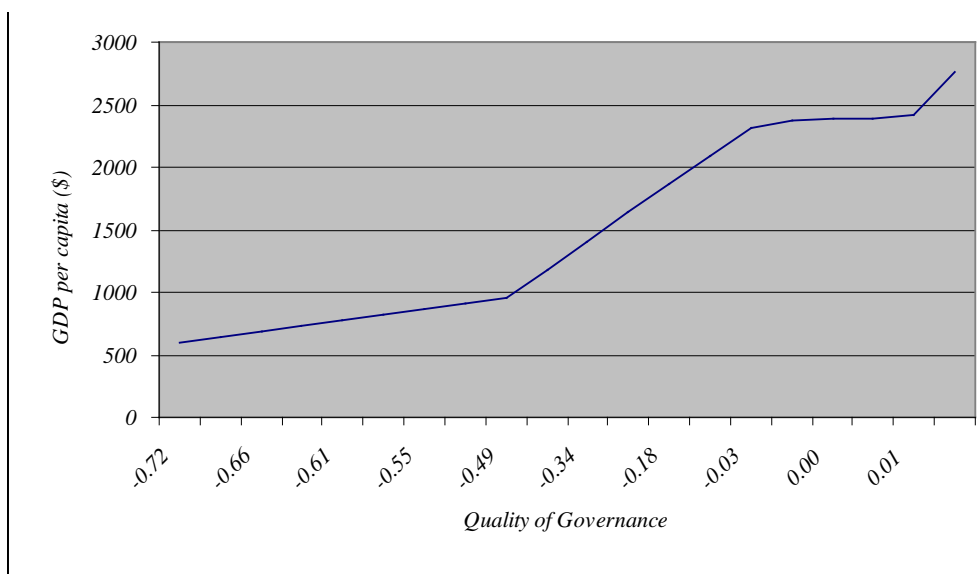
This model allows us to observe the performance of Cameroon over time, and its performance vis-à-vis other countries/regions. Figures 15 and 16 illustrate economic growth that is explained by governance for Botswana, Cameroon and Senegal:  $r^2$  measures the proportion of the total variation in economic growth that is explained by governance, as specified in this estimated model (Equation [3]).

Figures 15 to 17 show that Cameroon has consistently performed poorly in terms of its governance measure. The aggregate governance indicator covering the period 1996–2005 for sub-Saharan Africa is  $-0.72$ , much better than that for Cameroon ( $-0.88$ ). This is consistent with the findings of Edison (2003). He found that the aggregate governance measure of institutions is alone capable of explaining nearly three-quarters of the cross-country variation in income per head. For example, he found the governance index measure for Cameroon to be  $-0.72$ . Improving this quality of governance index to the average for all countries ( $0.13$ ) would raise the per capita income of Cameroon from US\$600 to US\$2,760 (Edison, 2003). Our extrapolation using his findings showed that improving the quality of governance index for Cameroon to the sub-Saharan African level of  $-0.49$  would raise the per capita income of Cameroon to US\$960 from US\$600 (Appendix 2). Figure 18 shows the impact of changes in the quality of governance on GDP per capita. An improvement in the institutional quality will increase GDP per capita, and vice versa. Thus, the established relationship is positive. For example, moving one decimal point from an institutional quality measure of  $-0.4$  corresponding to GDP per capita of about US\$1200 to  $-0.3$  would raise Cameroon's GDP per capita to US\$1700.

