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THE EFFECTIVENESS OF AID TO AFRICA SINCE THE HIPC INITIATIVE: ISSUES, EVIDENCE AND POSSIBLE AREAS FOR ACTION

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ACRONYMS AND ABBREVIATIONS

AfDB	African Development Bank and Fund
BADEA	Arab Bank for Economic Development in Africa
BOAD	West African Development Bank
BWI	Bretton Woods Institutions (IMF and World Bank)
CBP	Capacity Building Programme
CG	Consultative Group
CIDA	Canadian International Development Agency
CPIA	Country Policy and Institutional Assessment
DAC	Development Assistance Committee
DFI	Development Finance International
DFID	Department for International Development (UK)
EDF	European Development Fund
EIB	European Investment Bank
EU	European Union
GE	Grant element
GNI	Gross national income
HIPC	Heavily Indebted Poor Countries
IDA	International Development Association of the World Bank
IFAD	International Fund for Agricultural Development
IFF	International Financing Facility of the UK
IFIs	International financial institutions
IMF	International Monetary Fund
IsDB	Islamic Development Bank
LIC	Low income countries
LLDCs	Least Developed Countries
LTEF	Long-term expenditure framework
MCA	Millennium Challenge Account
MDBS	Multi-donor budget support
MDG	Millennium Development Goals
MTEF	Medium-term expenditure framework
MOU	Memorandum of Understanding
NDF	Nordic Development Fund
NEPAD	New Partnership for Africa's Development
NGO	Non-governmental organisation
Non-ODA	Non-concessional loans
ODA	Official development assistance
OECD	Organisation for Economic Development and Co-operation
OOF	Other official flows
OPEC	Organisation of Petroleum Exporting Countries
PEAP	Poverty Eradication Action Programme (Uganda)
PRGF	Poverty Reduction and Growth Facility
PV	Present value
PRS	Poverty Reduction Strategy
PRSP	Poverty Reduction Strategy Paper
SPA	Strategic Partnership with Africa
SSA	Sub-Saharan Africa
TA	Technical assistance
UN	United Nations
UNCTAD	United Nations Conference for Trade and Development
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund

EXECUTIVE SUMMARY

INTRODUCTION (CHAPTER 1)

1. At an international level, donors/creditors and African governments have been making major efforts to improve both the quantity and quality of development finance. On the donors/creditors' side, pledges made at the Monterrey Financing for Development Summit, the UK's proposal for the International Financing Facility (IFF) and the US Millennium Challenge Account are some of the main efforts being made to increase development financing, much of it intended to be provided as grants. In addition, donors/creditors are also taking significant steps to improve the quality of aid delivery through the work of the OECD's DAC, Strategic Partnership of Assistance (SPA) and other initiatives on harmonisation of donor procedures and practices. However, there are questions as to how effective these efforts are in raising both the quantity and quality of external assistance flows to African governments.

2. This study aims to do the following:
   - review the trends in donor/creditor financing low income African countries,
   - investigate how donor/creditor practices impact on the quality of development finance,
   - review international efforts to improve quality of development financing to African countries
   - propose how African governments can be empowered to have more control and analyse and source the external financing required to enable them to reach the MDGs, as part of a process of mutual accountability and partnership with the donor community.

OVERALL TRENDS AND COMPOSITION OF AID FLOWS TO AFRICA (CHAPTER 2)

3. Since the 1980s, there has been little growth of aid flows to all developing countries, include to African countries. However, the situation has changed dramatically since 2000:
   - Donors pledged increased resources at the Monterrey Financing for Development Summit and the G7 Summit at Evian.
   - New facilities and Initiatives were established, such as the Millennium Challenge Account, Education for All Fast Track Initiative, and Global Fund to Fight AIDS, TB and Malaria.
   - These pledges have also led to increased overall disbursements and a higher share of aid being disbursed to Africa.
   - The UK proposal for an International Financing Facility (IFF) holds out prospects of large-scale additional flows.
   - Most of these new resources are intended to be disbursed as grants, rather than loans, thereby potentially reducing the cost of borrowing for African governments. This has included a significant shift from loans to grants for LICs by IDA and the AfDB.
   - There has also been some increase in programme aid (budget support) in the last two years, particularly through multi-donor budget support programmes.

4. On the other hand, there are some unchanged characteristics or less positive trends:
   - Project aid and emergency assistance still account of the largest proportion (70% in 2002) of total aid to Africa, programme aid and debt relief accounting for 14% and 17% in 2002, respectively.
   - Large amounts of aid still go to middle-income countries or non-MDG-related projects.
   - Although moves to untie aid have been at the forefront of aid reform, 20% of total aid to Africa and 10% to African HIPCs (including most TA and much emergency assistance) is tied.
   - There is only limited evidence that aid is becoming more predictably or flexibly disbursed.
   - Many of the new international facilities and initiatives (eg MCA, Global Funds) risk reversing harmonisation and undermining support for PRSPs.
   - Overall conditionality on aid flows may well be proliferating rather than streamlining.
   - Donor aid shortfalls remain a problem with shortfalls compared to projections averaging 14% for programme aid and 26% for project aid for African HIPCs.
   - Without large-scale new replenishments from bilateral aid funds, shifts to grants by multilateral agencies could undermine their long-term ability to assist low-income countries.

5. In terms of the design of international policy on aid to Africa:
   - There is still widespread uncertainty about African countries' capacity to absorb aid productively and about macroeconomic "Dutch Disease" risks from aid flows.
   - There is no clear framework (beyond a minimum 35% grant element) for judging the impact of aid on long-term debt sustainability.
   - There is no consistent framework for ensuring that sufficient aid is mobilised to finance the MDGs for all countries which are committed to attaining them.

ASSESSING THE QUALITY OF AID FLOWS (CHAPTER 3)

6. In spite of recent initiatives on harmonisation of donor practices and the PRSP-based partnership, there is no systematic monitoring across all recipient countries, at the individual country level, of whether donors are living up to their pledges on aid quality and support for the PRSP framework, or behaving consistently across a range of African countries. Even more important, African countries are not systematically empowered to lead the monitoring of the improvement of aid quality themselves – donors still lead the process in most countries. To redress this situation the Heavily Indebted Poor Countries Capacity Building Programme[1] (HIPC CBP) has prepared a methodology to enable HIPC governments to assess the quality of aid they receive as part of the process of designing overall national debt and new financing strategies.

7. The key factors and issues of donor/creditor aid policies and procedures analysed using the HIPC CBP methodology are:
   For policies:
   - Concessionality: as measured by the grant element
   - Types of assistance: budget/balance of payments support, project, TA or food/commodity
   - Channel of assistance: via the budget or off-budget
   - Sectors and projects: support is for PRSP or donor-led priorities
   - Flexibility of assistance: can aid be channelled to new areas and/or used to meet unexpected financing gaps arising from economic shocks
   - Predictability of assistance: multi- or one-year commitments and whether they are fulfilled
   - Policy conditionality: the number and degree of enforcement of policy conditions
   - Policy dialogue: the degree of donor engagement in the economic policy dialogue and independent support for government policies or alignment with Bretton Woods Institutions.

   For procedures:
   - Conditions precedent – types and degree of enforcement and the disbursement delays arising in meeting these conditions
   - Disbursement methods: via cash direct to the budget or reimbursement claims
   - Disbursement procedures: the number and complexity and disbursement delays arising
   - Procurement procedures: the number and complexity and disbursement delays arising
   - Co-ordination: the degree of harmonisation between government and donors/creditors.

   A set of 23 evaluation criteria, grouped under 13 headings, have been developed, for which each donor can be assigned a score (with 1 scoring lowest and 5 highest) on the basis of objectively verifiable thresholds. Using these criteria African governments have assessed the overall quality of each donor's and creditor's resources on an objective basis.

[1] The HIPC CBP is a capacity building programme financed by the Governments of Austria, Canada, Denmark, Ireland, Sweden, Switzerland and the United Kingdom.

8. The second aspect of the methodology provides for the analysis of African government's own policies and procedures and the impact these have on the delivery of external assistance flows. The same factors are used to identify whether or not African governments have clear policies on concessionality and amounts of external assistance, preferred types and channels of assistance, priority sectors and/or projects, flexibility and predictability of development assistance, donor conditionalities and which are acceptable and which are not, and policy dialogue with donors/creditors and framework for strengthening it. The methodology can also be used to assess whether government has its own clear ideas on what it would prefer from donors in terms of their procedures, as well as the impact of government's procedures for processing conditions precedent, disbursements and procurement on actual delivery.

9. By combining the assessments of donor and government policies and procedures, the HIPC CBP methodology enables African governments to do the following:
   - Prioritise the most desirable donor and creditor sources of future new financing,
   - Assess dependence on donors/creditors providing good and poor quality aid and highlight donors/creditors which the government should look to to provide better quality and more aid in future,
   - Identify priority areas for overall improvement of donor and government policies and procedures at the individual country level,
   - Design a matrix as a framework for African governments and donors/creditors to work in partnership to strengthen quality and delivery,
   - Exchange information with other countries and monitor donor/creditor behaviour in Africa and other developing country regions against their international policy declarations, to see whether donors/creditors are behaving consistently and implementing best practices across all countries, and identify priorities for global initiatives on external assistance quality.

ANALYSIS OF DONOR/CREDITOR AND GOVERNMENT POLICIES AND PROCEDURES – MAIN FINDINGS (CHAPTER 4)

10. The main outcomes of the analysis of donor/creditor policies by African HIPC governments using the HIPC CBP methodology, are as follows:
   - The most problematic issue for HIPC governments is the lack of flexibility of funds, as many donors and creditors are much less willing than desired to provide additional budget or balance of payments support to meet exogenous shocks, or to switch funds to new government priorities.
   - Excessive conditionality on funds, poorer types of assistance being provided, funds continuing to go to non-priority sectors and projects and low predictability of funds (donors failing to disburse as pledged, to pledge multiyear funding, or to disburse in line with African HIPC governments' budget timetables) are other very important aspects of donor and creditor policies, which affect the efficient and effective delivery of aid resources to African HIPC governments to meet the Millennium Development Goals (MDGs) and to maintain debt sustainability.
   - Multilateral sources of finance tend to be more reliably channelled through budgets as programme aid, to the priority sectors and projects of the government, and more predictable. On the other hand, bilateral sources have greater concessionality, more flexibility and less conditionality.

11. For African governments, the main outcome is a general lack of formal external financing policy on aid and what exists tends to focus on concessionality, set out in the country's national debt strategy or on occasion in law, and sectors, usually defined in the Poverty Reduction Strategy. The lack of a comprehensive government external financing policy enables donors/creditors to maintain the leading role in driving a country's aid policy and the resulting quality of aid flows.

    More broadly, the lack of African government external financing policy, poor donor/creditor behaviour in comparison to what African governments want, coupled with the problems these cause for African government compliance, results in African governments finding it difficult to:
    - maintain debt sustainability and fund the Millennium Development Goals, without more concessional and less conditional funding,
    - meet funding needs arising from external shocks, without more flexibility of resources,

- avoid expenditure cutbacks, without more predictable financing,
- fund key poverty reduction sectors and projects because of donor-driven priorities,
- report back to donors/creditors and the IMF on aid flows, if funds are off-budget.

12. The analysis, by African HIPC governments, of donor/creditor procedures and their impact on disbursement delays reveals that the main factors causing disbursement delays are:
    - Cumbersome and time-consuming disbursement procedures, such as the provision of matching fund requirements and donor/creditor bureaucracy,
    - Over-complex disbursement methods, such as reimbursement claims,
    - Burdensome procurement procedures, including tying of resources and the time involved in conducting and vetting bidding and tendering procedures,
    - Difficulties in fulfilling conditions precedent so loan and grant disbursements can commence.

13. The main outcomes and areas for improvement in aid policy and procedures for the major multilateral donors and creditors are as follows:
    - <u>For IDA</u>: IDA's aid policies and procedures result in an above average score as it provides highly concessional, predictable, on-budget aid in support of government priority sectors and projects, although its provision is too tied up in conditionalities. Although IDA is seen as providing more flexible aid than many multilateral donors/creditors, there is a need for enhanced flexibility.
    - <u>For AfDB</u>: AfDB achieved a below average score reflecting the need to reduce the burden of policy conditionalities and significantly improve almost all aspects of its procedures, on which it was assessed as being well below average because these are far too cumbersome and time-consuming.
    - <u>For IMF</u>: IMF PRGF resources are ranked as being predictable, flexible and with the least burdensome procedures. However, the funds are seen as being the least concessional and highly conditional.
    - <u>For EU (EDF)</u>: EU policies score well, with the exception of predictability, but on procedures, it was ranked as below average and there is a need to reduce the burden of fulfilling conditions precedent and improve its disbursement and procurement procedures.
    - <u>For UN agencies</u>: overall the UN agencies provide highly concessional aid in support of government priority sectors and projects, but much of this aid is provided as project aid or technical assistance, delivered directly to line ministries, rather than as programme support to the budget. Better predictability of resources and less cumbersome disbursement procedures would also improve overall aid delivery.

14. The main outcomes and areas for improvement in aid policy and procedures for the G7 bilateral donors and creditors are as follows:
    - <u>Canada</u> provides highly concessional resources mainly in support of government priorities but its aid tends to be less flexible, less predictable and channelled off-budget than other bilateral donors. Changes in the method by which its aid is disbursed and better co-ordination with governments and other donors/creditors would enhance Canadian delivery.
    - <u>France</u> achieved a below average score because its aid is less concessional, less focused on government priority sectors and projects, less flexible and with more conditionalities. In addition, it ranked below average on disbursement methods and procurement procedures.
    - <u>Germany</u>'s aid policies are ranked above average with the exception of its tendency to channel funds off-budget. In terms of procedures, German aid delivery is good overall, although there is a need to improve the method of aid disbursement.
    - <u>Italian</u> aid scores very low, because it is viewed as being less concessional, less flexible, less predictable, delivered more in the form of project aid and technical assistance support and directed more towards Italian than government priorities. In procedural terms, there is a need to improve almost all aspects of its aid delivery.
    - <u>Japan</u> would benefit in policy terms by switching to more flexible programme support, provided on-budget. Less cumbersome and time-consuming disbursement and procurement procedures would also lead to improved aid delivery.

- United Kingdom is assessed by African governments as having among the best aid in policy and procedural terms, along with Ireland, Netherlands, Switzerland and the Nordics.
- United States aid is highly concessional but tends to be less flexible, less predictable, with more conditionalities and provided more in projects and technical assistance. Less cumbersome and time-consuming disbursement procedures would enhance its aid delivery.

15**.** In general, the methodologies of the OECD-DAC and SPA focus largely on procedures and the initiatives for improving harmonisation, and ignore many of the issues, especially the policy issues, African governments think are vital when assessing aid quality. While the Center for Global Development's work does cover some of these issues, it is more focused towards donors and dependent on donor-generated data. On the other hand, NEPAD highlights the need for African leadership but does not provide any practical assessment of compliance. A a result there is an urgent need for African governments to take the lead in using and disseminating the results of a methodology which reflects their needs.

POSSIBLE AREAS OF ACTION (CHAPTER 5)

16. The suggestions for priority actions for increasing the flow of high quality external assistance to Africa, to support the attainments of the MDGs, are presented at two levels:
    - International-level steps to improve the quantity and quality of aid to Africa.
    - Country-level actions by donors, creditors and African governments.

17. **KEY INTERNATIONAL-LEVEL ACTIONS**

    The key international steps to improve aid for Africa will be:
    - to increase overall disbursements to Africa by at least 60% (US$12 billion) a year, which is at the same time an amount Africa can absorb and in line with its needs to meet the MDGs. In light of the fact that recent pledges of aid would imply global increases of only a maximum of US$20 billion a year, this would mean sharply increasing Africa's share of global aid.
    - accelerating a global campaign by civil society, around the 5-year review of the Monterrey Summit, to ensure that "laggard" donors such as G7 members – Canada, Germany, Italy, Japan and the US – and smaller donors such as Austria, Greece, Portugal and Switzerland - increase their pledges and flows as rapidly as possible;.
    - ensuring that aid flows are allocated on a balanced basis to different groups of African countries (HIPCs, non-HIPC LICs, Sub-Saharan MICs and North African countries), in line with their commitment to the MDGs and poverty reduction rather than strategic interests.
    - maintaining or slightly increasing the proportion of multilateral flows in total aid to Africa, in order to maximise transaction cost benefits of coordination and pooling of funds, and reduce "strategic" motives for aid allocation, while retaining the independent funding abilities and policy decisions of bilaterals to keep Africa's funding sources sufficiently diversified.
    - dramatically reducing technical assistance and switching to capacity-building programmes
    - accelerating the trend to budget support for countries with adequate accountability systems, especially for non-HIPC low-income countries which still receive too many projects.
    - sharply increasing the share of project finance which goes to PRSP priority sectors and projects, especially in non-HIPC LICs – while broadening this definition to include all types of basic infrastructure, rural development and micro-credit programmes.
    - pushing harder for an agreement to untie all aid to all low-income countries (rather than just the least developed), including stand-alone technical assistance and food/emergency aid.
    - regularly (semiannually) monitoring whether Monterrey and subsequent pledges are being fulfilled by actual donor disbursements.
    - maintaining the current continent-wide balance between grants and loans in order to support long-term debt sustainability while not undermining the ability of multilateral institutions to support low-income countries using loan reflows (see separate note on grants for details).

