ORGANISATION DE COOPÉRATION ET DE DÉVELOPPEMENT ÉCONOMIQUES

OECD OCDE

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

DAC DEVELOPMENT PARTNERSHIPS FORUM, 27-28 FEBRUARY 2002

ODA and Private Finance:
Attracting Finance and Investment to Developing Countries

Session 1. Shaping the Enabling Environment for Private Financial Flows

Kempe Ronald Hope, Sr.
Senior Policy Advisor
Cabinet Office of the Executive Secretary
United Nations Economic Commission for Africa

Shaping the Enabling Environment for Private Financial Flows in Africa
A Governance Perspective

Shaping the Enabling Environment for Private Financial Flows in Africa
A Governance Perspective

by

Kempe Ronald Hope, Sr.
Senior Policy Advisor
Cabinet Office of the Executive Secretary
United Nations Economic Commission for Africa

DAC DEVELOPMENT PARTNERSHIPS FORUM
Paris, France
27-28 February, 2002

The Problem

The point of departure in this presentation is that bad governance in Africa shares most of the blame for the low levels of private financial flows into the region. This bad governance manifests itself in various combinations of ways including:

- Lack of parliamentary oversight;
- Lack of judicial independence;
- Rampant bureaucratic corruption;
- Lack of respect for the rule of law;
- Lack of budgetary transparency;
- Lack of participatory decision-making;
- Lack of respect for free and fair electoral processes;
- Bureaucratic delays in obtaining work permits for key foreign employees of foreign firms;
- Lack of enforcement of contracts and laws pertaining to property rights; and
- Lack of clear rules and laws on the repatriation of profits.

The Impact

One result of such bad governance is that there are no predictable rules of the game to attract long-term private domestic and foreign investment. Currently, in sub-Saharan Africa, gross domestic investment stands at about 17 percent of GDP and falls far short of investment in other parts of the world. In addition, sub-Saharan Africa also accounts for a very small share of foreign direct investment (about 1 percent) in the world economy.

We can also look at other indicators which influence net financial flows. Trade performance – the most tangible indicator of globalization, for example – has also been very weak. During 1960-69, Africa's share of total world exports was 5.3 percent, and of imports 5.0 percent. By 1990-98, however, these figures dropped to

2.3 percent and 2.2 percent, respectively. Bad governance (such as trade policies that are more protectionist than those of most of the continent's trading partners) has further affected the value of the continent's non-oil exports which amounted to US$69 billion in 2000 instead of an estimated US$191 billion if the region's countries had merely retained their 1980 export market share.

The Solution: Toward Good Governance

Improving governance is the key to solving Africa's development problems. It underpins everything else including efforts to stimulate trade and growth, to deliver public services more effectively, and enhance financial flows for private investment. From a broader perspective, African states must commit to improving governance for the following reasons, among others:

- To enhance their ability to implement development and poverty reduction policies with scarce resources;
- To execute public management functions in an accountable manner;
- To demonstrate transparent and participatory economic policy-making and execution as well as an open flow of information available to all stakeholders;
- To signal an adherence to standards of institutional functioning free of corruption or other rent-seeking behaviour;
- To create a credible policy environment in which domestic and international investors can have confidence and trade can be enhanced; and
- To strengthen absorptive capacity to attract and mobilize development assistance flows.

The benefits from good governance will, therefore, include maximizing the gains from globalization, including increasing financial flows; accelerating growth; reducing poverty; and creating a more stable, predictable macro-economic environment.

What Africa Needs to Do Now – An ECA Proposal

In support of the efforts to improve governance in Africa, the ECA has been spearheading the development of an African Peer Review (APR) mechanism as described below. This APR mechanism is being included in the ECA's guidelines document on economic and corporate governance being prepared in support of the New Partnership for Africa's Development (NEPAD) plan of action.