**Figure 15: Economic growth due to governance, Cameroon and Botswana**



**Figure 16: Economic growth due to governance, Cameroon and Senegal****Figure 17: Economic growth due to governance, Cameroon and sub-Saharan Africa**

**Figure 18: The impact of the quality of governance on GDP per capita**

### ***Baliamoune-Lutz (2005) modelling strategy***

The analysis of Baliamoune-Lutz focuses on two major determinants of economic development: institutions and social capital. The model also incorporates openness to international trade and human capital in order to explore the effect of interactions between social capital and human capital. Since the aim of the study was not to try to look at determinants of income, some commonly used variables such as physical capital and population or labour force were omitted. Baliamoune-Lutz estimated unbalanced panel equations (fixed and random effects estimations) based on the following general model:

$$\text{Income} = f(\text{human-capital}, \text{openness}, \text{institutions}, \text{social-capital}) \quad (1)$$

Baliamoune-Lutz tested the adequacy of the estimations using the Hausman specification tests. The variables included are an indicator of economic development, indicators of institutions, human capital, openness to international trade, and social capital. Also included are interactions between social capital. The dependent variable is the purchasing-power-parity adjusted value of per-capita income in log form. The indicator of human capital used by Baliamoune-Lutz was adult literacy. He used the ratio of imports and exports to GDP as a measure of openness to international trade.

To measure the connections between institutions (governance), investment and growth, he used the measure developed by Clague et al. (1999) which suggests measuring compliance with contracts and the security of property rights. Baliamoune-Lutz defined this as “contract intensive money” (*CIM*), which is equal to the proportion of deposits in

the money supply ( $M_2$ ). The idea behind this indicator is that the way financial assets are held depends on the definition of property rights. When economic agents think they are operating in a stable context, in which property rights are well defined and guaranteed, it is not risky to keep assets in deposit accounts and, consequently, cash becomes a less attractive option. Therefore, the proportion of deposits in the money supply will tend to increase. Better contract enforcement will encourage investment, leading to a higher rate of growth. The opposite situation would be caused by a poorly defined institutional framework.

The study also observed that the *CIM* measure is closely associated with economic freedom, political stability and financial development, and can be interpreted as an indicator of contract enforcement. We made an effort to quantify the institutional framework which Baliaoune-Lutz developed, exploring the relationship between governance and economic growth.

### Measuring governance

We viewed *CIM* as an indicator of governance. *CIM* represents the money kept in deposits as a proportion of the money supply:  $CIM = (M_2 - M_1)/M_2$ , where  $M_1$  is currency outside banks and  $M_2$  is the money supply including current and term deposits. The rationale behind this indicator is that when economic agents trust that contracts will be respected and in an environment considered to be safe, the agents hold a larger proportion of their money as deposits, so the *CIM* indicator tends to increase. *CIM* measures the proportion of transactions that rely on third-party enforcement and, hence, provides an indicator of the security of property rights. If contracts are enforced, a favourable atmosphere for investment is created. In this environment, the rate of capital formation will tend to rise, leading to economic growth. It follows that there should be a positive association between *CIM*, the investment rate and growth.

Using 1975–2000 panel data, Baliaoune-Lutz (2005) examined the effects of institutions (governance) proxied by contract-intensive money on economic development in 39 African countries. The results of this study indicate that there is a robust positive influence of governance on income. There are positive and very significant (at the 1% level) coefficients on the indicator of human capital (literacy) and the indicator of governance (*CIM*). However, the coefficient on openness to international trade is negative and while statistically significant (at the 5% level) is rather small in magnitude.

$$\text{Log}(GDP \text{ per-capita}) = 4.802 + 1.017CIM + 0.0334Literacy - 0.001Openness \quad (2)$$