- ensuring that all new initiatives and funds (whether independent – eg the Global Fund – or bilateral – eg the MCA - are oriented to enhance harmonisation and simplification of donor procedures, and alignment with African PRSPs, rather than funding separate projects.
- reinforcing efforts to streamline conditionality across the range of donor programmes (avoiding cross-conditionality and pooling of conditions), and establishing a system for regularly monitoring the level and stringency of conditionality across all donor programmes.
- ensuring that government and IMF programme forecasts of aid flows are in line with current trends and therefore allow governments more “fiscal space” to spend to attain the MDGs.
- monitoring aid shortfalls and their causes at a continental and individual country level to tackle causes and reduce shortfalls in a coordinated fashion.
- conducting analysis at a country-level of risks of aid dependency and Dutch Disease, but ensuring that these are balanced with analysis of the growth and anti-poverty benefits of additional aid, and oriented to improving the quality of aid to overcome any risks.
- ensuring that all non-concessional finance is targeted to essential private rather than public sector projects, and finances only “productive expenditure”.
- providing independent capacity-building support to African governments to enable them to:
    - improve aid management, via new laws, procedures and coordination structures
    - assess donor (and their own) performance in increasing high-quality flows; and
    - analyse fully their own aid needs, how to improve their procedures, absorptive capacity, and the effects of aid flows on long-term debt sustainability.

    Ideally such a programme would be implemented by exchanging research, information and mutual capacity-building assistance among African governments.

18. **KEY COUNTRY-LEVEL ACTIONS BY DONORS, CREDITORS AND AFRICAN GOVERNMENTS**

At the country level, the main policy implications of chapters 2 and 4 are:

African Government New Financing Policies need to be reviewed in order to:

- establish clear new borrowing policies which go beyond amounts and concessionality to cover all quality issues.
- enshrine policies in law, with supporting regulations for their implementation, and annual financing guidelines for PRSP and budget.

Such new policies would aim to:

- mobilise more aid in real terms over next 5-10 years (even if gradually falling as a percentage of GDP) to allow them to reach the MDGs
- move from loans to grants, to maintain or increase the concessionality of their financing while not eliminating the long-term prospect of accessing non-concessional finance especially for the private sector
- move from projects to budget support, and from TA to capacity-building.
- diversify their group of donors if they are relatively few, given that some donors are sharply increasing flows and may be looking to diversify recipients
- rationalise their donor group if it is too large, by discouraging small and poor quality cooperation programmes.
- insist on including more detailed, justified and growing aid projections in macroeconomic programmes agreed with the IMF
- conduct their own analysis of their macroeconomic and administrative capacity to absorb aid flows
- improve donor policies and further streamline conditionalities in order to reduce programme aid shortfalls
- accelerate efforts to streamline and harmonise donor procedures behind recipient government procedures, which themselves need to be dramatically improved, in order to overcome project disbursement problems.

In terms of Donor/Creditor Policies, the top priorities for action (in order) are*:*

- <u>Flexibility</u>: provide more grant-based rapidly-available “contingency” resources to fund protection against ‘shocks’ (see separate note on shocks for more details).

- Types of Assistance: maximise multi-donor budget support not closely linked to BWI "trigger" conditions; reduce stand alone projects, technical assistance, food aid and emergency assistance
- Policy Conditionalities: sharply reduce conditionality, and interpret country compliance more flexibly, making the vast bulk of aid dependent only on overall PRSP progress rather than individual policy conditions.
- Sectors and Projects: provide more finance solely for PRSP priority sectors and for priority projects within these sectors, eliminate earmarking of budget and sector support, and organise/report on aid according to government classifications,
- Predictability: make 3-5 year pledges and commitments, take all steps to disburse pledges on time, and adjust disbursement schedules to government budget processes.
- Channels of Assistance: maximise on-budget aid and report regularly to government.
- Concessionality: maximise grants where needed to maintain debt sustainability; offer loans in line with country grant element policy, avoid export or mixed credits for HIPCs.
- Policy Dialogue: improve independent in-country economic analysis capacity and participate in government-led meetings on economic policy and budget support.

To improve donor/creditor procedures the most urgent steps are:

- Disbursement Procedures: simplify and harmonise procedures, including eliminating matching funds requirements (or reducing them below 10%), and providing maximum pooled budget support.
- Disbursement Method: provide more resources through up front cash payments to government, rather than reimbursement or direct payment to suppliers.
- Co-ordination and Evaluation: strengthen harmonisation of procedures, and align with government procedures wherever possible.
- Procurement Procedures: eliminate formal and informal tying, encourage local procurement where possible, and preferably use government procurement procedures.
- Conditions Precedent: eliminate all except legal opinions and ensure timely monitoring.

To encourage donors to follow African Government Procedures, governments need to:

- improve their analysis and forecasting of expenditure plans and funding needs, debt sustainability, absorptive capacity and potential and actual shocks; and
- strengthen approval, signature, disbursement, procurement, reporting and audit procedures (see Table 5.1 below for details).

19. **MUTUAL PARTNERSHIP AND ACCOUNTABILITY**

Finally, it is vital to establish procedures for genuine mutual partnership and accountability between Africa and its donors and creditors. There has been a great deal of talk and launching of initiatives in this area, but so far with relatively practical focus on the ground (a notable exception being Uganda's PEAP Partnership Principles). As a result, there has been relatively little progress in the quality and disbursement speed of external assistance flows to Africa.

As a result, there is an urgent need for African governments to take the lead (supported by like-minded donors) in insisting on a system of mutual partnership and accountability, so that donors and creditors to adapt their assistance more fully to Africa's priorities.

The key issue is how this might be achieved. It could be done at two levels:

1. ***At the country level*.** African countries could present an annual long-term development financing strategy, and the findings of their evaluation of donors, at their annual Consultative Group or Round Table meetings. This presentation would not discuss scores of individual donors, but would focus on the areas in which the donor community as a whole and government were falling short of best practice, compare performance with that of donors and governments in other countries, and also stress new steps taken towards best practice by individual donors and government within each country in order to encourage better alignment by other donors. The meetings would also focus on agreeing a matrix of measures for mutual partnership and accountability between donors and government for improving the quality and accelerating the disbursement of aid, along the

lines of Table 5.1 of this paper. This matrix can then be used as checklist by African governments and donors/creditors to monitor progress in improving aid flows. Less detailed updates of progress reports could be presented at mini-CGs or other meetings at which donors and government discuss economic policy issues, and special meetings or task forces could be organised to tackle particular issues revolving around specific policies or procedures.

2. ***At the international level*****.** The country-specific results could also be synthesised into continent-level assessments of donor performance, on an annual or semi-annual basis and presented at continent-wide meetings between donors/creditors and African governments such as the UNECA Big Table, joint DAC-ECA, SPA meetings, or NEPAD meetings. It would be interesting, for example, for Africans to compare their priorities and findings with those of the DAC and the SPA. Such findings could also identify individual donors without identifying the recipient countries. If wanted, Africans and donors could agree on continent-wide priorities for immediate action and voluntary or binding targets with deadlines for donors to improve the quality of the aid. The results could also be used for informing bilateral discussions between African Ministers and individual like-minded donor Ministers, or joint discussions between groups of African Ministers and groups of like-minded donor ministers.

Ultimately such a system of mutual partnership, evaluation and accountability would be an excellent basis for establishing monitorable indicators for the aid component of MDGs and ensuring that Africa's donors and creditors genuinely live up to their Monterrey promises, so that Africa can fund and attain the Millennium Development Goals.

CHAPTER 1: INTRODUCTION

Since the turn of the Millennium, international attention has been focusing on how to increase the quantity and quality of official financing flows to Africa. This complements initiatives to relieve the debt problems of low income African countries, because it is vital to avoid repeating the development financing policies and practices of both donors/creditors and African borrowers, which gave rise to the debt problems in the first place.

In the past, poor donor/creditor policies and practices led to external assistance which was:
- expensive when provided in the form of loans rather than grants,
- donor-driven rather than government-led, failing to fulfil African governments' financing needs and priorities,
- slow disbursing, due to cumbersome and bureaucratic donor procedures and practices,
- unpredictable, as donors/creditors failed to honour pledges or release timely resources,
- poor value for money, when it was tied to purchase of donor country produced goods.

On the other hand, African governments also made poor borrowing decisions because of:
- Lack of a formal policy and strategy setting out their new financing needs and priorities, and ensuring a focus on programmes which would enhance growth and reduce poverty
- Poor absorptive capacity to use aid commitments effectively, due to poor government procedures and failure to push donors/creditors to streamline theirs,
- Weak capacity to analyse donor aid proposals to ensure the best quality aid is being mobilised or to negotiate with donors/creditors to improve their offers,
- Insufficient attention to debt sustainability, concessionality and quality of new resources.

More recently, at an international level, donors/creditors and African governments have been making major efforts to improve both the quantity and quality of development finance. On the donors/creditors' side, pledges made at the Monterrey Financing for Development Summit, the UK's proposal for the International Financing Facility (IFF) and the US Millennium Challenge Account are the main efforts being made to increase development financing, most of which is to be provided as grants. In addition, donors/creditors are also taking significant steps to improve the quality of aid delivery, through the work of the OECD's DAC, and the Strategic Partnership with Africa (SPA), on harmonisation of donor procedures and practices. There has also been considerable work to try to link export credit provision more closely to "productive expenditures" through voluntary codes. However, there are questions as to how effective these efforts are being in raising the quantity or quality of official assistance flows to African governments.

African governments, too, have been making major efforts to improve their borrowing policies. These have included trying to ensure development finance generates the maximum possible benefits for poverty reduction and development through the Poverty Reduction Strategy (PRS) process; designing and implementing national debt and new financing strategies; strengthening the legal framework for contracting new financing; and building the capacity of national staff to analyse new financing issues. Furthermore, some African governments and donors/creditors have embarked on joint steps to improve the delivery of aid flows through the establishment of multi-donor budget support programmes and donor-recipient compacts to harmonise procedures and practices.

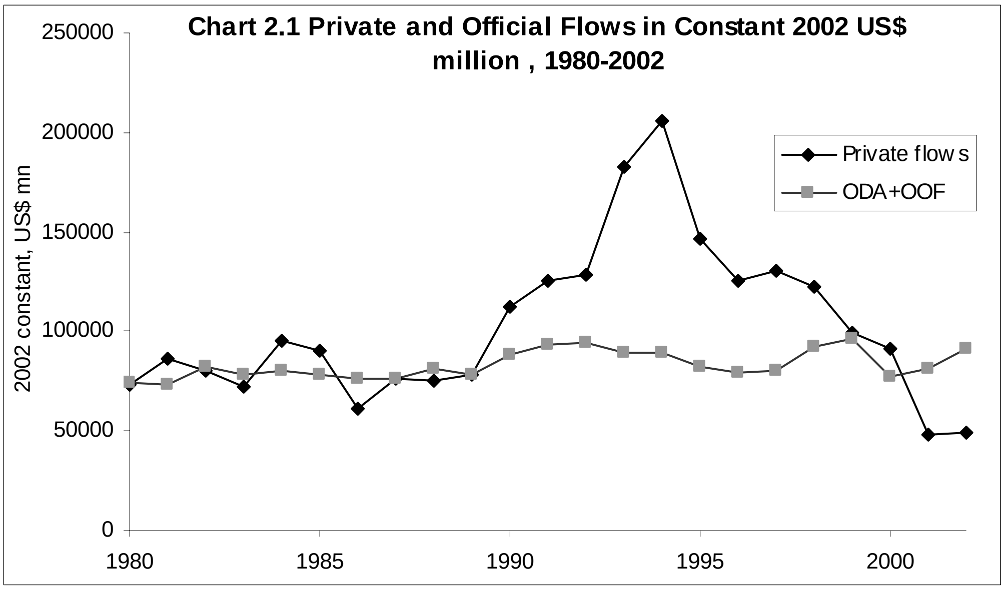
In this context, this study aims to do the following:
- review the trends in donor/creditor financing for low income African countries,
- investigate how donor/creditor and African government practices impact on the quantity and quality of development finance,
- review international efforts to raise the quality of official development finance for Africa and make proposals to accelerate and deepen such efforts
- propose how to empower African governments to have more control over analysing and sourcing the external financing required to enable them to reach the MDGs, as part of a process of mutual accountability and partnership with the donor community.

CHAPTER 2: OVERALL TRENDS AND COMPOSITION OF AID FLOWS TO AFRICA

2.1 GENERAL TRENDS

2.1.1. External Resource Flows to Developing and African Countries

External resources and financial flows to the developing world have undergone some significant changes historically and especially in more recent years. While aid flows rose in the 1980s and early 1990s, they quickly declined after the end of Cold War due to pressures on the fiscal budgets of bilateral donors, and a move to using private capital flows by a selective group of largely middle-income developing countries (see Chart 2.1.).



Note: Measured in gross disbursements
Source: OECD DAC

As Chart 2.1 shows private capital flows (in real terms) have been extremely volatile, and have seen a sharp decline following the Asian financial crisis in 1997/98 to the point where they are now one third below the levels of the 1980s. On the other hand, aid flows, measured as Official Development Assistance (ODA) and Other Official Flows (OOF),[2] have remained steadier and even risen modestly over the last 20 years.

The main developments in the last ten years can be highlighted through a comparison of the volume of aid and private flows in 1992 and 2002 on a regional basis:

- **Africa**: The quantity and composition of aid and private capital flows in 2002 is near identical to that of 1992.
- **Asia**: Both private capital and aid flows in 2002 are more than halved since 1992.
- **South America**: Aid flows have more than halved between 1992 and 2002 and the region has moved from being a net recipient of private flows to being a net contributor.
- **Europe**: The continent received the same amount of flows in 2002 as in 1992 although composition has shifted from predominantly private capital flows to predominantly aid.

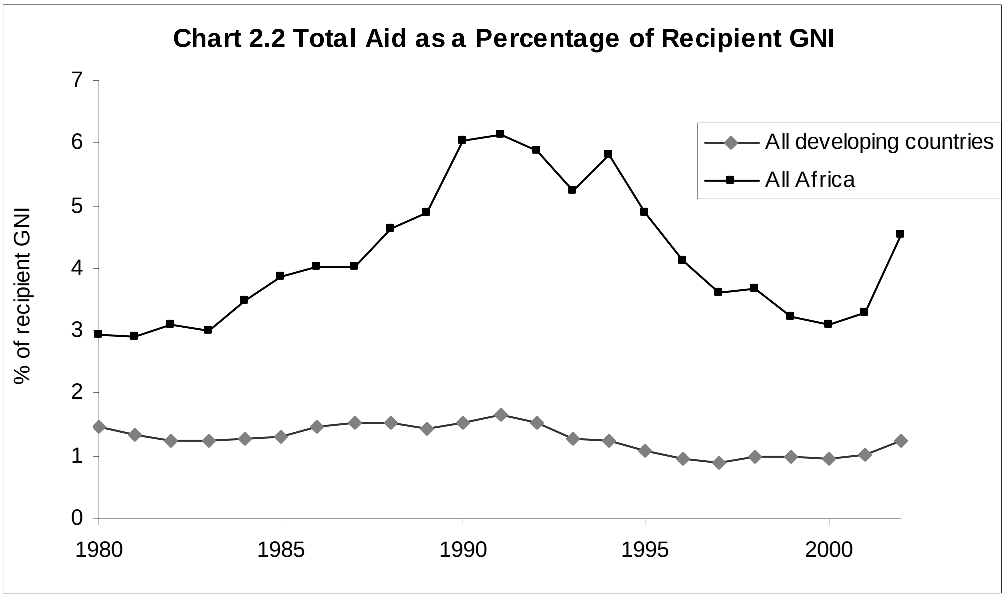
Details of the trends in flows regionally can be found in Annex 2, Charts A.2.1 and A.2.2.

2.1.2. Aid Flows

Total aid flows have increased in nominal terms from about US$30 billion in 1980 to over US$80 billion in 2002. However, the late 1980s and early 1990s stand out as the period of the most rapid growth in aid disbursements (see Chart 2.3). Thereafter, until 2000 they stagnated or declined (falling especially in real terms). This resulted from increased pressure on donors' fiscal balance, which reduced aid budgets, as well as the end of the cold war which reduced the need

[2] For definitions of ODA and OOF see Annex 1.

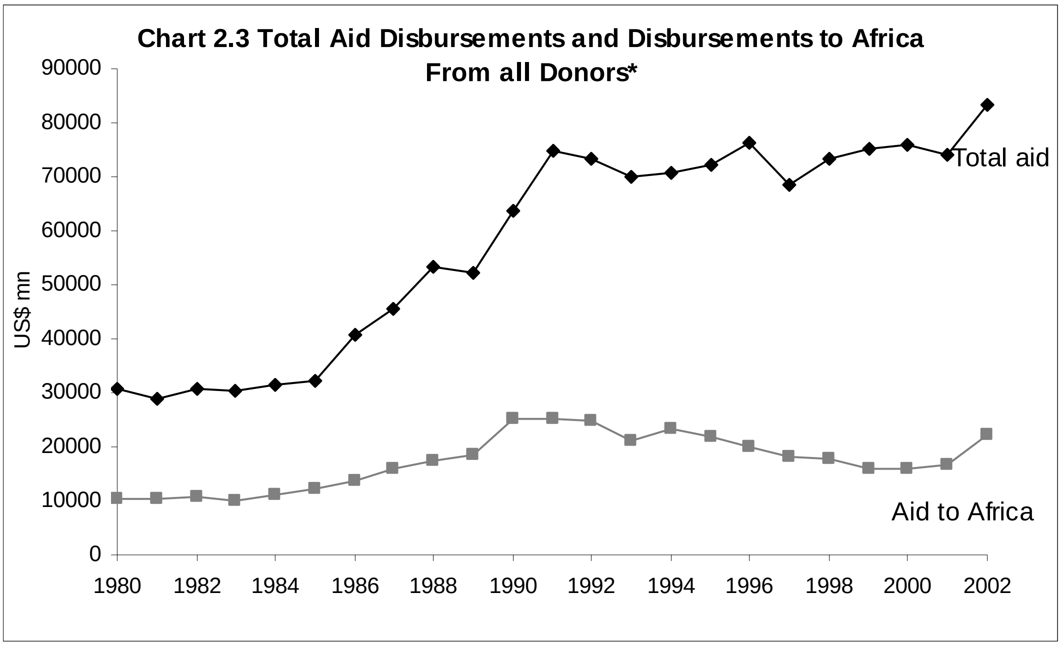
for "strategic" aid flows. Aid has only increased again in 2001-2003, due in part to new aid initiatives but also to growing allocations to debt relief (see also 2.2.3 below).