The African Peer Review (APR) Mechanism

The APR mechanism that the ECA is proposing builds on the concept of African ownership to allow African leaders to act on assessments of governance issues, in their countries, that have been conducted by their fellow Africans in an independent and non-emotional manner. A credible APR process would have both an accountability and a broader development perspective. The accountability perspective is derived from the need to demonstrate to citizens, and the larger international community, that the political commitment and will exists to engage in self-monitoring and to take corrective actions where required. The development perspective is derived from the need to effect systems of good governance to encourage private investment and a climate for enhanced donor flows to stimulate growth and reduce poverty. Ideally, the APR process would allow for the interests of donors and recipient countries to converge.

The APR mechanism is an idea whose time has come. It is therefore a diagnostic tool that is designed to provide an independent assessment of the differences in country performance and diversity with respect to political governance and economic and corporate governance. It would also validate, or qualify, any relevant assessments conducted by external partners, such as those done by the World Bank and IMF (ROSCs and CFAAs, for example).

Objectives of the APR Mechanism

The APR mechanism will focus on the key features of political, economic, and corporate governance in the country being reviewed and, in that regard, its primary objectives will be the following:

- To enhance African ownership of the development agenda;
- To monitor progress towards agreed goals, codes, and standards;
- To identify, evaluate, and disseminate good practices;
- To ensure that policies are based on the best current knowledge and/or the practical experience of peer countries;

- To assess how good practices can be effectively transferred to other African states;

- To use peer scrutiny and pressure to induce the adoption of good practices and adherence to agreed codes and standards; and

- To identify capacity gaps and recommend approaches to address those gaps.

Implementation Modality for the APR Mechanism

Administrative Arrangements

First, we are proposing that the APR mechanism would be managed by, and situated in, a secretariat located in the ECA. This is necessary to maintain the credibility, integrity, and national, regional, and international acceptance of the outcomes of any given country APR process. Moreover, the ECA possesses the requisite expertise and infrastructure to provide the technical and logistical inputs that would be required to sustain a credible APR process.

Second, it should be noted that peer reviews are data intensive and some independent sources of data would also have to be used beyond those provided by the governments of countries being peer reviewed.

Third, countries can either volunteer to be peer reviewed or be selected for peer review through a process that must entail decision-making by the NEPAD Heads of State and Government Implementation Committee.

Fourth, the members of the team, as well as their terms of reference, must be approved either by the NEPAD Steering Committee or by the Heads of State and Government Implementation Committee. Such an approved team should not comprise more than two members and would be selected from a Panel of Eminent Africans that would be established specifically to conduct these peer reviews. A third member of the team will be provided by the APR Secretariat to enhance technical expertise and ensure the robustness and credibility of the process and its outcomes. **All members of the team should not be citizens of the country to be peer reviewed.**

The Process

The process for the implementation of the APR mechanism will entail three stages. In Stage One, an analysis will be conducted of the development and governance environment in the country to be peer reviewed. Key issues will be identified for the country, as relevant, such as the role of the judiciary, parliamentary oversight functions, corruption, political representation problems, fiscal management, and so on. Much of the data for this analysis will be obtained from the ECA governance project which will provide reports on the state of governance in several African countries as well as comparative analyses of where a given country is with respect to other countries in the region. Additional sources of information will also be identified.

Stage Two of the APR process will be conducted in two parts by a mission team visiting the country under review. The first part will deal with political governance standards related to such critical matters as electoral processes, peace and security, judicial independence, the functioning of democratic institutions, and bureaucratic corruption, for example. The mission's work here will be significantly informed by the Stage One analysis and augmented by other sources of information such as from the OAU's Conflict resolution unit, national civil society groups, outcomes of independent monitoring of electoral processes by reputable organizations, and reports by well respected international NGOs like Transparency International and the International Institute for Democracy and Electoral Assistance (IDEA), for example.

Part two of the second stage will be focused on economic and corporate governance issues with particular emphasis on public financial management and accountability including the legal and administrative framework for fiscal management, budget formulation and execution, financial reporting, and auditing practices, for example. Much of the information and data here will be obtained from government sources. However, other independent sources of information will also need to be consulted, such as the ECA, AfDB, World Bank, and IMF, for example.

In both parts of this stage Two APR process, mission members will interact with, and interview extensively, the relevant government officials; parliamentarians; opposition party members not in parliament; banking and financial sector representatives; private sector representatives; officials of resident missions of regional and international organizations; and representatives of civil society groups, including the media, NGOs, universities, and trade unions, for example.

