IS GLOBALIZATION, DE JURE AND DE FACTO, TRIGGERING CAPITAL FLIGHT IN THE AFRICAN ECONOMIES AND MAKING THEM A WORLD'S ENVIRONMENTAL NET CREDITOR?

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Overview

Capital flight may be concisely described as the net capital outflows that are not recorded in the Balance of Payments (Ndikumana and Sarr, 2019). The outflows may be "licit" or "illicit", denoting repatriated capital by foreign investors, or financial flows unrecorded which is earned outside and does not return, respectively. The capital flight out of an economy corresponds to an inflow into another country (Cheung et al., 2020). Diverse events can trigger capital flight, such as currency manipulation, political uncertainty, and economic performance. When the capital flight phenomenon occurs, the most common consequences are lower investment, weakened currency, government debt, and a slowdown in economic growth or an economic recession. That is, a decline in investment and Foreign Direct Investment (FDI), a fall in demand for domestic currency, and less capital available. Several economies that have suffered high capital flight have fallen into sovereign default episodes (Dachraoui et al., 2020). Therefore, when in a considerable amount, capital flight have severe economic consequences on any economy. However, the economic consequences of capital flight on developing economies are more pronounced because capital is in short supply and they depend substantially on foreign capital (Meierrieks and Schneider, 2021). African economies have been experiencing considerable progress in macroeconomic stability. However, despite economic growth acceleration and foreign capital inflows, many African economies have been experiencing rapid growth in capital flight. They have been considered a large-scale capital flight source. Since 1970 African countries have recorded an increasing amount of capital flight. From 1970 to 2018 $2 trillion US Dollars of capital flight were recorded (Ndikumana and Boyce, 2021). In 2020 African economies experienced an exceptional episode of capital flows, and the capital flight phenomenon exponentially increased. The financial shock was substantial and consequently, it contributed to an increase in the number of people below extreme poverty in these nations (Cezar et al., 2022).

Besides economic challenges that are addressed in the literature, capital flight or illicit financial flows also arise severe energy and environmental challenges. Illicit financial flows can originate in the illicit exploitation of environmental resources and are associated with the unsustainable use of finite natural resources UNCTAD (2020). Large-scale extraction of natural resources is highly capital and energy intensive, which could lead to the depletion of capital stocks and increase climate-related risks. Furthermore, the low level of environmental standards may lead to the illicit and unsustainable exploitation and trade of natural resources. Therefore, could the energy sector be one of the main channels of Illicit financial flows? According to the *Tackling Illicit Financial Flows for Sustainable Development in Africa Report* developed by UNCTAD (2020) the amount of illicit financial flows per year from African countries, dwarfs the amount of official development assistance that these economies receive annually. Sustainable development in the African economies requires massive investments, which these economies cannot afford without external help. Therefore, the loss of capital through illicit financial flows arises further challenges for the mobilization of resources in these countries to adapt to climate change. The research questions that arise are: how could African economies accomplish sustainable development and environmental goals if the amount of capital outflow is higher than the amount of development assistance? Is capital flight undermining global decarbonization?

The main objective of this research is two-fold. Firstly, considering that capital flight and globalization share the ability to transpose national borders, this research aims to analyse globalization as a driver of capital flight in African countries, and the consequences of capital flight and globalization on economic growth and human development in these countries. Secondly, this research aims to analyse the role of capital flight in sustainable development and environmental performance (considering the energy sector) of the African economies. To the best of our knowledge, no other studies provide an analysis of the relationship between capital flight, globalization *de jure* and *de facto*, economic growth, human development, and environmental performance.

Methods

This paper used annual data from 1998 to 2019 for a group of 20 African countries. The phenomenon of capital flight could be triggered by diverse government events. Therefore, besides each dimension and measure of globalization, governance indicators were also included in this analysis, namely regulatory quality index, political stability, and governance effectiveness. The capital flight computation used in this study follows the procedure developed by Boyce and Ndikumana (2001) and updated by Ndikumana and Boyce (2018). Both globalization and capital flight demonstrate, mainly economic, long-run consequences. Thus, in a preliminary econometric analysis, the Autoregressive Distributed Lag (ARDL) model was used. However, to ensure robust results, a second method will be applied.

Results

This research first intends to provide empirical evidence of the role of capital flight on economic growth and human development. Then, understand if globalization triggers capital flight in the countries under analysis. Lastly, understand the role played by capital flight in the accomplishment of sustainable development goals. The preliminary results support that as expected and concurring with the literature, capital flight restricts economic growth. Also, seems to be evidence that the effect is only verified in the long-run, suggesting that capital flight is a long-run phenomenon in the economy. The same effect is suggested for human development. The results of the reverse models suggest that the negative relationship between economic growth and human development, and capital flight is bilateral. Both economic and human development discourage the capital flight phenomenon.

Regarding globalization, the preliminary results support that the effect of globalization on economic growth and human development is very similar. Through these results seems to be evidenced that social and political globalization *de jure* induce both economic growth and human development. Social globalization *de jure* behaves as a driver of capital flight, while political globalization de facto seems to mitigate it. Regarding the accomplishment of the sustainable development goals, it is expected that capital flight may be limiting the financial resources needed by the African economies to invest in mitigation and adaptation climate change strategies. Consequently, capital flight may undermine strategies such as climate finance to accomplish their purpose.

Conclusions

The preliminary findings of this research support that economic growth and human development have a negative bilateral relationship with capital flight. A weak economic performance triggers capital flight, and capital flight leads to a slowdown in investment and increases poverty. This evidence suggests that the African economies under analysis may have been facing a trade-off between improving economic growth and mitigating capital flight. This trade-off could result from the origin of the economic growth in the African economies. Economic growth based on the intensive exploitation of natural resources, or the use of a cheaper labour force will not reflect improvements in the standard of living or improvements in the economic system. As well as economic growth based on activities resulting from taking advantage of lax environmental regulation. This, consequently, will give rise to growing capital flight as there is more capital available.

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