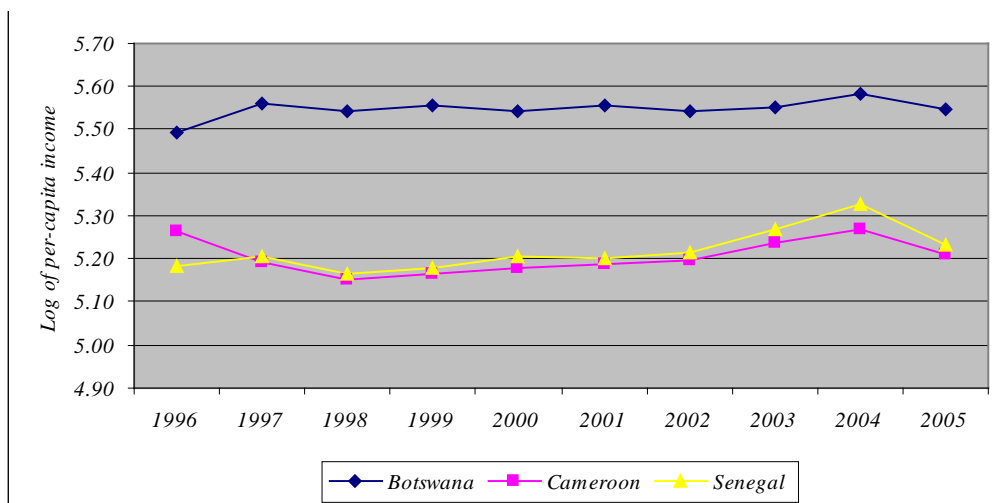
(0.081) (0.109) (0.0008) (0.0005)

Standard errors are in parentheses.

Using the Baliaoune-Lutz (2005) model for Cameroon, Botswana and Senegal we were able to explore the performance of Cameroon vis-à-vis the other two countries. In Figure 19 we see the trend of income that is explained by *CIM*, literacy and openness for these countries. Figures 19 and 20 show the trend of *CIM* for these countries. The estimated Baliaoune-Lutz model indicates that literacy and openness affect income to

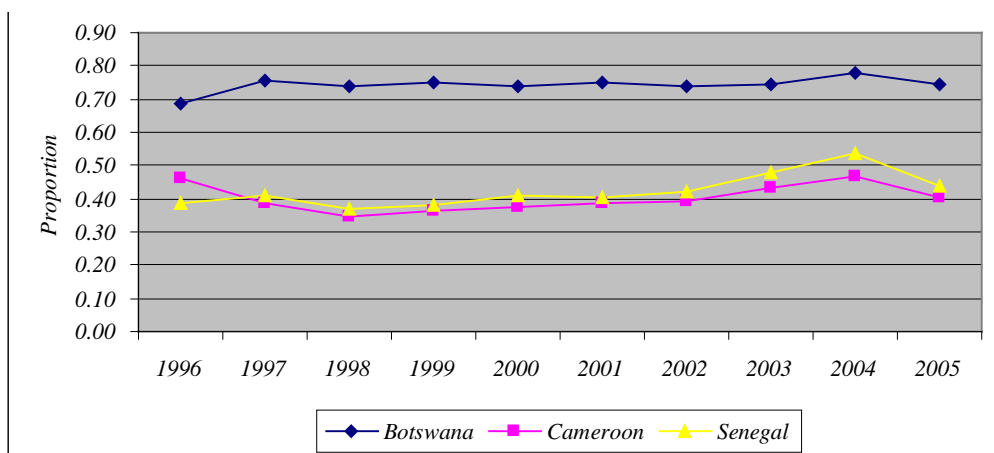
a relatively negligible extent. In other words, *CIM* is the principal determinant of income in this model. The governance trend in these countries predominates. Consequently, the gap between trends in these countries could be attributed to differences in the quality of governance.

**Figure 19: A comparative analysis of income due to CIM, openness and literacy**



In comparative terms, Botswana outperforms Senegal and Cameroon in the quality of governance. There is little difference between Cameroon and Senegal. Endowed with significant natural resources—petroleum, forestry and a rich agricultural base—and sufficiently skilled human resources, one would expect Cameroon to have a high level of income compared to Botswana and Senegal.

**Figure 20: A comparative analysis of CIM**



## Growth model analysis

Figures 10 through 14 show the degree of linear association between the ICRG governance measure and the GDP per capita. The *a priori* expectation of positive correlation is observed for the sub-region and all three countries though with various correlation coefficients ( $r$ ): Cameroon records the lowest (0.60) compared to those of Botswana (0.86), Senegal (0.87) and SSA (0.80). The implication of this phenomenon is that in Cameroon, there is a weak (linear) association between governance and economic growth.