Source: OECD DAC

Chart 2.2 reflects the relative importance of aid in African countries compared to the developing world as a whole. For Africa, aid as a percentage of Gross National Income (GNI) has been between 3% and 6% over the last 20 years, compared with less than half this figure for all developing countries. The chart also shows a more pronounced fall in aid as a percentage of GNI for Africa during the 1990s, by almost 3 percentage points over 6 years. Yet Africa is now benefiting from a rapid reversal in this trend, with aid rising to 4.5% of Africa's GNI in 2002.

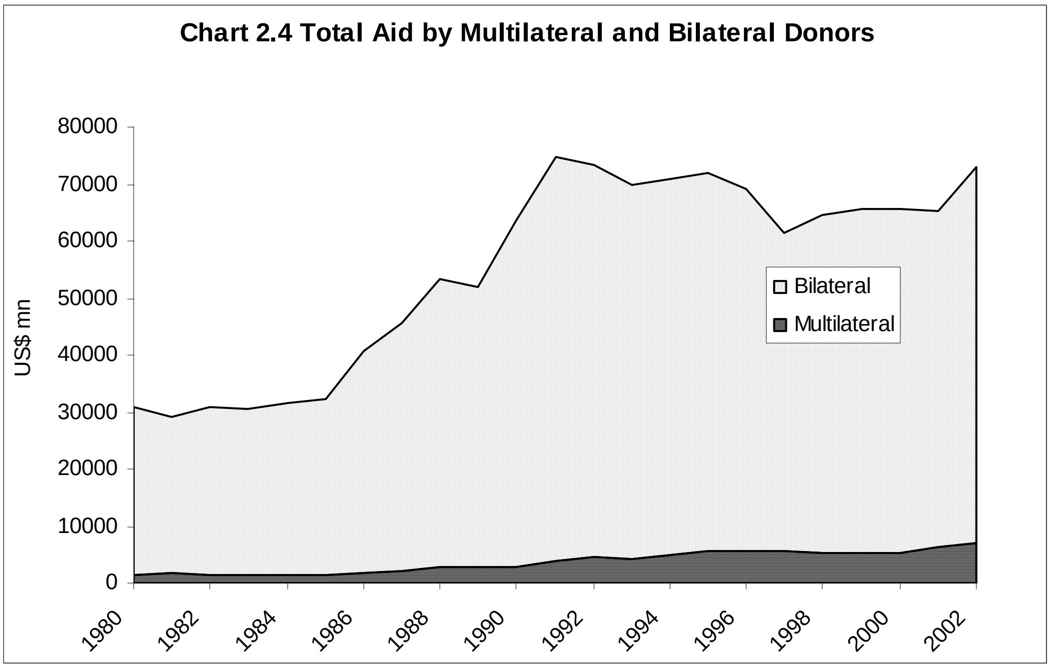
The main reason for the earlier decline in aid to Africa, as illustrated by Chart 2.3, has been a diversion of aid to other regions. Aid to Africa has only doubled in nominal terms in the last two decades, while total aid flows have almost trebled. Aid to Africa declined throughout the 1990s, while aid to Europe (the ex-Soviet Union and Balkans) and South America increased. Only since 2000 has this diversion reversed, with Africa receiving the bulk of the new increase in aid flows.



*****All donors: DAC bilateral donors, multilateral donors and non-DAC bilateral donors.
Source: OECD DAC

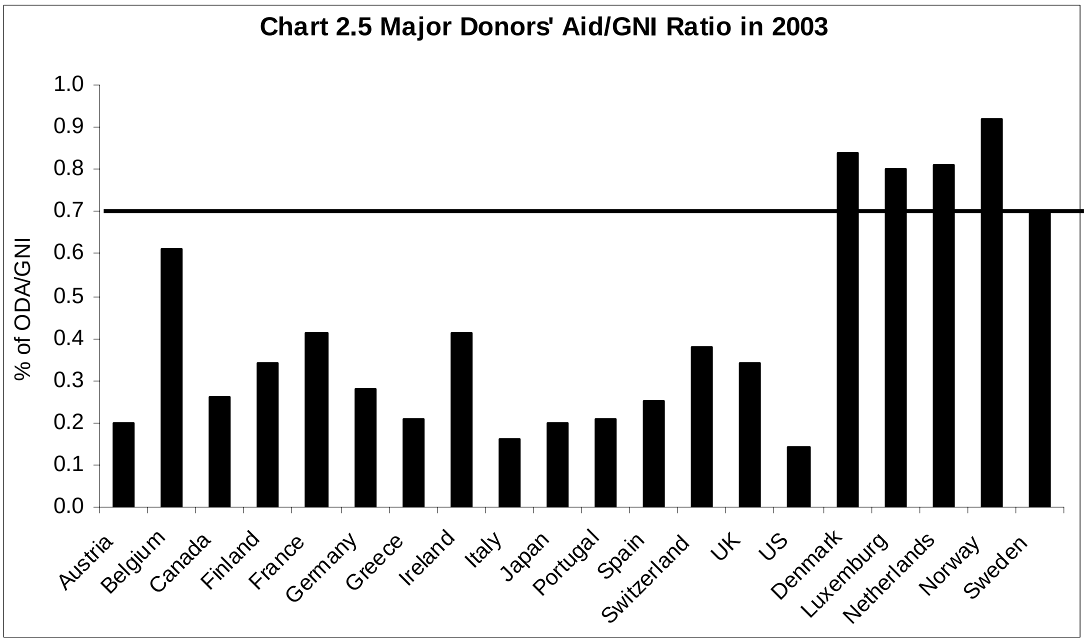
2.1.3. Sources of Aid

For developing countries as a whole, the vast bulk of development aid has always come from bilateral sources (governments). Their predominance has increased since 1980, rising from 87% of all aid to 91% in 2002, as Chart 2.4 highlights. While bilateral aid increased dramatically over the 1980s, before falling slightly in the 1990s, multilateral aid experienced a slower though more steady growth. Bilateral aid in 2002, at US$ 66 billion, was below the peak of US$71 billion in the early 1990s. On the other hand multilateral aid grew from US$ 3.9 billion in 1992 to US$ 7.1 billion in 2002.



Source: OECD DAC

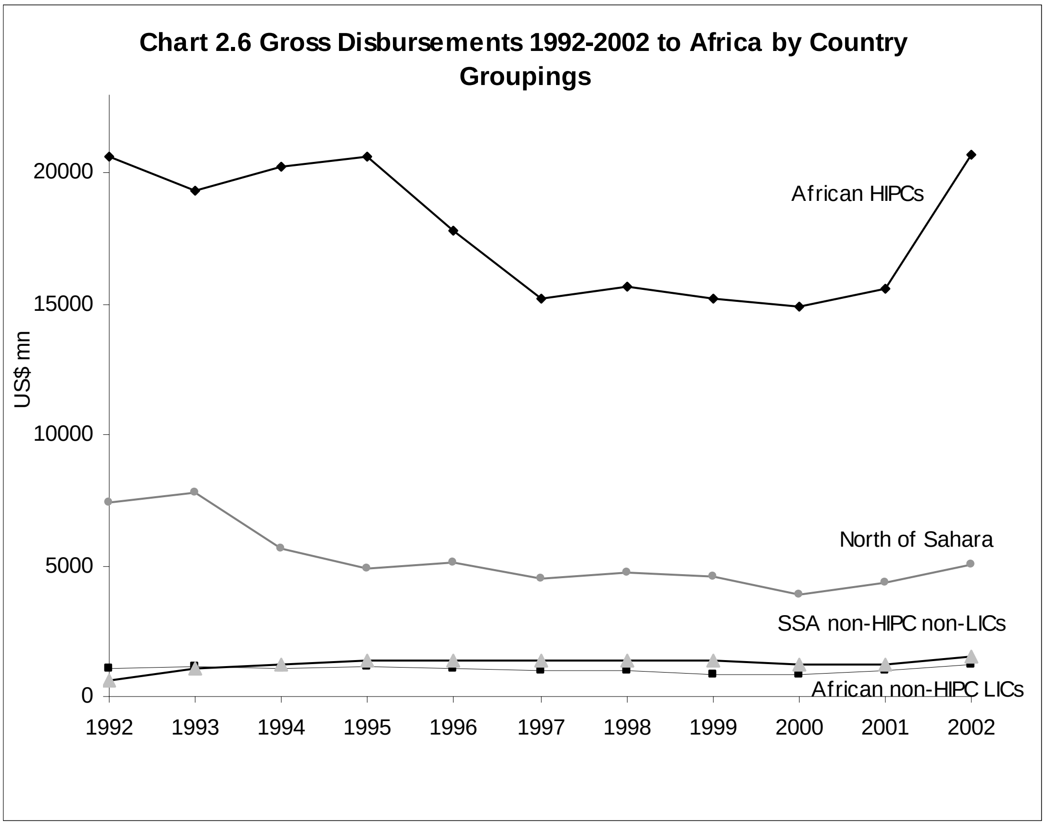
Both multilateral and bilateral donors have recently stepped up their efforts to provide more aid to developing countries. Nevertheless, for bilateral donors, the long-standing benchmark figure of 0.7% of GNI remains a long way off for most OECD countries. Currently only five OECD countries have reached the 0.7% target (Denmark 0.84%, Luxemburg 0.8%, Netherlands 0.81%, Norway 0.92% and Sweden 0.7%).



Source: OECD DAC and Country budget reports

2.2 TRENDS WITHIN AFRICA

Looking more closely at Africa and country groupings within Africa, it is evident that aid flows have not followed the same generally upward trend as the rest of the developing world in the last twenty years (see Chart 2.3 and 2.6.). Since 2001, gross disbursements have bounced back, but around 50% of this has been delivered through higher debt relief.[3] The remainder reflects higher new aid disbursements due to the launching of NEPAD in 2001, greater peace and stability, and progress with PRSPs, which are raising confidence and aid flows to Africa.[4]



Source: OECD DAC

Within the continent, different groups have seen very different trends in aid:

- the 34 African HIPC countries receive the bulk of aid flows to Africa (US$ 20.7 billion in 2002). These flows largely followed the same trend as for the whole continent (see Charts 2.3 and 2.6), declining in 1995-2001 and increasing thereafter. As a result, aid to HIPCs only recovered to 1992 ***nominal*** levels in 2002.
- African non-HIPC low income countries (LICs) and Sub-Saharan African non-HIPC non-LICs received substantially less aid, with gross disbursements in 2002 of US$1.2 billion and US$ 1.5 billion, respectively. However, both these groupings display a more steady gross disbursement picture than for the HIPCs, and disbursements to non-HIPC LICs have stayed at the same nominal levels, while aid to non-HIPC non-LICs actually doubled over the decade.
- Finally, the middle-income countries North of the Sahara have continued to receive high levels of aid, but have not benefited from recent growth in aid, showing an overall decline from US$ 7.4 billion in 1992 to US$ 5 billion in 2002.

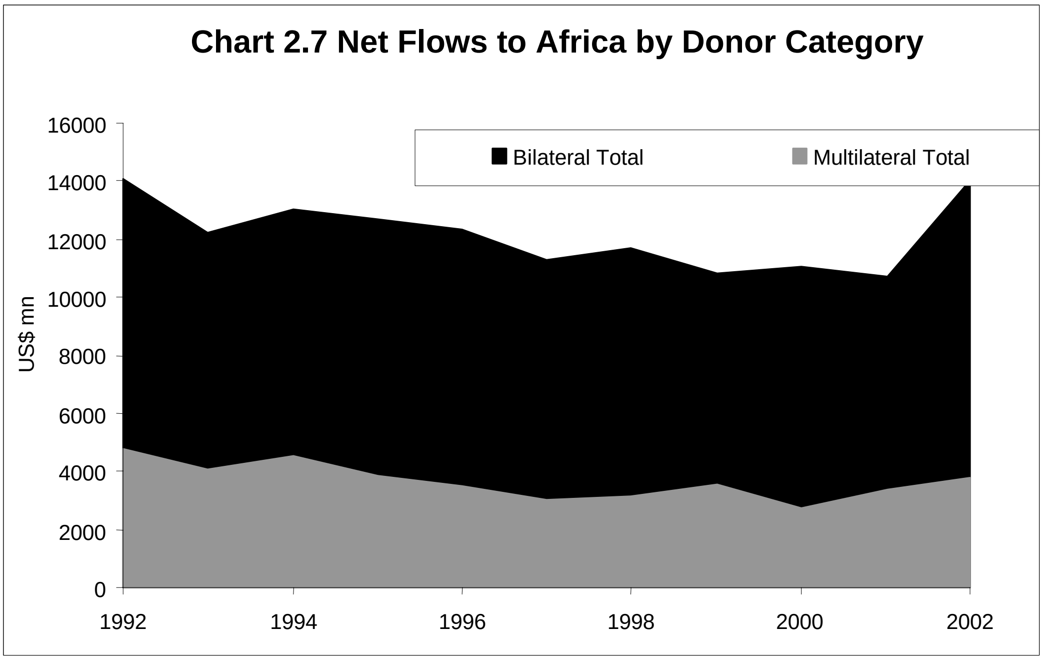
Overall, taking a slightly longer historical perspective, there has not been a diversion of aid from non-HIPCs to HIPCs: rather HIPCs are merely restoring their mid-1990s share of aid to Africa.

2.2.1. Donor Category Trends

Multilateral aid accounts for a much higher share of net flows to Africa than to other developing regions. While it remained steady at between 25 and 30% until 1990, subsequently bilateral net

[3] GDF, 2004
[4] OECD, AfDB, 2002

flows[5] became more erratic and declined during 1992-2001, so that the multilateral share increased to one third in spite of a slight nominal decline (see Chart 2.7.). In 2002, bilateral net flows rose sharply again to US$14 billion.

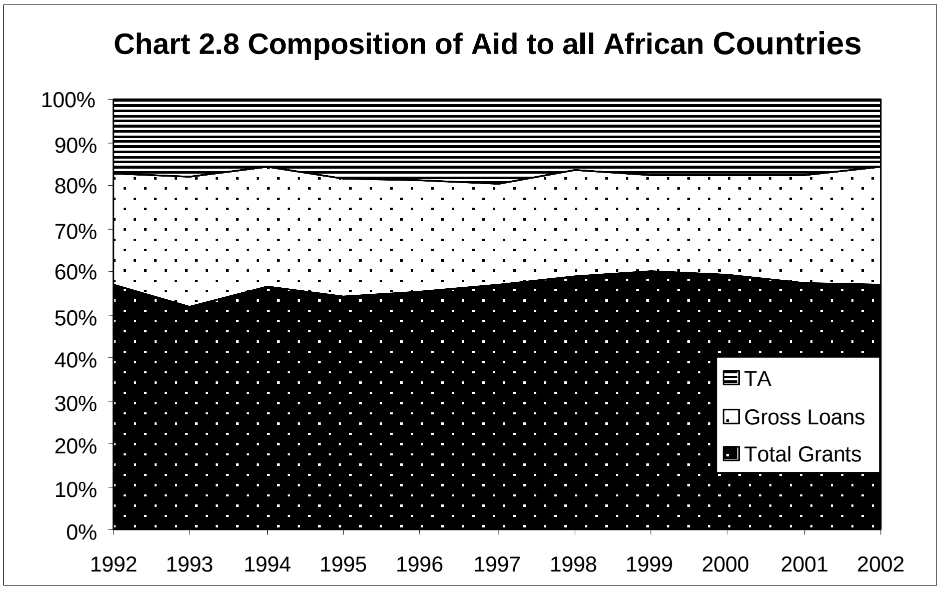


Source: OECD DAC

2.2.2. Grants, Loans and Technical Assistance

According to published DAC data, the breakdown of Africa's aid between grants (50-60%) and loans (20-30%) has remained relatively stable in the last ten years. This stability, reflected in Chart 2.8, is repeated when looking at the African HIPCs, where grants are slightly higher (average 60%) and loans slightly lower (average 20%).

Technical assistance flows have also been relatively stable as a percentage of flows, at around 20%. However, these data vastly underestimate the real size of TA, as they include only separate TA projects and programmes. Around 20% of larger programmes and projects is also estimated by African governments to be on TA, raising making the total TA share to 40%.



Source: OECD DAC

5 Net flows are gross disbursements of loans and grants less loan principal repayments.

The breakdown between grants and loans and technical assistance has, however, shown more marked shifts in the last ten years, when disaggregated into bilateral and multilateral aid. While bilateral aid has shifted further towards grants and technical assistance, and away from loans, the reverse is the case for multilateral aid. A comparison between 1992 and 2002 shows that multilateral loans have risen from 45% to 77% of total aid to Africa. At the same time the share of loans in bilateral aid has decreased from 55% to 23%, as reflected in Charts 2.9 and 2.10 More details of the shift by bilateral donors towards grants and away from loans can be seen in Chart A.2.3 and A.2.4 in Annex 2.