The mission will prepare a report on its findings, a draft of which will be discussed with the government concerned. Those discussions are designed **only** to ensure the accuracy of information and to offer the government an opportunity to provide its views on how the identified shortcomings may be addressed. **However, the mission's report will remain independent and the findings contained therein will not be cleared by the government concerned.**

Stage Three, the final stage of the APR process, will involve discussions of the outcomes of a mission and the recommendations regarding the next steps. These discussions will occur in a forum of a Committee of Ministers of Finance and Central Bank Governors. This forum will be convened periodically through the APR Secretariat for this purpose. The deliberations and decisions of this forum will be conveyed to the NEPAD Heads of State and Government Implementation Committee through the NEPAD Steering Committee.

Some Indicators

In assessing governance, it is useful to engage a set of indicators which can provide information on whether there is failure or compliance with codes and standards and the nature of the remedies that may be required. For the APR process, mission reports will employ relevant governance indicators. These indicators will not be in the form of rating indices or scorecards (which may be regarded by African leaders as too academic and not hands on) but will instead be objective–fact–based measures (OFBM) of the quality of governance. The OFBM has the potential for greater operational relevance than indices or scorecards which tend to be inconsistent, unreliable, or affected by the biases of the observer. Moreover, the OFBM, has the capacity of being observable and/or verifiable, as well as being easily interpreted, by general members of society and not just the educated.

Tables 1 and 2 provide examples of possible indicators of the quality of governance using the OFBM. It should be noted that, for each indicator used by a mission team, the sources of the information will need to be provided.

Table 1: Examples of Indicators of Political Governance

No.	Indicator	Governance	
		Good	**Bad**
1.	Are political parties allowed to freely mobilize	Yes	No
2.	Has the last national election been free and fair	Yes	No
3.	Are the decisions of the courts respected by the government	Yes	No
4.	Is criticism of the government allowed in the media	Yes	No
5.	Are trade unions free to mobilize	Yes	No
6.	Have any government officials been convicted on corruption charges	Yes	No
7.	Are there high government officials known to have engaged in corrupt acts that have not been arrested	No	Yes
8.	Are there bribes that have to be paid for getting government services such as a passport	No	Yes
9.	Are there serving military personnel in high government posts	No	Yes
10.	Are there regular arbitrary violent clashes between government and opposition groups inspired by government supporters	No	Yes

Table 2: Examples of Indicators of Economic and Corporate Governance

No.	Indicator	Governance Good	Governance Bad
1.	A clear legislative basis for budgeting exists with adhereable rules	Yes	No
2.	Are there formal constraints on budget deficits and expenditures	Yes	No
3.	Are the formal constraints on budget deficits and expenditures adhered to	Yes	No
4.	Are there frequent and large variances between appropriations and actual expenditures	No	Yes
5.	Is civil society allowed to participate in the budget process	Yes	No
6.	Is the central Bank prohibited/restricted by law from deficit financing	Yes	No
7.	Can Central Bank decisions be arbitrarily overturned by government	No	Yes
8.	Are there unambiguous rules and laws on corporate behaviour	Yes	No
9.	Are there enforceable rules and laws on property rights and contracts	Yes	No
10.	Do the delays in the annual auditing of public accounts exceed 90 days	No	Yes
11.	Are the tax laws fairly enforced to enhance domestic resource mobilization	Yes	No

Conclusion

Africans have to take responsibility for improving governance in their countries. To be sure, many African countries are already addressing governance problems. The APR mechanism outlined here can provide a new form of peer group pressure to help spread this experience. However, the donor community must also display a willingness to provide support where capacity constraints are identified.

Understandably, the APR mechanism is a significant innovation, but it will take time to build up trust amongst African countries for its implementation. This has been the pattern in the OECD where member countries assess each other's economic performance and compliance with international commitments. The experience there has also been that pressure for change is generated by public exposure rather than sanctions. As stated before, the APR mechanism is an idea whose time has come, African governments must now move quickly toward its acceptance and implementation.