To determine the cause–effect relationship between governance together with other determinants and economic growth, and, therefore, provide support to the foregoing correlation analysis (on a rigorous basis), we adopted the log-linear (constant) growth model using the Knack (2002) model. Using Cameroonian data, we obtained the following results:

$$gdp_c = 5.538 - 0.015X_1 + 0.048X_3 + 0.030X_4 - 0.008X_5 + 0.020X_6 + 0.006X_7 \quad (1)$$

(0.999) (0.011) (0.026) (0.017) (0.0099) (0.011) (0.0098)

$$\text{Adj R}^2 = 0.61 \quad \text{DW} = 1.52 \quad \text{P}[F^*] = 0.006$$

The values in parentheses are the standard errors of the estimated parameters, and  $gdp_c$  is the log of GDP per capita. The  $X_i$ ,  $i = 1, 3, 4, 5, 6, 7$  are as defined by the Knack (2002) model. The rationale for choosing this functional form of regression model is that this type of model is particularly useful in situations where the explanatory variables show the trend over time since in this condition the model describes the constant percentage rate of growth ( $\beta_i > 0$ ) or decay ( $\beta_i < 0$ ) in the dependent variable ( $gdp_c$ ).

Our model, which explains 61% of changes in GDP per capita, demonstrates that a constant 2% rate of decay in Cameroon's economic growth is due to the country's poor quality of governance while the year-to-year variability of inflation accounts for about 1%. On a positive note, educational attainment, financial development and openness to the rest of the world affect economic growth by about five, two, and one constant percentage rate of growth, respectively. The effect of poor governance on economic growth corroborates the weak degree of correlation between governance and economic growth in Cameroon observed in the correlation analysis.

We also investigated the responsiveness of economic growth to governance together with other explanatory variables. We did this by logging all the variables such that the resulting estimated parameters from an appropriate regression measure the elasticity of the dependent variable with respect to the independent variables, that is, the percentage change in the dependent variable for a given (small) percentage change in the independent variable. We observed that in Cameroon, economic growth was highly inelastic to governance whereas educational attainment was elastic. This observation implies that Cameroon stands to reap more from economic growth if it could be more serious about improving its quality of governance.

### *Transparency International Cameroon*

To corroborate our findings, we presented the findings of a study carried out in 2006 by the Transparency International office in Cameroon. In this study, managers and senior workers in various businesses in Cameroon, beginning from small through medium to large businesses by Cameroon standards were interviewed on their perceptions of the constraints to doing business in this country. Less than 1% of those interviewed thought the level of corruption has reduced in Cameroon during the past three years. In contrast, 30% thought it has increased. Another 30% thought the level of corruption has stayed the same.

Interviewees perceived the two main factors explaining rampant corruption in Cameroon as low salaries and the lack of sanctions or punishment for those found to be corrupt (see rankings below). The government does not really seem to care about the problem or does not consider it important enough. This behaviour tends to encourage corruption and impunity, to the detriment of economic activities.

The study found that more than 94% of entrepreneurs affirm that the judicial system is corrupt, which supports the fact that the judicial system is not credible. Because the judicial system is corrupt, it is not possible to consider Cameroon a country where there is effective rule of law. This means that the enforcing of contracts cannot be effective.

In addition to an ineffective judicial system, the police force and the gendarmerie were also found to be very corrupt. With members of these forces of law and order corrupt, enforcing law and protecting the businesses is very uncertain. Those who are corrupt, therefore, tend to behave with impunity.

Most of the business operators interviewed felt that the government was encouraging corruption, making it difficult for businesses to operate.