Chart 2.9 Composition of Aid to all Africa by Donor, 2002

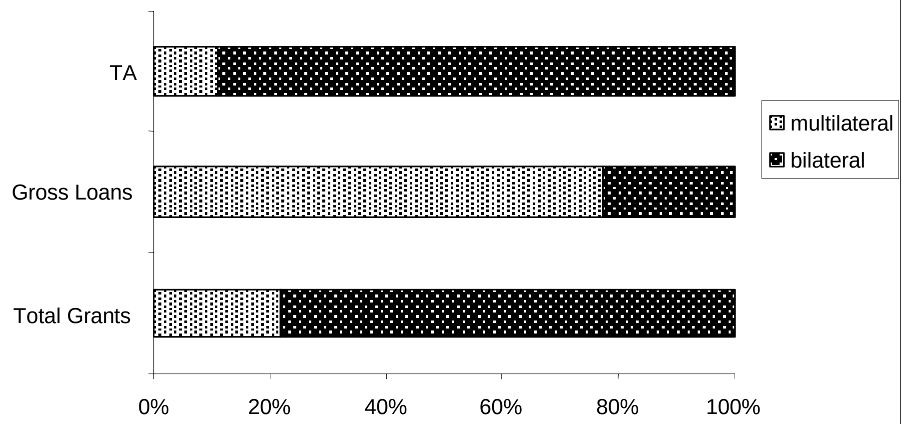
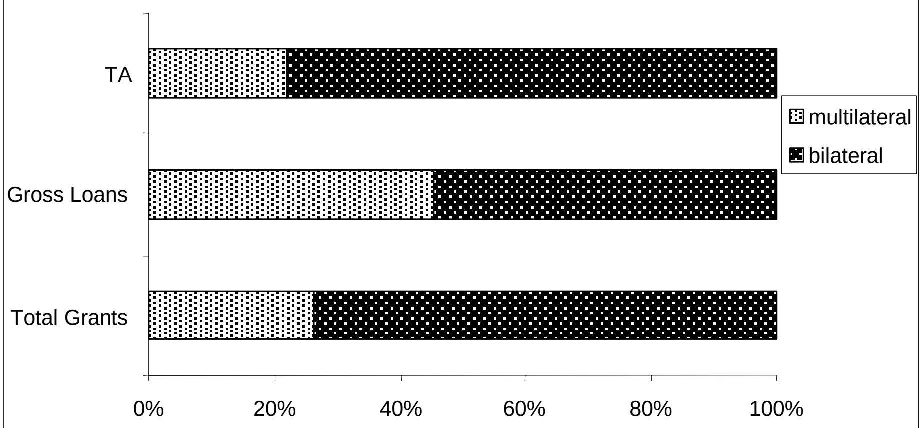


Chart 2.10 Composition of Aid to all Africa by Donor, 1992



Source: OECD DAC

2.2.3. Programme, Project and Other Types of Assistance

The composition of aid flows in terms of programme and project assistance highlights some interesting variations among recipient groups. As Table 2.1 indicates, African HIPCs have seen a dramatic decline in project aid as a share of their total aid (12%) compared to only amall declines for developing countries as a whole and other African LICs. Interestingly, the share of programme aid (budget support) has fallen by between 4% and 6% for all country groups, though preliminary data for 2003 indicate some reversal of this trend. However, while this has been offset for HIPCs by a dramatic increase in the share of debt relief which in many ways is equivalent to programme aid (by 15%), non-HIPC low-income African countries have seen only a 3% increase in the share of programme aid, and have almost all of their aid (92%) concentrated in projects.

For African HIPCS, all African and all developing countries, debt relief has now overtaken programme aid as the second largest form of aid. Emergency assistance also has increased between 1992 and 2002 so that it now represents 7% of aid flows for HIPCs, African countries and the developing world, and is the second most important flow for other African LICs.

Table 2.1 Composition of Aid by Type of Assistance in 1992 and 2002

	Africa						Developing Countries	
	HIPCs		Non-HIPC LICs		Total			
Type of Assistance	1992	2002	1992	2002	1992	2002	1992	2002
Project Aid	66%	54%	93%	92%	63%	63%	75%	72%
Programme Aid	22%	17%	6%	2%	18%	14%	15%	9%
Debt Relief	7%	22%	0%	3%	14%	17%	8%	12%
Emergency Assistance	5%	7%	1%	4%	5%	7%	3%	7%

Source: OECD DAC

2.2.4. Aid and PRSP Spending

There has been increased pressure on donors to provide assistance in sectors relating to meeting the MDGs and that have a direct impact on reducing poverty. Charts 2.11 and 2.12 appear to show that there has been relatively little progress in this area. Only 15% of ODA actually went towards PRSP sectors in African HIPCs in 2002. Agriculture and Water Supply and Sanitation have seen reductions in shares of 5% and 2% respectively since 1992. Meanwhile ODA to Basic Education and Basic Health is up by 1% and 2% respectively. However as almost all HIPC-related debt relief is also going to PRSP spending, the total of aid going to PRSP sectors is likely to be closer to 35%, compared to around 20% in 1992.

In terms of technical assistance there is a higher concentration on PRSP sectors. A total of 26% of technical assistance is allocated to PRSP sectors in African HIPCs (especially basic health and education), while the figure for all Africa is a mere 13%.

Chart 2.11 African HIPCs ODA by PRSP Sectors, 2002

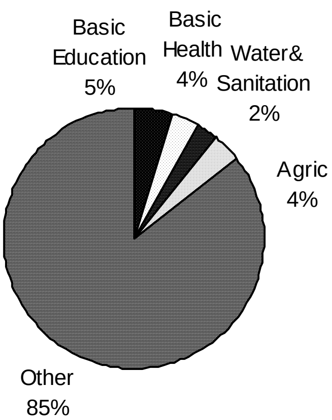
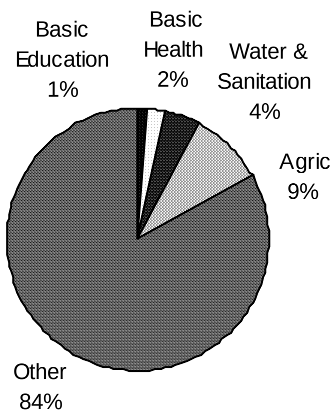


Chart 2.12 African HIPCs ODA by PRSP Sectors, 1992



Source: OECD DAC

2.2.5. Aid Tying

Over the last decade moves to untie aid have been at the forefront of aid reform. As illustrated in Charts 2.13 and 2.14, this aspect of aid reform has been relatively successful, such that 89% of aid to African HIPCs is now untied, compared to 53% in 1992. For Africa as a whole 80% of aid was untied in 2002, compared with 51% in 1992 (see also Charts A.2.5 and A.2.6 in Annex 2). However, non-HIPC Sub-Saharan African low-income countries, and North-African countries, have not seen the same progress in untying aid, and continue to have tied or partially tied aid at 63% and 53% respectively.

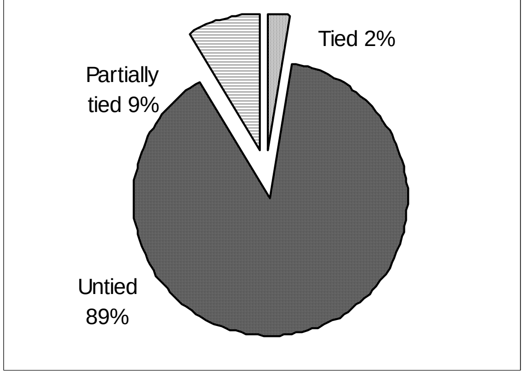


Chart 2.13 Tied, Partially Tied and Untied Aid to African HIPCs, 2002

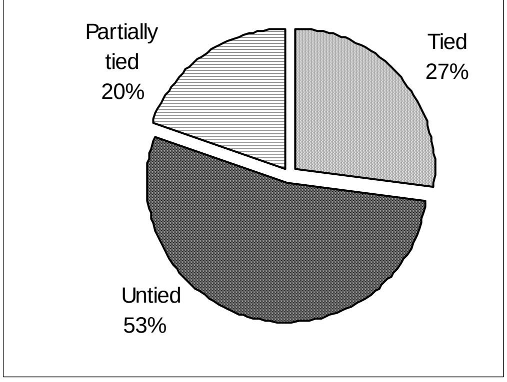


Chart 2.14 Tied, Partially Tied and Untied Aid to African HIPCs, 1992

Source: OECD DAC

2.3. Recent Initiatives And Prospects For Aid To Africa

2.3.1. Aid Quantity

Recent initiatives have dramatically improved prospects for a higher quantity of aid to Africa. Commitments made in 2000 around the time of the Monterrey Financing for Development Summit, implied a 25% increase in aid flows above the existing US$50 billion. Since then, Belgium, France, Spain and the UK have gone further in their pledges of 0.7% of GNI, indicating that the intended increase could now be closer to 40% or US$20 billion.

For Africa, the outlook is even brighter, given that major donors at the 2003 G7 Summit in Evian agreed that 50% of additional aid (as opposed to 25% of current aid flows) would go to Africa. Donors have also indicated that most of the new funding will go to low-income countries, reversing the continuing excessive focus of aid on middle-income countries. Nevertheless, given that the additional aid needs to meet the MDGs are estimated by various sources at US$50 billion per annum until 2015, even current pledges fall well short of needs.[6]

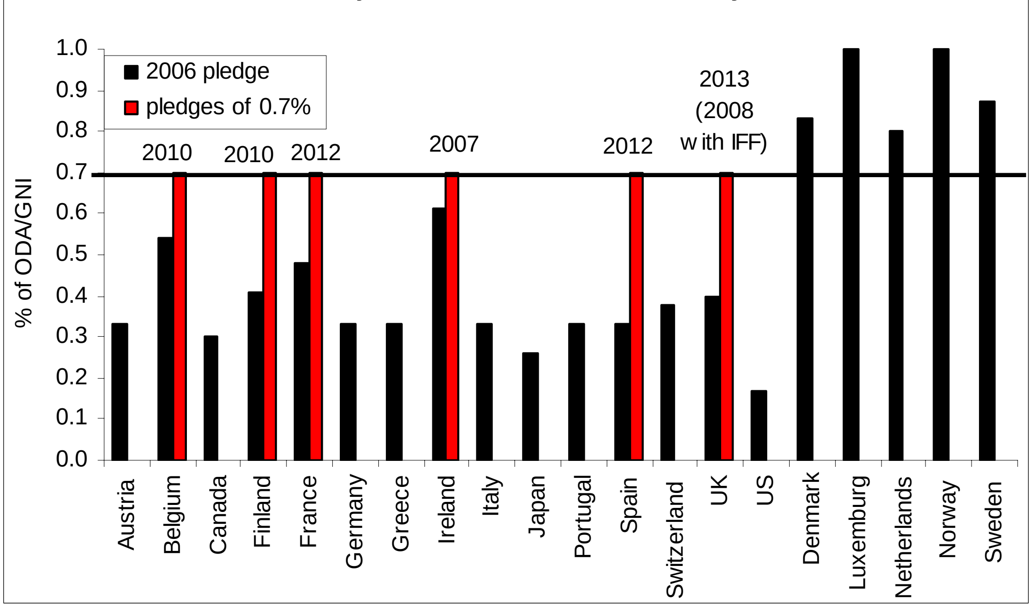


Chart 2.15 Major Donors' Aid/GNI Ratio Beyond 2006

Source: OECD, DAC

[6] IDA 14, 2004

As shown in Chart 2.15, fulfilling recent pledges would allow major progress towards 0.7% targets. However, only four more countries have fixed dates for meeting the target before the end of the decade (Ireland by 2007, Belgium and Finland by 2010, and the UK by 2010 if the IFF is introduced), which would mean that only 9 of the 20 largest OECD donors will reach the target by then. France and Spain have indicated their intent to reach the target but without setting precise deadlines, and 9 countries have not even indicated any intent.

In general, according to DAC preliminary data for 2002-03, increases in disbursements appear to be living up to pledges – with one notable exception being the US, where congressional appropriations are delayed and much lower than expected. Equally positively, international civil society and government support for aid has grown considerably, building on the demonstrated success of debt relief and other poverty-focussed aid in achieving universal primary education and major health improvements in several low-income African countries.

2.3.2. Aid Quality

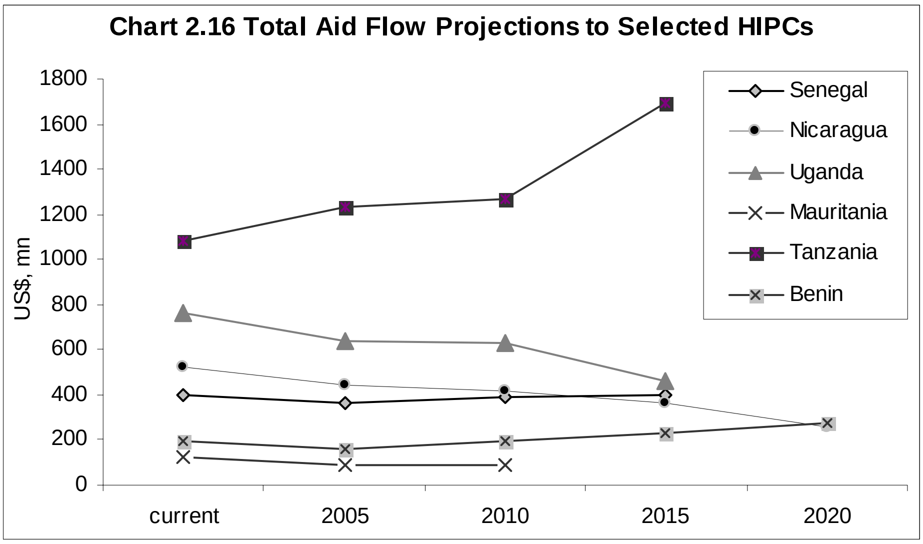
The international community has also committed itself to improving the quality of aid, through various initiatives, notably the Rome Declaration on Harmonisation, and follow-up initiatives by the OECD Development Assistance Committee (DAC) and the Strategic Partnership with Africa (SPA) to monitor progress in improving aid quality. However, these initiatives and Africa's own analysis (see Chapters 3 and 4) indicate that, in terms of quality, less progress is being made:

- One positive feature is that almost all of the additional funds will be provided as grants,. The multilateral development banks (IDA and AfDF) in particular look likely to increase the share of their finance provided as grants – but it will be essential that these shifts are fully funded by large-scale bilateral grants in order to avoid undermining their long-term ability to support low-income countries which depends in part on using loan reflows.
- There is also likely to be an increase in the share of multilateral institutions, notably with large intended replenishments for IDA and the AfDF. This is seen by African governments as potentially positive in reducing transaction costs and "strategic" motives for aid allocation, but negative in making Africa more dependent on a few aid sources.
- Some donors (such as the UK) have indicated their intent to switch further towards multi-year programme aid (budget support), which can disburse more predictably and flexibly to offset exogenous shocks for African countries, but most of the recent pledges (notably the US Millennium Challenge Account) will be implemented as project aid, potentially implying slower disbursement and more cumbersome procedures.
- Another potentially positive aspect is that there looks likely to be an increasing concentration of aid on poverty reduction sectors. However, this is offset by the fact that most donors continue to take a very narrow view of priority sectors, focussing on primary health and education, while penalising growth-promoting sectors such as basic infrastructure, agriculture and micro-credit.
- Other new initiatives, such as the Global Fund to Fight AIDS, TB and Malaria are being constructed almost entirely outside the current drive for harmonisation and simplification of procedures, and requiring spending additional or parallel to PRSPs.
- Overall conditionality and cross-conditionality on aid flows may well be tightening with the growing[7] .
- There is little sign of a serious initiative by most donors to reduce technical assistance and move to genuine capacity-building.
- There is also little sign of further progress on untying for non-HIPC LICs or on untying remaining technical assistance or emergency aid.

2.3.3. IMF Programme Projections

One of the intended effects of additional aid flows is to allow African countries to spend more on attaining the Millennium Development Goals. However, aid forecasts in IMF programmes are lagging behind the new trends. Overall, aid flows are being forecast to fall in 50% of programmes, to stagnate in 25% and to rise in only 25%. This leaves programmes having to be overoptimistic about the potential financing contribution of non-debt private flows in order to finance their growth, and falling short of increased government spending needed for the MDGs.

[7] See Killick (2004).



Source: IMF, World Bank

In addition, there appears to be an inverse relationship between projected aid trends and economic performance (as measured by World Bank CPIA or IMF stabilisation indicators). As shown in Chart 2.16, of the top six scorers on CPIA, five have falling aid flows in medium term, though three have rising flows projected for the long-term – while the worst performers have rising aid projections.

There is also no clear or consistent rationale behind programme projections – for example, either increased aid flows in short-to-medium term to allow increased spending on MDGs, or of reducing aid dependence in the medium-term as good macroeconomic performance allows country to mobilise more domestic resources for MDG funding. Yet, in relation to GDP, almost all medium-term projections of aid flows are falling sharply.

In terms of quality, there is also no consistent rationale:

- Grants are being forecast to be falling or stable in 85% of programmes, whereas loans are forecast to rise in 35% of programmes. There is also no evidence of projecting a switch to grants for those countries with the highest debt burden. Indeed grants are projected to exceed loans in the next ten years only for around 60% of countries.
- Nor is there any consistent projected increase in the concessionality of loans (most projections are based on the same terms as in recent years).
- Programme aid is being forecast to tail off rapidly, but project aid forecast to continue at around current real or nominal levels. There is no consistent forecast of higher programme aid for the best performers.
- Projections of low grant flows, low concessionality and low levels of budget support in government financing have meant that, in order to avoid renewed debt unsustainability, PRGF macro frameworks have to be more restrictive (eg in Ethiopia, Mali and Rwanda), allowing governments to spend less money than desired, falling short of the MDGs.

2.3.4. Aid Shortfalls

There is a considerable literature indicating that aid volatility and shortfalls are major causes of macroeconomic instability in African countries[8], undermining progress to the MDGs. Evidence from HIPC CBP workshops is that shortfalls compared to projections average 14% for programme aid, but 26% for project aid. Grants also appear to be more vulnerable to shortfalls than loans. In almost all IMF programmes, projections are inaccurate by more than 10% - and in 50% of programmes, by more than 20%.

There is little evidence that shortfalls are related to country "performance" in terms of either medium-term IMF track record or CPIA indicators. Rather, programme aid shortfalls seem to be much more linked to specific events such as electoral cycles, natural disasters, or suspensions of IMF programmes. However, larger and consistent project aid shortfalls are linked to major problems with donor and government disbursement procedures. On the other hand, there is

[8] For example, Bulir and Hamann (2001).

growing evidence that, for some countries, shortfalls are falling rapidly in countries where donors are switching to faster-disbursing programme aid and establishing improved mechanisms (such as multi-donor budget support) for disbursement.

2.3.5. The Impact of Aid[9]

One important reason for the increased quantity of aid (and the slower improvement in quality of aid) is the belief, based on evidence of the success of new PRSP-oriented budget support, debt relief and project aid, that aid can have a positive impact on growth and poverty reduction. The literature overwhelmingly supports these conclusions.

However, three concerns continue to be commonly raised about growing aid flows:

- ***African absorptive capacity constraints***. It is extremely common in the donor community to hear that country X (or sector Y within a country) cannot absorb more aid. This is usually based on a static view of country absorptive capacity based on current government and donor procedures. A recent World Bank paper on supporting the MDGs has stressed the need for long periods to improve absorptive capacity in many low-income African countries. Yet there are a growing number of dramatic success stories in increasing absorptive capacity in Africa. In 1998 in Uganda, when President Museveni launched Universal Primary Education, donors doubted that Uganda could absorb more aid for education. Five years later Uganda is absorbing three times as much donor education funding. Various other HIPCs have in recent years successfully implemented programmes such as decentralisation, MTEFs, financial accountability capacity building and procurement reform, which have dramatically increased their absorptive capacity. As a result, African officials are confident that large expenditure programmes are currently under-funded and could rapidly absorb additional money.[10]
- Excessive aid dependency. Donors and African governments have all long been worried about excessive dependency on donor aid, which can have negative effects on economic performance and divert policymaker attention from managing the economy to dealing with aid. However, recent literature indicates that the level of aid at which is begins to have consistent pernicious effects is around 25% of GDP, well above the current levels for Africa as a whole and almost all African countries. In addition, there are concerns in a context of increasing aid about the long-term sustainability of the flows and therefore of funding to maintain the investments they fund. However, this can be overcome by donor commitment to long-term aid flows (for example through until 2015) – and initial kick-starting aid will be essential to African economies growing to the point where they can generate more tax revenues to fund their own long-term development.
- Potential risks of Dutch Disease. Some have suggested that rapid increases in aid flows could appreciate Africa currencies and undermine competitiveness of exports, thereby compromising long-term growth prospects. However, a growing literature of multi-country and country-specific analysis[11] is indicating that the supply effects of high-quality aid should be expected to offset demand effects and eliminate virtually all risk of Dutch Disease.

Overall, high quality aid can be expected to overcome all of the above problems. Recent analysis[12] has indicated that Africa could absorb an additional US$12 billion a year in aid, especially if large countries such as Nigeria and Sudan begin receiving funds. This would also be the minimum necessary for African countries to have any chance of attaining a reasonable proportion of their Millennium Development Goals. But, of course, better policies and procedures, leading to higher quality aid flows, would vastly improve their positive impact - as one example, untying the remaining tied aid to Africa would increase the value of aid by 10% at a stroke. The following chapters therefore look in more detail at progress on recipient government and donor policies and procedures, to assess the priorities for action.

[9] This section is based on the excellent literature survey by Foster (2003), which accords with the views of African governments that high-quality aid can have major positive effects and that the potential negative effects ad absorptive capacity constraints are considerably exaggerated.

[10] See HIPC Ministerial Declarations (www.dri.org.uk), and also the many success stories on absorptive capacity cited at the Beijing conference on Scaling Up in 2004.

[11] See Adam and Bevan (2003) and Mwanza (2004)

[12] See Foster 2003; World Bank 2003

CHAPTER 3: ASSESSING THE QUALITY OF AID FLOWS

It is striking that, in spite of recent initiatives on harmonisation of donor practices and the PRSP-based partnership of African governments and donors, there is no systematic monitoring across all African recipient countries, at an individual recipient country level, of whether donors are living up to their pledges on aid quality and support for the PRSP framework, or behaving consistently across a range of African countries. Even more important, African countries are not systematically empowered to lead the monitoring of the improvement of aid quality themselves – donors still lead the process in most countries.

To redress this situation the HIPC CBP has prepared a methodology to enable governments to assess the quality of aid they receive as part of the process of designing overall national debt and new financing strategies[13]. This involves training African governments in an objective framework for analysing donor and creditor (and their own) policies and procedures, in order to help them identify which are the 'best' external financing sources to fund their poverty reduction and economic development programmes, and how they can improve the quality of all their external finance.

3.1 HIPC CBP METHODOLOGY FOR ANALYSING DONOR/CREDITOR POLICIES AND PROCEDURES

The 'traditional' factors used by African governments to assess resources available from donors and creditors are the concessionality of funds being offered, as measured by the grant element[14], and the amount being made available. While these two factors can provide a quantitative basis for assessing donor/creditor resources, they do not encompass the qualitative aspects of funds, such as, is the money being provided as fast disbursing budget support or as slow disbursing project aid or as technical assistance to fund foreign consultants? Furthermore, are the resources predicated on the government fulfilling multiple conditionalities and are they to fund the government's priority sectors and projects, as set out in its Poverty Reduction Strategy Paper, or to finance a donor-driven project?

So if African governments are to take into account the qualitative, as well as the quantitative, aspects of donor/creditor resources, they need to have a framework for analysing individual donor and creditor aid policies taking into account both the quantitative and qualitative aspects of aid. The key policy factors and issues to be addressed are as follows:

- **Concessionality:** does the donor/creditor provide grants, or loans or both? What is the average grant element of the recently-signed loans and is this in line with the concessionality ceilings or other terms established by government policy? Does a creditor provide non-concessional funds and, if so, on what grant element and terms?
- **Types of Assistance:** what percentage of the donor/creditor support is provided as programme/budget support, sector support, project aid, technical assistance or food aid/aid-in-kind? Is the budget, balance of payments or sector support entirely un-earmarked?
- **Channels of Assistance**: what percentage of the donor/creditor support is provided directly to the Ministry of Finance budget, as opposed to via the line ministries or other agencies, or with a government guarantee for the private sector?
- **Sectors and Projects**: which sectors or projects has each donor/creditor funded and are these in support of the key PRSP priority sectors/projects? Does the donor/creditor specify separately its priority sectoral or project support, or is all aid to PRSP priority sectors/projects provided by budget support?
- **Flexibility**: has the donor/creditor come forward rapidly to fund unanticipated budget or balance of payments financing gaps with programme aid, and to respond to new government priority areas? Does it have a reserve of contingency programme aid that can be allocated to the country in the event of external shocks?
- **Predictability:** does the donor/creditor agree to commit funds several years in advance or on an annual basis? Does it continually pledge to provide external assistance but fail to deliver commitments on time or not at all?

[13] While the methodology was initially developed for HIPC governments under the HIPC CBP programme, it is just as applicable to and can be used by all African countries. It can also be applied to non-aid external finance flows.
[14] See Annex 1 for an explanation of how the grant element is calculated.

- **Conditionality:** does the donor/creditor have no conditionalities additional to implementation of government policies in the PRSP or PRGF, or are there a considerable number of additional bilateral policy conditions (e.g. sectoral, project-specific etc.)? How strictly does the donor/creditor enforce its conditions before suspending flows? Are the bilateral conditionalities easy to comply with or are they time consuming resulting in significant disbursement delays?
- **Policy Dialogue:** how strictly are the donor/creditor disbursements tied to IMF and World Bank programme implementation, or is there flexibility for it to decide to continue disbursing even if there are temporary problems with the BWI programmes? To what degree does the donor/creditor play an independent role in the macro policy dialogue, encouraging African country leadership, streamlining of BWI conditions and flexibility in the macroeconomic framework?

By focusing on these factors and issues, African governments can document individual donor/creditor aid policies and assess their compatibility with national requirements.

In addition to their aid policies, donor/creditor procedures for disbursement and procurement of aid can have a significant impact on the actual resource flows to a country. In particular the main factors and issues relating to donor/creditor procedures are as follows:

- **Conditions Precedent:** does the donor/creditor require only a legal opinion before loan and grant agreements are effective and disbursements can commence? Or does the donor/creditor impose many conditions precedent and are these conditions relatively straightforward or difficult to comply with and what sort of disbursement delays arise as a result?
- **Disbursement Method:** which disbursement method (direct cash, by reimbursement, direct to suppliers or a combination of all these methods) does the donor/creditor favour? What percentage of funds is disbursed by direct cash, reimbursement claim and/or direct to suppliers? Does the disbursement method vary with the type of finance (loans vs. grants, programme vs. project)? What implications does the method of disbursement have for the timeliness of disbursement receipts and what length of delays can arise on average?
- **Disbursement Schedule:** does the donor/creditor disburse funds according to a schedule or is the timing of disbursements irregular at its own discretion? If there is a disbursement schedule, is it agreed with government and is it in line with government budget planning?
- **Disbursement Procedures:** does the donor/creditor have many or fewer procedures and are these easy or difficult to comply with? Does the donor/creditor require government to provide matching funds in the budget? In addition, are donor/creditor disbursements affected by monitoring issues such as regular project reviews, pre-shipment or destination shipment inspections, banking arrangements, timing within the donor/creditor financial year, submission of regular accounts and reports, bureaucratic requirements and ‘red tape’, and project implementation procedures?
- **Procurement Procedures**: which type of donor/creditor finance (loans, grants, export credits, programme vs. project) is tied, partially tied and untied and if so, by what percentage? What percentage of loan/grant funds can be used for national procurement? Does the donor/creditor insist on international competitive bidding for all procurements or are there limits below which direct purchases can be done? Are international competitive bidding procedures cumbersome to implement and do they result in significant disbursement delays and if so, for how long?
- **Co-ordination:** are there any formal donor/creditor initiatives for harmonising and co-ordinating disbursement and/or procurement procedures and practices? If so, does the donor/creditor participate? What degree of harmonisation of procedures is being achieved through the existing initiative(s)? Which donors/creditors already have common disbursement and procurement procedures, outside of any formal initiatives? What procedures are common to these donors and creditors? Is the donor/creditor willing to adopt or abide by government disbursement and procurement procedures (if these exist)? Or does the donor/creditor insist on following its own procedures?

On the basis of both the policy and procedural factors, the CBP methodology uses a set of 23 evaluation criteria, grouped under 13 headings for which each donor/creditor can be assigned a score (with 1 scoring lowest and 5 highest) on the basis of objectively verifiable thresholds.

Using these criteria African governments have assessed the overall quality of each donor's and creditor's resources on an objective basis.

These findings can then be combined with an analysis of the amount and percentage of total disbursements provided by each donor and creditor during recent years. This will yield an indication of the degree of reliance of the recipient government on each donor/creditor, and whether the government should be aiming to diversify or reduce its list of donors and creditors.

3.2 ANALYSIS OF AFRICAN GOVERNMENT POLICIES AND PROCEDURES

Using the same factors, the HIPC CBP methodology can be drawn upon to identify whether or not African governments have clear new financing policies and procedures and assess the impact these have on the delivery of external assistance flows. The key policy factors and issues to be addressed from the point of view of African governments are as follows:

- **Concessionality**: are there limits on the amounts and/or terms of new grants and loans that can be contracted? Is there a stated preference on the type of new financing to be sought e.g. for grants over loans? Are new borrowings on non-concessional terms allowed and, if so, under what conditions?
- **Types of Assistance**: is there a stated preference for a particular type of assistance (programme/budget support, debt relief, sector support, project aid, technical assistance, food aid)? Is there a stated preference for any particular type of supplier of finance – multilateral or bilateral donor/lender, external commercial lender?
- **Channels of Assistance**: does the government have a stated preference for the channels of assistance (i.e. on/off budget, via Ministry of Finance or via line ministries)?
- **Sectors and Projects**: which are the government's key sector/project spending priorities to be supported by external assistance?
- **Flexibility**: does the government have a preference for the most appropriate assistance for budget or balance of payments gap financing? Is there a need for contingency financing in the event of external shocks?
- **Predictability**: has the government expressed a view on which donors/creditors provide the most predictable and consistent financing in support for the government's policies?
- **Degree of Conditionality**: has the government expressed any preference for the degree or type (macro, sectoral, project) of conditionalities to be placed on donor and creditor funds?
- **Policy Dialogue**: is the government providing leadership in its dialogue with donors and creditors on macro policy, streamlining of Bretton Woods Institutions' conditionalities and flexibility of the macroeconomic framework?

In addition, the methodology can also be used to assess whether the government has its own clear ideas of what it would prefer from donors/creditors in terms of their procedures, as well as the impact of the government's own procedures for processing conditions precedent, disbursements and procurement on actual aid delivery, as follows:

- **Conditions Precedent**: do delays occur because the government has difficulty processing and complying with the conditions and, if so, which are the most difficult? Are there delays in the government informing the donor or creditor that conditions have been fulfilled and if so, why?
- **Disbursement Method:** do delays arise because of difficulties preparing reimbursement claims and disbursement requests? Do the delays arise because of difficulties receiving information needed for reimbursement claims from line ministries and projects and if so, why?
- **Disbursement Procedures:** are there problems with the availability of matching funds and has this led to project or programme delays? What are the main reasons for a lack of matching funds? Are funds usually available to meet down payment requirements for export and suppliers credits? Do the government's arrangements for monitoring projects and programmes cause delays to disbursements? Do the government's accounting and reporting procedures lead to delays? Do staffing issues/constraints cause delays to processing disbursements and if so, what are the key problems? Are there delays arising because of cumbersome central back or commercial bank procedures for opening bank accounts, handling foreign exchange transactions, processing deposits and claims and other financial procedures?

- **Procurement Procedures:** do government procedures for vetting bids and awarding contracts cause delays? Does the government have its own procurement procedures? Do these procedures result in timely procurement or is this a slow and cumbersome process? Are delays in getting customs clearance for imported goods a problem? Do donor/creditor requirements for tax exemptions on imported goods take time to process and result in delays?
- **Co-ordination**: has the government established its own disbursement and procurement practices that it would like donors/creditors to use? Have donors/creditors been informed of these procedures? Has the government tried to get donors/creditors to harmonise reporting and financial procedures and if so has this been successful? Have donors/creditors lined up behind government procedures and if so which ones?

3.3 OVERALL ASSESSMENT OF AID QUALITY

By combining the assessments of donor and government policies and procedures, the HIPC CBP methodology enables African governments to do the following:

- Prioritise the most desirable donor and creditor sources of future new financing,
- Assess donors/creditors providing good and poor quality aid and highlight donors/creditors which the government should target to provide better quality and more aid in future,
- Identify priority areas for overall improvement of donor and government policies and procedures at the individual country level,
- Design a matrix as a framework for African governments and donors/creditors to work in partnership to strengthen quality and delivery (for an example, see Chapter 5.),
- Exchange information with other countries and monitor donor/creditor behaviour in Africa and other developing country regions against their international policy declarations, to see whether donors/creditors are behaving consistently and implementing best practices across all countries, and identify priorities for global initiatives on external assistance quality.

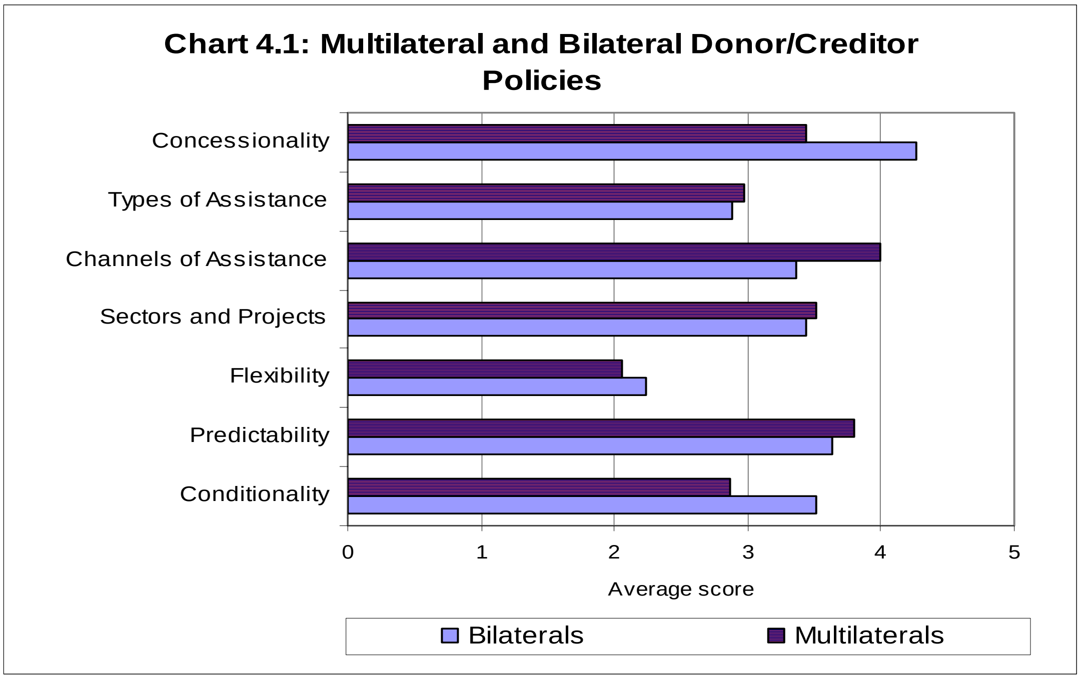
CHAPTER 4: ANALYSIS OF DONOR/CREDITOR AND GOVERNMENT POLICIES AND PROCEDURES – MAIN FINDINGS

The results of the analysis of donor/creditor and government policies and procedures, by thirteen African HIPCs, using the HIPC CBP methodology, are presented below. For each policy and procedural criterion, the results for both donors/creditors and government are presented together to show clearly the interaction between African government policy and procedural preferences for external resource flows, donor/creditor behaviour compared with what African governments want and the problems African governments encounter in compliance, due in part to a lack of adequate national policies and procedures.