Ranking of the causes of corruption in the public sector:

- No punishment of those who are corrupt.
- Government does not consider the problem important enough.
- Desire for personal enrichment.
- Low salaries for civil servants.
- Discretionary appointment of people in responsible positions.
- Some government officials have exorbitant powers.
- The administration functions badly.
- The absence of rules and clear norms for the conduit of activities.
- Pressure from superiors and highly placed people.

## 5. Conclusion

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Most studies that relate governance to economic growth use cross-country data because governance measures are based on perceptions. This makes it difficult to do time series studies for single countries. This study looked at how governance has affected economic growth in Cameroon over time. We used models estimated by various authors, using cross-country data. Using their estimates, we plugged in Cameroon's governance data over time. Specifically, we used the methodology for determining governance indicators for countries on an annual basis developed by Kaufman et al. (2005). Unfortunately, their index set goes back only to 1996.

One of the cross-country studies we used is that of Edison (2003). He showed that if in 2002, Cameroon's governance index of -0.72 were to improve to the sub-Saharan African average of -0.49, the per capita income would improve from US\$600 to US\$900. Using this analysis, we showed that it was possible to determine the cost of bad governance, that is, the difference between the sub-Saharan African situation and that of Cameroon.

In addition to the Edison (2003) study, we used the studies by Knack, Stephen, Balamoune-Lutz and Stefan Lutz, and by Transparency International in Cameroon to establish that there is a direct relationship between governance and economic performance, and that Cameroon has lagged behind in development in a major part because of bad governance. The policy implication of this result is that as governance indicators improve, the economic performance will also improve.

## Notes

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1. See the World Bank data site <<http://www.countrydata.com/wizard>>
2. We are able to do this estimation because the ICRG data set from 1982 to 2002 was available.

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# Appendix

**Table 1: 3SLS regressions for governance and economic growth (Easterly et al. [2006] model)**

Measures of institution	$\beta_0$	$B_1$	OID: Sargan statistic	OID: Hansen Statistic
Voice & Accountability	1.727 (8.23)	0.974 (3.11)	1.50 (0.22)	1.54 (0.21)
Government Effectiveness	1.844 (9.56)	0.930 (3.29)	2.22 (0.14)	2.50 (0.11)
Control of Corruption	1.876 (10.01)	0.829 (3.28)	2.58 (0.11)	2.84 (0.09)
Political Stability	1.991 (11.05)	1.001 (3.31)	1.90 (0.17)	1.93 (0.16)
Regulatory Quality	1.216 (3.89)	2.212 (3.33)	0.13 (0.72)	0.14 (0.70)
Rule of Law	1.848 (10.95)	0.843 (3.40)	3.11 (0.08)	3.28 (0.07)

Values in brackets are the t-statistic (p-value for Sargan/Hansen stat.): all are significant at 5%.

Source: Authors.

**Table 2: Extrapolation of Edison's governance–income relationship**

s/n	Institutional Quality	GDP Per Capita
1	-0.720000 CMR	600.0000
2	-0.692000	645.0000
3	-0.663000	690.0000
4	-0.634000	735.0000
5	-0.605000	780.0000
6	-0.576000	825.0000
7	-0.548000	870.0000
8	-0.519000	915.0000
9	-0.490000 SSA	960.0000
10	-0.413000	1185.0000
11	-0.335000	1410.0000
12	-0.296000	1635.0000
13	-0.180000	1860.0000
14	-0.103000	2085.0000
15	-0.025000	2310.0000
16	-0.006000	2367.0000
17	-0.001000	2381.0000
18	0.004000	2395.0000
19	0.014000	2423.0000
20	0.130000 All	2760.0000

Source: Authors' computations

**Table3: Correlation matrix**

	GDPPCG	VOIACC	POLISTAB	CORRCONTR
GDPPCG	1.000000	-0.316090	-0.104343	0.092678
VOIACC	-0.316090	1.000000	0.499138	-0.328113
POLISTAB	-0.104343	0.499138	1.000000	-0.137774
CORRCONTR	0.092678	-0.328113	-0.137774	1.000000