4.1 DONOR/CREDITOR AND GOVERNMENT POLICIES

The main findings of the analysis of donor/creditor policies by African HIPC governments using the HIPC CBP methodology, illustrated in Chart 4.1[15], are as follows:

- The most problematic issue for HIPC governments is the lack of flexibility of funds, as many donors and creditors are much less willing than desired to provide additional budget or balance of payments support to meet exogenous shocks, or to switch funds to new urgent government priorities.
- Excessive conditionality on funds, poorer types of assistance (especially multiple small projects and technical assistance) being provided, funds continuing to go to non-priority sectors and projects, and low predictability of funds (donors failing to disburse as pledged, to pledge multiyear funding, or to disburse in line with African HIPC governments' budget timetables) are other very important aspects of donor and creditor policies, which affect the efficient and effective delivery of aid resources to African HIPC governments to meet the Millennium Development Goals (MDGs) and to maintain debt sustainability.
- Multilateral sources of finance tend to be more reliably channelled through budgets as programme aid, to the priority sectors and projects of the government, and more predictable. On the other hand, bilateral sources have greater concessionality, more flexibility and less conditionality.



For African governments, the main finding is that most lack a formal external financing policy on aid. What exists tends to focus on concessionality, set out in the country's national debt strategy or on occasion in law, and on priority sectors, usually defined in the Poverty Reduction Strategy.

[15] Results for Policy Dialogue are not included in Chart 4.1 as the methodology has been recently updated to include this criteria and results are only available for a small number of African HIPCs at this stage.

The lack of a comprehensive government external financing policy enables donors/creditors to maintain the leading role in driving a country's aid policy and the resulting quality of aid flows.

More broadly, lack of African government external financing policies, poor donor/creditor response to African government preferences, and the problems these cause for high-quality aid flows, results in African governments finding it difficult to do the following:

- maintain debt sustainability and fund the Millennium Development Goals, without more concessional and less conditional funding,
- meet funding needs arising from external shocks, without more flexibility of resources,
- avoid expenditure cutbacks, without more predictable financing[16],
- fund key poverty reduction sectors and projects because of donor-driven priorities,
- report back to donors/creditors and the IMF on aid flows, if funds are off-budget.

The following sections describe African HIPC governments' findings of analysing donor/creditor and government policy criteria in more detail. Detailed results for the major donors and creditors are presented in the charts in Annex 3.

4.1.1 Concessionality

The concessionality policy for new external financing of most African governments can be summarised as follows:

- Seek grants in preference to loans,
- No new non-concessional borrowings (ie loans with grant element of less than 35%) as agreed with the IMF as one of conditionalities of the country's adjustment programme[17].

Table 4.1 below summarises the formal concessionality limits of selected African HIPCs.

Table 4.1: Concessionality Policies of Selected African HIPC Countries

Benin	Preference for grants and concessional loans
Burkina Faso	Preference for grants and highly concessional loans
Cameroon	35% minimum grant element
Chad	Preference for grants and concessional loans
Congo	Preference for grants
Ethiopia	Preference for grants. Minimum 35% grant element
Gambia	35% minimum grant element
Ghana	Preference for grants. Minimum 35% grant element
Guinea Bissau	35% minimum grant element
Malawi	Most concessional loans possible. 35% minimum grant element
Mali	35% minimum grant element
Mauritania	Preference for grants and highly concessional loans
Mozambique	40% minimum grant element
Niger	Preference for grants
Rwanda	50% minimum grant element
Sao Tome & Principe	35% minimum grant element
Senegal	Preference for grants and highly concessional loans
Sierra Leone	35% minimum grant element
Tanzania	Preference for grants. 50% minimum grant element
Uganda	Preference for grants. IDA comparable terms for loans
Zambia	Preference for IDA comparable loan terms

Sources: HIPC governments

[16] The macro impacts of aid shortfalls are discussed in detail in the Government of Ghana's Study of Aid Flows, Budget, Balance of Payments and Monetary Effects, 1999.

[17] This limit does not apply to PRGF loans or rescheduling credits.

In practice many African countries try to negotiate higher grant elements than the minimum 35% agreed with the IMF[18]. Interestingly, however, the IMF does not link its minimum grant element to the 50% threshold set by the United Nations for Least Developed Countries (LLDCs)[19].

In most African HIPC countries, the policy on concessionality is set out in the country's national debt strategy. However, in many cases, this policy has yet to be formally adopted and ratified by the parliamentary process. Furthermore, it is not clear that governments are always scrupulous in implementing their stated policy strictly. One country which has enshrined the minimum grant element for new borrowings in law is Tanzania in its revised Government Loans, Guarantees and Grants Act, 2003[20]. In addition, the Government of Tanzania has specified, by formal regulations, how its debt and new borrowing strategy is to be implemented institutionally, including the analysis to be done prior to contacting new financing.

Few African countries have established annual limits on new external financing, either in nominal amounts or in terms of the impact on the national debt sustainability[21], although many require that external borrowings be approved by parliamentarians. Instead the projected amount of new annual loan and grant disbursements, agreed as part of the country's IMF programme, are frequently treated as indicative benchmarks. However, as noted in Chapter 2, these projections can differ markedly from actual inflows and therefore the value of IMF projections as benchmarks is questionable.

Bilateral funds are significantly more concessional than multilateral funds, reflecting the number of donors, such as Belgium, Canada, Denmark, Ireland, Switzerland, UK and USA, providing only grants to low income African countries in recent years. While other bilateral donors, such as Germany, Japan, the Netherlands and Sweden, provide mainly grants, they have also lent money to some African nations directly, or through their export credit agencies. Despite the fact that the IMF imposes, as part of a country's PRGF programmes, a 35% minimum grant element on new borrowings by African governments, some bilateral creditors still offer more expensive export credits. Some bilateral creditors package these expensive loans with a grant, as a mixed credit, so that the grant element of the overall package is just below the 35% minimum.

The multilateral providers of grants are the European Union (EU), through the European Development Fund (EDF), and the United Nations agencies, including UNDP and UNICEF. The least concessional providers of finance, identified by African HIPC governments, are the Arab Bank for Economic Development in Africa (BADEA), European Investment Bank (EIB), IMF, Islamic Development Bank (IsDB), Kuwait, OPEC, Saudi Fund and Spain.

The main differences in African countries' experiences of donor/creditor concessionality reflect bilateral donors/creditors, such as Austria, Italy and Spain, which have provided mixed credits to some governments and highly concessional loans or grants to others. In the case of multilateral creditors, some African governments have been able to negotiate more concessional loan terms from BADEA and the IsDB than others.

Table 4.2 below summarises the concessionality and average terms of selected multilateral and bilateral creditors.

[18] For Zambia, a minimum grant element of 40% has been agreed with the IMF.

[19] See Annex 1 for discussion of the grant element calculation and concessionality thresholds.

[20] Since the grant element calculation is highly dependent on the discount rate used to calculate the present value of debt, it is also recommended that countries specify the appropriate discount rate(s) to be used, so as to preclude disputes with potential creditors about loan concessionality, and thereby be able to reject loans of dubious concessionality.

[21] The Government of Uganda is proposing to set an annual external borrowing ceiling, in nominal terms, at a level consistent with debt sustainability starting with next year's budget. The limit has been set at $203m for 2004/05, although the changes in the legislative process for doing this are on-going.

Table 4.2: Concessionality of Lending Terms of Major Multilateral and Bilateral Creditors

Creditor	Loan Terms			Grant element (%)	
	Maturity (yrs)	Grace period (yrs)	Interest rate/ service fee (%)[1]	IMF method (with CIRR rates + margins)[2]	OECD method (with 10% discount rate)
Multilateral creditors					
IDA (IDA only countries)	40	10	0.75	68.9	80.5
(blend countries)	35	10	0.75	66.4	78.6
IMF (PRGF)	10	5.5	0.50	27.9	49.1
AfDF	50	10	0.75	72.7	83.1
IFAD	40	10	0.75	68.9	80.5
BADEA	18 - 30	4 - 10	1.0 - 4.0	24.2 - 65.5	36.7 - 74.2
IsDB (least developed members)	30	10	0.75	63.4	76.3
(standard)	15 - 25	3 - 7	max 2.5%	18.2 - 39.0	41.0 - 56.0
OPEC Fund	20	5	1.0 - 2.75	36.9 - 50.4	48.0 – 59.9
Bilateral creditors					
Paris Club creditors					
Japan (LLDCs)	30	10	1.0	33.8	74.2
(low-income)	30	10	1.8	22.5	67.4
(middle income)	25	7	2.2	13.2	58.3
Germany (IDA only countries)	40	10	0.75	71.0	80.5
(other countries)	25	10	2.0	49.4	63.1
France ODA	30	10	2.0	52.9	65.7
USA ODA	40	10	2.0 - 3.0	49.2 – 59.8	60.4 – 69.3
Non-Paris Club creditors					
Kuwait Fund (average terms)[3]	22	4	3.5	25.8	43.1
Saudi Fund	20	5	2.0	37.7	53.1

1 Service fee instead of interest charge for IDA, AfDB, IsDB.
2. For loans with maturity < 15 years, discount rate is 6-month average (July-Dec 2003) currency-specific CIRR rate + margin; for loans with maturity > 15 years, it is 10-year average (1994-2003) discount rate + margin.
3. Interest rate includes 0.5% service charge

Sources: creditor websites and documents

4.1.2 Types of Assistance

Some African governments have a clearly stated preference for programme assistance[22]. In addition, African HIPC Ministers have expressed their preference for receiving more donor/creditor support in the form of programme aid, as opposed to project aid or technical assistance,[23] because programme aid allows a government to use its external resources on the basis of its own priority spending needs, as set out in its annual budget and poverty reduction strategy, whereas project aid and technical assistance are more vulnerable to being directed towards donor/creditor priority projects and recruitment of donor/creditor-country experts.

Ten African governments[24] have, in collaboration with donors and creditors, put this into practice by establishing multi-donor budget and balance of payments support programmes, whereby pooled donor/creditor funds are released on a regular basis, to support poverty reduction spending. For a discussion of the pros and cons of multi-donor budget support programmes, see the box below.

[22] The Government of Uganda has stated this policy preference in its Poverty Eradication Action Plan and other African governments have set out this policy in their national debt strategies.
[23] Declaration of the 8th HIPC Ministerial Meeting In Kigali, April 2003 available on www.dri.org.uk.
[24] Benin, Burkina Faso, Ethiopia, Ghana, Madagascar, Malawi, Mozambique, Rwanda, Tanzania and Uganda.

Multi-Donor Budget Support Programmes

Multi-donor support programmes are designed to provide more programme support directly to the government to fund its poverty reduction strategy. Participating multilateral and bilateral donors vary from country to country and have included multilateral institutions such as the African Development Bank, European Union and World Bank; and the governments of Belgium, Canada, Denmark, Finland, France, Germany, Ireland, Italy, Netherlands, Norway, Portugal, Sweden, Switzerland and the United Kingdom.

The main benefits of such programmes for governments can include:

- Common benchmarks for assessing the country's performance, based on existing criteria set out in the country's PRGF and PRS,
- Improved dialogue between donors/creditors and the government,
- Funding commitments based on government's poverty reduction strategy and MTEF budget process,
- Realistic triggers for performance-based disbursements. In the Ghana agreement there is a two-tranche disbursement mechanism with (1) a base payment of 50% of the annual allocation based on the outcome of annual IMF/PRGF review and (2) a performance linked payment of 50% of the annual allocation, linked to six specific triggers,
- Regular payment schedules agreed and followed,
- Common review processes, sometimes linked to the annual review of the government's poverty reduction strategy,
- One banking arrangement,
- Regular meetings, usually semi-annually, between government and donors/creditors, timed in order to to facilitate the budget process and minimise additional technical work, and
- Common reporting and auditing arrangements.

The potential drawbacks can include the following:

- Likelihood that all participating donors/creditors will suspend disbursements if the government's macroeconomic programme goes on-track with the IMF,
- Conditionalities for disbursements turn into the highest common multiple amongst the donors and creditors, with donor/creditor specific conditionalities being included. It can also lead to greater intrusiveness of donors/creditors in policy dialogue,
- Increases inflexibility of donors/creditors in interpreting compliance with conditionalities. There is the potential for all disbursements to be suspended unless there is donor/creditor unanimity that performance-linked triggers have been met, or for one donor/creditor to cause the suspension of all disbursements. This can be problematic for triggers related to governance and human rights issues where donors/creditors can have different interpretations on government's performance. There needs to be clear understanding between government and donors of how to react to missed indicators,
- Lack of consultation and agreement amongst donors/creditors prior to review meetings with government, leading to dispersion of donors' messages. There is a common view in Mozambique that lack of prior consultation and prior agreement of the 15 donors participating in its budget support programme means that meetings often focus on donor issues rather than dialogue with government,
- Excessive time taken to negotiate and agree the framework for joint support. In the case of Mozambique, there is a 21-page Memorandum of Understanding between the government and 15 donors, which required 19 drafts and took more than one year to finalise, and
- Heavy burdens of review processes on key government officials and donor representatives, especially if this is additional to other government-donor meetings.

In addition, African HIPC governments have indicated the following preferences with respect to the type of assistance provided by donors and creditors:

- delivering the maximum possible debt relief under the HIPC Initiative and on a bilateral basis because they regard it as a good form of budget/balance of payments support,
- minimise technical assistance, especially if not essential to implementing particular projects, in favour of increased capacity building support, and ensure sufficient budget and time allocations for the delivery of effective capacity building. Ideally governments would like to buy technical assistance from a 'common pool' of funds provided for this purpose[25], and
- reduce food aid imported from developed countries and design transparent procedures for the purchase of all food on local or regional markets, where available.

According to African HIPC governments, a higher proportion of programme aid is provided by multilateral donors and creditors than by bilateral ones, although the difference is not large, in

[25] For more details, see Government of Uganda's Poverty Eradication Action Plan, Volume 3.

part reflecting the growing number of bilateral donors/creditors participating in multi donor budget/balance of payments support programmes. The IMF scores well on this factor as all its lending to low income African countries, through its Poverty Reduction and Growth Facility (PRGF), is programme support. The AfDB, EU, and IDA also provide above average amounts of programme assistance, reflecting policy moves to increase this type of support in recent years. For bilateral sources, Denmark, Ireland, Netherlands, Sweden, Switzerland and UK provide the most programme assistance, followed by Canada, France, and Germany, reflecting national policies to provide more programme resources.

It is the view of African HIPC governments that the donors and creditors providing the least programme assistance, and hence the most project aid and/or technical assistance, include BADEA, EIB, IFAD, IsDB, OPEC and the UN agencies amongst multilateral donors/creditors and Austria, China (PR), Italy, Japan and Spain amongst the bilateral donors/creditors. As the role of the UN agencies is primarily technical rather than financing, much of their aid is delivered in the form of technical assistance, through for example UNCTAD and UNDP, or the direct provision of services, such as UNICEF's programmes for immunisation of children.

4.1.3 Channels of Assistance

African governments maintain a preference for donor/creditor aid to be directed via the budget, rather than going directly to line ministries or other agencies, although this preference may not be stated formally. This policy can be strengthened by shifting towards more programme aid and by ensuring that the Ministry of Finance is fully conversant with all prospective new financing proposals and the Minister of Finance has the sole authority to contract loans and grants on behalf of government. For example, in Tanzania, line ministries are required by law to submit a request or proposal to acquire any loan or grant quarterly to the National Committee responsible for advising the Minister of Finance whether the loan or grant can be contracted, thereby ensuring the Ministry of Finance is fully informed of all new loans and grants contracted. Governments would also like greater integration of all food and emergency assistance into the budget preparation process.

Multilateral sources are scored more highly by African HIPC governments on this factor, reflecting their policies of dealing directly with the central government. Hence more of their aid is disbursed directly to the government's budget rather than to line ministries or other agencies, with the exception of the UN agencies, which frequently provide funds directly to line ministries or other agencies. IMF funds are disbursed directly to the central bank. Bilateral donors/creditors do not score as well and Canada, China (PR), Japan and Switzerland are the donors/creditors providing the most funds off-budget, whereas Kuwait, Netherlands, Saudi Fund, Sweden and UK provide the most funds on-budget. In terms of cross-country experiences of channelling assistance on or off-budget, the largest variation is shown by China (PR), EU, EIB, Germany, Japan and the UN agencies.

4.1.4 Sectors and Projects

African government's Poverty Reduction Strategies set out clearly their policies for priority sectors and projects, and so there should be little excuse for donors/creditors to insist upon funding their own priorities rather than governments. However, in some instances, donors and creditors have been accused of influencing governments to ensure that the donor/creditor priority sectors are also those of the PRSP.

Although donors/creditors acknowledge government priorities in principle, there are still difficulties with some donors/creditors earmarking (1) the budget support provided to specific sectors, thereby reducing inter-sectoral flexibility of funding[26] and (2) the sector support provided to sub-sectors or projects, thereby reducing intra-sectoral flexibility. Donors/creditors sometimes use earmarking in order to be able to participate in sectoral reviews and thereby impose additional conditionalities through this process[27]. Sectoral and sub-sectoral coordination and review processes can then become very onerous and time-consuming for donors and government alike – as, for example, with the 23 groups of this type in Senegal .

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[26] For example, the EU has both non-target and target budget support, the latter to be utilised only for specific lines of the national budget, although its policy is to move toward the former.
[27] See the Government of Uganda's Poverty Eradication Action Plan, Volume 3, December 2001.

While some donors/creditors have a policy of supporting government priority sectors in principle, their aid is not always directed towards poverty reducing projects within these sectors. Instead, it remains directed towards donor-driven projects. For example, one European donor provided a facility to fund hospital construction in Ghana, which conformed with the government's priority sectors, but did not meet the government's full project requirements as it was built without an operating theatre. Some donors continue to intervene very actively to insist that their projects or programmes be included in government priorities when they might otherwise have been omitted. There is also a reluctance by donors and creditors to organise or to classify their country programmes on the basis of the African country's PRS classifications and instead they insist on retaining their own, which can be complicating.

Some donors/creditors will not fund all government sectoral priorities but instead they want to concentrate funding on few sectors where they feel their resources will be most effectively and efficiently used. For example, the Dutch government is restricting the number of sectors it supports in each partner country to two or at most three.

While many donors/creditors are fully prepared to provide resources to meet African government priority spending needs on poverty reduction, many African governments also see the development of national infrastructure as a priority. Under NEPAD, sub-regional and continental infrastructure developments in transport and telecommunications are set out as priority areas for Africa as a whole and there is a potential conflict between these priorities and donor/creditor priorities of funding only poverty reduction expenditures.

According to African HIPC governments, multilateral donors/creditors are better than bilateral sources at providing resources to meet government priorities. Above average multilateral performers are IDA, AfDB, IFAD, EU and the UN agencies, with EIB funding being the least likely for financing government priorities. Ireland, Netherlands and UK are the best bilateral supporters of government priorities, in part reflecting their policies of providing high levels of programme aid, which enables the government to finance its priorities directly through the budget. Austria, China (PR), France, Italy and Kuwait are the least likely to support government priorities. The main differences in African country experiences is amongst those donors/creditors which are least likely to provide support for government priority sectors.

4.1.5 Flexibility

Lack of donor/creditor flexibility to provide additional resources to meet external shocks or to respond rapidly to new government priorities is the most problematic policy area identified by African HIPC governments. Multilateral sources are seen as slightly less flexible than bilateral sources. While many multilateral agencies, such as IDA and EDF, use a formula of some type for allocating aid resources to countries for a specific time period, such as 3 years, some agencies have limited scope for adjusting this allocation during this period, thereby reducing the flexibility of funding, albeit enhancing its predictability. Others, however, such as the EU, are able to top up country allocations to meet unforeseen shocks, but African governments have not had very positive experiences so far with the new EU FLEX system for such funding.

African governments tend not to have formal policies on aid flexibility. However HIPC Ministers[28] have advocated for much greater contingency financing, to enable them to access concessional external resources to meet budget and/or balance payments difficulties arising due to shocks. Since many of these 'shocks' are predictable and recurrent (eg droughts in Malawi), this can be done by inserting additional contingency tranches in donor/creditor budget support grants and loans, in order to offset any foreseeable shocks. The current international facilities, such as the IMF's Compensatory Financing Facility and the EU's FLEX instrument, designed to provide additional resources to assist countries cope with external shocks, have been inadequate and the main respondents in such circumstances have tended to be European bilateral donors/creditors with more flexible aid policies.[29]

Some bilateral donors, notably the Netherlands and the UK, have systems to provide flexibility. In the UK this includes a contingency allowance in each country's aid budget allocation, the possibility of viring funds between programmes, and an overall contingency reserve, which can

[28] See HIPC CBP Newsletter Issue 17, 3rd Quarter 2003 on www.dri.org.uk.
[29] See separate paper, *Overcoming Africa's "Shocks"*, for further discussion of this issue.

be used for extra budget support or emergency aid[30]. However, African governments rarely have information on such facilities and therefore are not in a position to request this support.

The most flexible bilateral sources are Denmark, Ireland, Netherlands, Sweden and UK, with Canada, Italy, Kuwait, Saudi Fund, Switzerland and USA being the least flexible, according to African HIPC governments. Variations in bilateral donor/creditor flexibility between African countries was most notable in the case of Belgium, China (PR), Denmark, France, Germany, Netherlands, Spain and Sweden, in that they have been more flexible in some countries and significantly less so in others. The EU is the most flexible multilateral donor/creditor whereas the BADEA, EIB, IFAD and the IsDB are the least flexible. Countries' experiences of flexibility of the BADEA and OPEC, in particular, have shown the most variation, with some recipient countries finding both donors/creditors considerably more flexible than others.

4.1.6 Predictability

Although few African governments have a formal policy on predictability, they prefer multi-year donor/creditor pledges of external aid resources which can be factored into national Medium-Term Expenditure Frameworks (MTEFs) and budget planning processes. While many donors/creditors do provide multi-year pledges at Consultative Group or Round Table meetings, governments rarely press all donors/creditors for this or for multi-year disbursement projections.

While donors/creditors are very good at making multi-year pledges, the ability of some to fulfil these pledges with actual disbursements is risible (due largely to the cumbersome procedures described in 4.2 below). As a result, some donors/creditors have huge pipelines of committed but undisbursed funds[31]. In order to improve the predictability of donor/creditor disbursement projections, some African governments, such as the Government of Uganda, are now discounting projected donor and creditor inflows to reflect more realistic disbursement levels, based on past trends.

According to African governments, multilateral donors/creditors are marginally better at making and honouring multi-year pledges, with IDA and the IMF being the best performers, and the EU and IsDB being the worst, although the differences amongst multilateral scores is relatively small. The IMF, IDA and AfDB all have multi-year programmes with countries, which provide medium-term projections of both resource commitments and annual disbursements. The experience of African countries on specific donor/creditor predictability differs quite markedly, notably for BADEA, EU, OPEC and the UN agencies, which for some countries scored quite highly on predictability whereas for others they received a low score.

For bilateral donors/creditors, there is a greater range in predictability scores, with Ireland, Netherlands, Sweden and UK being the most predictable, and Italy, Saudi Fund and Switzerland being the worst performers. In terms of cross-country experiences of donor/creditor predictability, the largest variations occur with Austria, France, Italy and Japan.

The budgetary systems of some bilateral donors, such as the UK, enable them to pledge funds on a multi-year basis, particularly for programme aid. However, for other bilateral donors, the constraints of their national budget process means they can only make pledges of programme aid on an annual basis, usually at the beginning of the government financial year.

4.1.7 Conditionality

African governments have indicated that they want to work with donors/creditors to minimise the aggregate number of performance conditionalities, including those under PRGF programmes agreed with the IMF[32] and the PRSP. In addition African governments are keen to discourage the bilateral performance conditionalities over and above those already agreed as part of PRGF and PRSP processes, as well as cross-conditionalities, both formal and informal, between donors and creditors. The latter can lead to one donor deciding to suspend disbursements for reasons of its own, often on an interpretation of political governance issues, and others following suit although there is no formal breaching of their own bilateral agreements.

[30] See DFID Strategic Review of Resource Allocation Priorities, January 2003.
[31] Although the volume of unspent EU project funds, which effectively doubled between 1993-2000, has stabilised, it still stands at about €20 billion.
[32] On average, African countries' PRGF agreements contain 11 conditionalities.

In the view of African HIPC governments, the strictness shown by donors and creditors in interpreting PRGF, PRSP and other conditionalities varies. Some donors and creditors are more willing than others to be flexible so as to minimise suspension of aid flows. This is particularly important in the case of multi-donor support programmes where a requirement of unanimity in assessment of progress can lead to suspension of budget support, with disastrous economic consequences. Therefore, African governments would prefer to retain donor/creditor freedom to respond individually to performance conditionalities by, for example, asking donors to state explicitly what share of their disbursements is to be linked to specific performance criteria, enabling partial disbursements to continue if there are performance shortfalls.

Overall multilateral donors and creditors provide more conditional funds, than do bilateral donors and creditors, and therefore achieved a lower score in African governments' analyses. Multilateral creditor conditionalities tend to be both more numerous and more strictly enforced than those of their bilateral counterparts. IFAD, OPEC and the UN agencies are seen as the most lenient in this regard, whereas the AfDB is considered the most problematic in terms of compliance and the resulting delays in disbursements. In order to control the proliferation of donor/creditor conditionalities, a number of multilateral organisations, such as IDA, IMF and AfDB, are taking steps to align their country assistance programmes more with the priorities of the country's poverty reduction strategy, and to streamline conditionalities, but African governments do not yet perceive these as having a major impact. The largest cross-country variation in the enforcement and delays arising from conditionalities by multilateral creditors comes from BADEA and the EU.

Some bilateral funders, notably China (PR), have fewer conditions and compliance is not interpreted with such stringency, so disbursements are rarely suspended even if the country is off-track with the IMF. Other bilaterals which take a more relaxed view of conditionalities, are seen as Belgium, Denmark, Germany, Ireland, Kuwait, Netherlands, Sweden, Switzerland and UK. On the other hand, Austria, Canada, France, Italy, Japan, Saudi Fund, Spain and USA have an above average burden, including many bilateral conditions. African countries' experiences of bilateral conditions show the largest variation for France, Italy and Japan.

4.1.8 Policy Dialogue

In most African countries formal policy dialogue with donors and creditors is conducted at Consultative Group or Round Table meetings held every few years. However, this is not usually sufficient and so some African governments have instituted more regular, quarterly or semi-annual, meetings with donors and creditors through, for example, the mini-Consultative Group process on Ghana, the Donor Assistance Group in Ethiopia and G14+ World Bank Group in Mozambique. Moreover, regular policy dialogue and meetings with donors/creditors have been built into the multi-donor budget support programmes, which enhance this process. On the other hand, less advanced African governments have virtually no in-country fora for policy dialogue with donors, often leaving such dialogue to be led by and conducted among donors, even though they perceive this as a highly negative circumstance which undermines their ability to inform donors accurately about their policies.

In general African HIPC governments view the donors/creditors of OECD countries and major multilateral institutions as being the most engaged in policy dialogue, with a strong correlation between engagement and those donors providing budget support. Policy dialogue is therefore much more active and successful in promoting stable aid flows in countries with large numbers of donors providing budget support.

4.2 DONOR/CREDITOR AND GOVERNMENT PROCEDURES

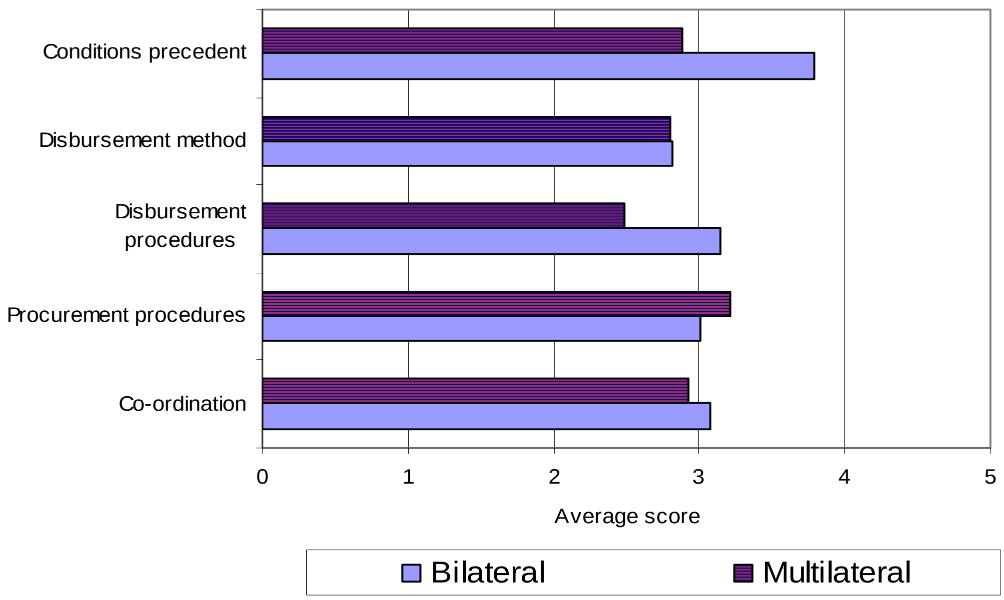
In recent years there has been considerable international impetus to improve aid delivery through the harmonisation of disbursement and procurement procedures. This has involved initiatives for better co-ordination and streamlining of procedures amongst donors and creditors themselves as well as between donors/creditors and African governments. For example, the introduction of multi-donor budget support programmes has led to a commonality of donor/creditor procedures for programme assistance, which is welcomed by African governments. However, there remain major problems for African government compliance with donor/creditor procedures outside of the multi-donor budget support programmes.

Although a number of African governments have been making good progress in establishing their own procedures, particularly for procurement, donors/creditors have shown a reluctance to adopt governments' procedures or harmonise their procedures with those of governments. The main issues identified by African governments with regard to disbursement and procurement procedures and the impact these can have on delivery of aid flows are set out below.

The results of the analysis of donor/creditor procedures and their impact on disbursement delays are summarised in Chart 4.2. The main factors causing disbursement delays are:

- Cumbersome and time-consuming disbursement procedures, such as the provision of matching fund requirements and donor/creditor bureaucracy,
- Over-complex disbursement methods, such as reimbursement claims,
- Burdensome procurement procedures, including tying of resources and the time involved in conducting and vetting bidding and tendering procedures,
- Difficulties in fulfilling conditions precedent so loan and grant disbursements can commence.

Chart 4.2: Multilateral and Bilateral Donor/Creditor Procedures



Detailed results for the major donors and creditors are presented in the charts in Annex 3.

4.2.1 Conditions Precedent

African governments' preference is for the minimum number and complexity of conditions precedent so funds can be disbursed as quickly as possible after a loan or grant has been signed. They find that conditions precedent relating to governance, human rights and structural issues are often the most difficult and time-consuming to comply with. Furthermore, they maintain that such conditions precedent should be aligned with triggers or benchmarks in PRGF and PRS programmes and not additional to them. The other issues identified as causing delays in fulfilling the conditions precedent are as follows:

- Lack of institutional capacity to monitor their implementation and to inform donors/creditors of their fulfilment on a timely basis,
- Poor institutional co-ordination within government resulting in delays when, for example, there are problems of information flows between a line ministry responsible for implementing a specific condition and the external resources unit of the Ministry of Finance responsible for liaising with donors/creditors,

- In many cases, departments/units responsible for raising external resources are often only interested in and rewarded for raising new loans and grants and not in ensuring their timely implementation,
- Lack of well-qualified and motivated staff can also be a problem.

One of the most common difficulties African HIPC governments face, in fulfilling conditions precedent is the significant time required to obtain any necessary parliamentary approval of loan agreements[33]. In the worst cases, the bureaucratic and parliamentary procedures for this process can take up to a year, while delays of 6 to 9 months are common. In Mali and Benin, for example, if parliament is not in session this can add 3 months to obtaining approval. In addition, these governments need to seek a legal opinion by the Supreme Court for each agreement, which can result in 6 to 12 month delays. In Burkina Faso, there is also the requirement that each decision be published in an official government journal of record.

Almost all donors/creditors require a legal opinion before allowing loan/grant disbursements to commence. However, multilateral donors/creditors tend to have considerably more and complex conditions precedent, sometimes involving structural/administrative conditions (such as setting up a separate project monitoring unit) or legislative changes (for example introducing new legislation). On the basis of African HIPC governments' analyses, the AfDB and EU are the most problematic in this regard, whereas BADEA, EIB, IMF, OPEC and the UN agencies have the fewest and least cumbersome conditions precedent amongst multilateral donors/creditors. The AfDB, for example, has acknowledged that the multiplicity of loan conditions and the inability of many governments to fulfil them on time is the cause of delays and hence it has taken steps to reduce these delays (see Box). At the end of 2003, 29% of AfDB loan approvals between 1988 and 2003 were not effective and disbursements had yet to commence[34].

AfDB's Plan to Reduce Disbursement Delays[35]

The AfDB anticipates that its new Action Plan to improve operations will diminish disbursement delays by reducing in the time take for:

- Loan signatures by borrowers from almost 1 year to less than 6 months,
- Loan signature to effectiveness, by fulfilling the conditions precedent, from more than 12 months to below 6 months,
- Processing disbursement requests from over 15 days to 10 days,
- Procurement time from 13-20 months to 6-8 months.

The practice of establishing cross-financing conditions amongst the donors/creditors jointly funding a specific project can also be problematic as the recipient has to fulfil the conditions of all donors/creditors before any disbursements can take place. There can also be disbursement delays because of the cumbersome nature of donors/creditors procedures for monitoring a country's progress in complying with conditions precedent.

Bilateral donors/creditor have, on average, fewer and less-consuming conditions precedent and hence are scored more highly by African HIPC governments. Belgium, Canada, Denmark, Germany, Netherlands, Switzerland and UK score best in this regard, whereas Austria, China (PR), Italy, Saudi Fund and Spain have the most difficult and time-consuming conditions precedent amongst bilateral donors/creditors. In terms of African country experiences, AfDB, BADEA IDA, IsDB and France and Italy are noted as having the greatest variations in treatment amongst recipients and borrowers.

4.2.2 Disbursement Methods

African governments prefer upfront direct cash disbursements as this provides resources immediately to the recipient, whereas disbursement through reimbursement claims can result in lengthy delays because of the time required to compile all the information and documentation required for submission of a claim and the time required by donors/creditors to process claims.

[33] Parliamentary approval may be required for both loans and grants. However it is more common to have to obtain approvals for loans, as loans impose a liability on government whereas grants do not.
[34] See AfDB, Action Plan to Improve Implementation of ADF Operations, May 2004.
[35] *Ibid*.

African governments regard disbursements via direct payment by donors/creditors to foreign suppliers as highly problematic, as they are often not informed of the actual disbursements or amounts.[36] This is especially true for technical assistance provided by expatriate experts or consultants, who are hired, contracted and paid by the donor/creditor with little or not involvement of the recipient government, which may not even be provided with data on the amounts spent. Since much of food/emergency aid is provided as aid-in-kind, through the shipment of food or other goods directly from the donor/creditor country or purchased from a third country, disbursement data for this type of aid may not be readily available to African governments. In addition, this disbursement method can preclude the possibility of using donor funds to purchase goods or service nationally, when available, is limited.

African governments have identified complex disbursement methods of both multilateral and bilateral donors and creditors as causing major disbursement delays. The disbursement methods of the IMF, IFAD, UN agencies, Belgium, Denmark, and UK are the least problematic for governments, whereas those of AfDB, BADEA, IsDB, OPEC, Saudi Fund and Spain result in the longest disbursement delays. Overall the best performers tend to be those providing mainly programme aid which is often disbursed through direct cash payments to the government consolidated fund, while the worst performers tend to be those providing mainly project aid. There does not appear to be any significant variation of disbursement methods across different African countries, with the exception of Canada, EU, Japan and the UN agencies.