**Table 4: Summary statistics**

	GDPPCG	VOIACC	ROLAW	CORRCONTR
Mean	2.388889	-0.587222	-1.067778	-1.024444
Median	2.390000	-0.910000	-1.060000	-1.050000
Maximum	3.060000	0.900000	-0.920000	-0.780000
Minimum	1.910000	-1.180000	-1.190000	-1.110000
Std. dev.	0.360605	0.719918	0.089726	0.109984
Skewness	0.351297	1.077273	0.104349	1.427479
Kurtosis	2.431629	2.865373	2.012898	3.729258
Jarque-Bera	0.306257	1.747572	0.381722	3.255975
Probability	0.858019	0.417368	0.826247	0.196324
Observations	9	9	9	9

**Table 5: Data collected**

Year	GDPPCG	VOIACC	POLISTAB	GOVEFF	REGQUAL	RULAW	CORRCONTR
1996	2.35	-1.05	-0.98	-1.04	-0.82	-1.18	-1.1
1997	2.53	-0.91	-0.865	-0.825	-0.485	-1.05	-1.105
1998	2.56	-0.77	-0.75	-0.61	-0.15	-0.92	-1.11
1999	2.01	0.065	-0.65	-0.525	-0.075	-0.99	-1.08
2000	1.91	0.9	-0.55	-0.44	0	-1.06	-1.05
2001	3.06	-0.1	-0.505	-0.515	-0.385	-1.125	-1.045
2002	2.06	-1.1	-0.46	-0.59	-0.77	-1.19	-1.04
2003	2.63	-1.14	-0.68	-0.615	-0.74	-1.095	-0.91
2004	2.39	-1.18	-0.9	-0.64	-0.71	-1	-0.78

**Table 6: Statistical table for all six governance indicators for Cameroon**

Governance indicator	Year	Percentile rank (0–100)	Estimate (-2.5 to + 2.5)	Standard error	Number of surveys/polls	Regional average, percentile
Voice and accountability	2005	14.0	-1.19	0.14	9	32.8
Political stability/o violence	2005	34.0	-0.34	0.22	8	33.9
Government effectiveness	2005	21.5	-0.90	0.16	10	27.0
Regulatory quality	2005	23.3	-0.76	0.16	10	28.1
Rule of law	2005	15.5	-1.02	0.15	12	28.0
Control of corruption	2005	8.4	-1.15	0.16	9	29.0

Source: Kaufmann et al. (2006). 05.

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## Abstract

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Endowed with significant natural resources—petroleum, forestry and a rich agricultural base—and sufficiently skilled human resources, Cameroon has the potential to be one of the wealthiest countries in sub-Saharan Africa, yet it has not been able to develop since independence. This is an indication that resources alone cannot significantly lead to sustainable growth. This study has established that political and economic governance play a key role in growth. The paper has empirically assessed the impact of governance on the performance of the Cameroonian economy. In the paper, we have used the models of Knack (2002), Edison (2003), Baliaoune-Lutz (2005) and Easterly et al. (2006) on governance and economic growth, to establish that there is a positive and significant relationship between governance and economic growth. We have also used the results of the model by Edison (2003) to cost bad governance. Using the coefficients from his findings, we have established that if governance measures in Cameroon improved from an index of -0.72 to the sub-Saharan index of -0.49, the country's gross domestic product (GDP) per capita would rise from US\$600 to US\$900. If the governance index for the country were to improve to the global level of 0.13, the GDP per capita for Cameroon would climb from US\$600 to US\$2,760. We have also used a study carried out by Transparency International Cameroon to reinforce the findings of Knack (2002), Edison (2003) and Baliaoune-Lutz (2005). Since progress towards good governance in Cameroon has at best been mediocre, it is not surprising that the economy has remained fundamentally under-developed.