4.2.3 Disbursement Procedures

African governments have frequently expressed their dislike of donor/creditor requirements to provide matching funds. Donor/creditor insistence on matching funds causes disbursements delays because firstly, governments need to provide for matching funds in their annual budgets, and if the current year is missed, then this means waiting for the next budget cycle. There is also an issue in some countries (such as Ethiopia and Ghana) of line ministries or district authorities not including matching fund provisions in their annual budget submissions. Secondly, even when budget provisions for matching funds are made, governments are not always able to comply quickly to release the funds in a timely manner. This is particularly the case for countries with cash budgeting, when there are shortfalls in anticipated revenue receipts. Delays can also arise because of bureaucratic treasury procedures and/or lack of information flows between the treasury and implementing line ministries or agencies.

Other compliance issues which African governments have identified as being problematic and leading to significant disbursement delays can include the following:

- the insistence by donors/creditors for tax exemptions being granted on donor/creditor funded imports of goods and services,
- the complexity and bureaucracy for processing disbursement notices,
- the need to conduct review and/or audit missions and project inspection/monitoring before further disbursements can take place,
- the setting up of banking arrangements and the organisation of appropriate signatories. While programme aid is usually disbursed directly to the government's main bank account, donors and creditors often require the setting up separate bank accounts for each project which can lead to delays because of form filling and getting appropriate signatories for the account. If, for example, the Minister of Finance is required to be a signatory for the account, disbursement delays can arise if it takes time to get his/her signature for each release of funds.

In addition, the timing of disbursements can be heavily influenced by the donor/creditor financial year, with approvals and release of funds at the beginning of the financial year being slower than towards the end of the financial year when donors/creditors want to close their annual accounts, rather than being aligned with African government budget cycles.

While African governments have institutional procedures for monitoring and managing donor/creditor disbursements, disbursement delays can arise because these procedures are not well documented. Shortages of well trained and motivated staff are also an issue. Disbursements delays because of weak national capacity to monitor projects and programmes

[36] The Government of Ghana conducts regular surveys of all its donors and creditors to ascertain data on all disbursements.

in a timely manner, for example, desk officers may not be well versed in donor/creditor procedures and so compliance with procedures may depend on regular donor/creditor missions.

For African HIPC governments, multilateral donor/creditor disbursement procedures are on average more numerous and cumbersome to fulfil than those of bilateral donors/creditors and hence they achieve a lower score. The AfDB and IsDB are the worst performers with the complexity of disbursement procedures leading to the longest disbursement delays[37]. For bilateral donors/creditors, Austria, Italy, Saudi Fund and Spain have procedures causing the longest disbursement delays, whereas Denmark and Switzerland have the fewest and least cumbersome procedures. The donors/creditors, which are the least consistent in the way they implement disbursement procedures across African HIPC countries, are BADEA, EU, France, Germany, Japan and Saudi Fund.

4.2.4 Procurement Procedures

In principle African governments want to establish their own procurement procedures and to have all donors/creditors agree to adopt them, thereby eliminating the multiplicity of donor/creditor procedures they are currently having to work with. A number of African HIPC governments, such as Ethiopia, Mauritania and Uganda, are taking the lead in developing national procurements procedures, and others are moving forward as part of the international harmonisation initiatives. However, some donors/creditors are still unwilling to adopt national procurement procedures, and continue to insist on using their own procedures.

The main problems of donor/creditor procurement procedures, identified by African HIPC governments as causing disbursement delays, include the following:

- tying aid to the purchase of goods and services from the donor/creditor country (see the Box below) . Although many donors/creditors may have a formal policy of providing untied assistance, in practice it can be informally 'tied' by, for example, the placing of advertisements for the provision of goods in the donor country press or posting notices of consultancy contracts only on the embassy notice boards. The use of donor-appointed procurement agents can also influence procurement decisions.
- complexity and bureaucracy of conducting and vetting bidding and tendering procedures and the time required to implement these,
- time taken to process customs clearances of imported goods and to process customs tax exemptions requested by donors and creditors. A number of countries are considering removing the customs tax exemption status for donor/creditor funded imports or to request donors/creditors to classify the amount of tax exemptions granted as matching funds contribution by government,
- lack of transparency of procurement when it comes to technical assistance. Often governments are not consulted a priori about the hiring of technical experts and expatriate staff for projects which involve government.
- lack of national capacity – institutional and staffing – to implement the donor/creditor procedures effectively and in a timely manner. In some cases, this is more problematic at the line ministry or implementing agency level, where officials are not fully familiar with their implementation. In addition, commissions or panels set up to award contracts are often not adequately staffed and meetings are infrequent or sometimes only on an ad hoc basis, all of which can lead to delays.

Since programme aid is mainly provided directly to governments for budget expenditures and unconstrained in procurement terms, bilateral and multilateral donors/creditors providing this type of aid are scored more highly by African HIPC governments. However, for those donors/creditors providing primarily project aid and technical assistance, their procurement procedures and practices can cause significant disbursement delays. Amongst multilateral donors/creditors, BADEA, EU, IFAD and IsDB have the most cumbersome and slow procurement procedures. Amongst bilateral donors/creditors, procurement procedures of Austria, the Saudi Fund and Spain cause the most disbursement delays. The donors/creditors identified as being the least consistent in the way they implement procurement procedures across African HIPC countries are AfDB, Canada, EU, and France.

[37] The AfDB disbursement ratio (disbursements/undisbursed balance) has varied between 12.9% and 25.5% in the period 1996-2002 and slipped to 12.3% in 2003, reflecting an increase in the undisbursed balance.

Overall bilateral procurement procedures cause more delays than do those of multilaterals, in part because bilateral donors/creditors are more likely to tie aid to the purchase of the donor/creditor country goods and services, despite recent progress in untying (see Chapter 2).[38]

Some donors/creditors have made major efforts to streamline their procurement procedures in recent years. For example, the EU has reduced its number of different tendering procedures from 46 to 8 since 2000. However elsewhere delays are still considerable despite revisions to procedures. In the case of the AfDB, the 13 and 20 months required from the commencement of the preparation of bids, to signature and submission of signed contracts is in part because of the lack of sufficient procurement experts.

Impact of Tying Aid

Table 4.2 illustrates the level of tied aid commitments of OECD donors/creditors to all developing countries in 2002. Those still tying more than 30% of commitments in 2002 were Australia, Austria, Canada, Greece, Portugal and Spain, although Canada has recently changed its policy and agreed to implement the OECD-DAC agreement.

If donors/creditors persist with a policy of tying procurements, it can reduce the value of aid by anything up to 70% compared with procurement in the recipient country and up to 25%-40% compared with cheaper external sources. Tying of technical assistance to the use of expatriate staff or experts from the donor/creditor country is highly prevalent, and can significantly reduce the value for money of this assistance, where expatriate salaries can push up costs by a factor of 10.

Table 4.2 Share of Tied ODA, 2002*

Australia	43.3	Luxembourg	3.3
Austria	31.0	Netherlands	11.4
Belgium	61.0	New Zealand	24.0
Canada	38.6	Norway	0.9
Denmark	17.9	Portugal	66.9
Finland	17.5	Spain	40.1
France	8.5	Sweden	21.5
Germany	13.4	Switzerland	4.9
Greece	86.1	United Kingdom	0.0
Ireland	0.0	United Stated	na
Italy	61.8	**DAC Countries -Total**	**15.2**
Japan	17.2		

*Tied and partially tied commitments, excluding technical co-operation. For Ireland and UK share of gross disbursements. 2001 data for Belgium, Italy, Luxembourg
Na – no data reported to OECD
Source: OECD DAC

4.2.5 Co-ordination

International efforts towards harmonising disbursement and procurement procedures amongst donors/creditors and aligning these more closely with African governments' own procedures, for example, through multi-donor budget support programmes, have improved co-ordination. While these initiatives are generally welcomed by African governments, they are also seen as focusing more on the harmonisation of procedures amongst donors and creditors than on aligning donors/creditors behind African government procedures. In addition, donors are seen to be more concerned with harmonisation of procedures, than on aligning their policies with those of African governments' poverty reduction strategies.

Overall African HIPC governments score bilateral donors and creditors slightly higher than multilateral donors/creditors on co-ordination. The best performers tend to be those donors/creditors participating in multi-donor budget support programmes, such as IDA, AfDB and the EU amongst the multilateral donors/creditors (although IFAD and the UN agencies also achieve above average scores), and Belgium, Denmark, Ireland, Netherlands, Switzerland and the UK amongst the bilateral donors/creditors. In terms of cross-country experiences of donor/creditor co-ordination, the most significant variations were noted for Canada, EU, France, OPEC and UN agencies.

[38] In 2001, the G8 donors endorsed the OECD-DAC agreement to provide untied aid, except for free-standing technical co-operation and food aid, to Least-Developed Countries, and to promote local and regional procurement.

4.2.6 Amount and Diversity of Assistance

Analysing the proportion of aid received from each donor and creditor provides African governments with an indication of their dependency on particular donors and the split between multilateral and bilateral sources. For example, IDA is by far the largest of Ethiopia's 28 major multilateral and bilateral donors/creditors, providing an average of 44% of loan and grant disbursements in the last 3 years. The case of Ethiopia demonstrates that simply having a large number of donors/creditors does not necessarily indicate less dependence on one or two individual donors/creditors. Other countries with large numbers of donors/creditors include Ghana, Mozambique and Tanzania, whereas West African states such as Burkina Faso, Mali and Mauritania have far fewer donors/creditors. The range of the number of donors/creditors in African countries varies between 8 and 65. In general, Francophone and Lusophone African countries have much fewer donors than their Anglophone counterparts, even when they have a comparable level of policy performance. There is an urgent need to provide better-performing countries in these groups with more diversity of donors in order to make them less vulnerable to suspension of aid by one key donor.

The benefits to government of having a large number of donors/creditors can include:

- Disbursement shortfalls or withdrawal by one donor will have less impact,
- More flexibility and predictability of total inflows due to less dependence on any one donor,
- Donors can be more encouraged to pursue MDBS and other harmonisation initiatives,
- Negative changes in individual donor policies and procedures have less impact overall, and
- Presence of more donors provides more opportunities to highlight individual best practices.

The drawbacks for government of having a large number of donors/creditors can include:

- Managing a multiplicity of smaller donor/creditor funded projects,
- Dealing with many different donor/creditor procedures for disbursements, procurement, financial reporting, project and programme monitoring and auditing,
- Difficulties in co-ordinating multiple and over-lapping donor meetings and review missions.

Overall, African governments view as desirable a reasonable degree of diversification, especially where this allows them to attract donors which have the best policies and procedures, but not excessive levels where it diverts government from economic management.

4.2.7 Export Credits and NGO Assistance

Many African countries receive significant amounts of funding from NGOs, such as Oxfam, Save the Children, the new Global Fund and other civil society sources, including religious organisations. In addition, some central government or other agencies borrow commercially, using export credits, to fund, for example, the national airline. The HIPC CBP methodology can also be used to analyse and rank these sources of funding.

In general terms, NGO funding is highly concessional, being primarily grants, with few conditionalities. It often supports government priority sectors but not necessarily priority projects. However, it tends to be channelled off-budget, inflexible and not very predictable. In terms of procedures it has few conditions precedent and less cumbersome disbursement procedures, but it is often tied with payment often made direct to suppliers. African governments see the highest quality NGO assistance as comparable to the highest quality bilateral/multilateral aid, but indicate that there is a huge variation so that a lot of NGO assistance scores very low.

Although export credit and other commercial financing is non-concessional and often off-budget, and frequently does not fund priority PRSP sectors or projects, it is usually quick disbursing, with few conditionalities. In procedural terms, it often has more conditions precedent, disbursement usually takes place direct to the supplier, and procurement is almost always tied. In general, African governments rank such assistance well below that of aid donors/lenders and NGOs.

4.3 Prioritising Donors And Creditors By African Governments

On the basis of the analysis above of donor/creditor policies and procedures, African governments are able, using the HIPC CBP methodology, to rank and prioritise their donors and creditors on the basis of the quality of aid. Table 4.4 below summarises the donor/creditor ranking of 13 HIPCs, with donors and creditors being classified as having an above average scores on policy and procedures and those with below average scores. This ranking takes into account all the quality of aid policy and procedural factors discussed in detail above[39].

Some donors/creditors are consistently scored as above or below average by all the HIPCs. For example, BADEA and the EIB are ranked as having below average scores by all HIPCs whereas some donors/creditors, such as the ADF and Japan, are ranked as having scores above average by some countries and below average by other countries, reflecting the cross-country differences in how policies and procedures are implemented.

Table 4.4: Overall Ranking of Donors and Creditors by Selected HIPCs

	Above average scores on policies and procedures	Below average scores on policies and procedures
Multilateral		
	European Union (EDF) IDA IFAD IMF UN agencies	African Development Fund BADEA European Investment Bank Islamic Development Bank Nordic Fund (NDF) OPEC West African Development Bank (BOAD)
Bilateral		
	Belgium Canada Denmark Finland Germany Ireland Luxembourg Netherlands Norway Sweden United Kingdom USA	Austria China (PR) France India Italy Japan Kuwait Fund Libya Portugal Saudi Fund South Korea Spain Switzerland

Donors/creditors are listed in alphabetic order, within each classification.

The main outcomes and areas for improvement in aid policy and procedures for the major multilateral donors and creditors are as follows:

- IDA's aid policies and procedures result in an above average score as it provides highly concessional, predictable, on-budget aid in support of government priority sectors and projects, although it is too tied up in conditionalities. Although IDA is seen as providing more flexible aid than many other multilaterals, there is a need for enhanced flexibility.
- AfDB achieved a below average score reflecting the need to reduce the burden of policy conditionalities and significantly improve almost all aspects of its procedures, on which it was assessed as well below average because these are far too cumbersome.
- IMF PRGF resources are ranked high for being predictable, flexible and having the least burdensome procedures. However, they are also seen as the least concessional and highly conditional.
- EDF policies score well with the exception of predictability, but on procedures it was ranked well below average. There is an urgent need to reduce the burden of conditions precedent and improve its disbursement and procurement procedures.
- UN agencies provide highly concessional aid in support of government priority sectors and projects, but too much is provided as project aid or technical assistance,

[39] Ranking is done on the basis of the average score for all bilateral and multilateral creditors.

directly to line ministries, rather than as programme support to the budget. Better predictability of resources and less cumbersome disbursement procedures would improve overall delivery.

The main outcomes and areas for improvement in aid policy and procedures for the G7 bilateral donors and creditors are as follows:

- Canada provides highly concessional resources mainly in support of government priorities but its aid tends to be less flexible, less predictable and channelled off-budget than other bilateral donors. Changes in the method by which its aid is disbursed and better co-ordination with governments and other donors/creditors would enhance Canadian delivery.
- France achieved a below average score because its aid is less concessional, less focused on government priority sectors and projects, less flexible and with more conditionalities. In addition, it ranked below average on disbursement methods and procurement procedures.
- Germany's aid policies are ranked above average with the exception of its tendency to channel funds off-budget. In terms of procedures, German aid delivery is good overall, although there is a need to improve the method of aid disbursement.
- Italian aid scores very low, because it is viewed as being less concessional, less flexible, less predictable, delivered more in the form of project aid and technical assistance support and directed more towards Italian than government priorities. In procedural terms, there is a need to improve almost all aspects of its aid delivery.
- Japan would benefit in policy terms by switching to more flexible programme support, provided on-budget. Less cumbersome and time-consuming disbursement and procurement procedures would also lead to improved aid delivery.
- United Kingdom is assessed by African governments as having among the best aid in policy and procedural terms, along with Ireland, Netherlands, Switzerland and the Nordics.
- United States aid is highly concessional but tends to be less flexible, less predictable, with more conditionalities and provided more in projects and technical assistance. Less cumbersome and time-consuming disbursement procedures would enhance its aid delivery.

4.4 COMPARISON WITH OUTCOMES OF OTHER INITIATIVES

The compliance difficulties and constraints identified by African HIPC governments, using the HIPC CBP methodology, are similar to those of **OECD DAC**'s Needs Assessment Survey, included in its report on *Harmonising Donors Practices for Effective Aid Delivery*, and in some instances go further in highlighting the practical problems countries face such as excessive demand on national officials' time and lack of information and data. According to the OECD survey, the most burdensome donor practices to effective aid delivery are:[40]

- donor driven priorities and systems. This covers the pressure brought to bear on countries policies and procedures; and donor/creditor aid management systems designed mainly to meet donor, not African country, needs and priorities,
- difficulties with donor procedures. In particular the survey highlights procurement and technical assistance as the two main areas challenging countries, as well as problems arising from frequent changes in donor/creditor policies, systems and staff,
- uncoordinated donor practices. This leads to diverse and multiple requests on government to meet different donor/creditor accountability requirements,
- excessive time demands, including multiple uncoordinated donor missions at short notice,
- delays in disbursements, which include those arising from bureaucratic procedures, complications related to pooled funding arrangements, and issues of interpretation of conditionality slippages.
- lack of information, which includes lack of transparency on financial information, and
- demands beyond national capacity, including donor demands for public sector reform and excessive expectations of information technology.

[40] The main findings and initiative suggestions are tabulated on frequency of mention by the countries surveyed. For more details see the OECD's *Harmonising Donor Practices for Effective Aid Delivery* 2003.

In addition to highlighting the key problems, the OECD DAC survey also summarises the key initiatives for improving the effectiveness of development assistance identified by developing countries, which mirror some of the areas of action set out in Chapter 5, as follows:

- Simply and harmonise procedures and systems,
- Align procedures on countries' systems,
- Share information,
- Untie aid,
- Respect national priorities and strategies,
- Strengthen national capacities,
- Use a co-ordination structure, and
- Rely on budget support and sectoral programme aid.

The OECD-DAC harmonisation work has resulted in recommended good practices for effective donor-government partnerships which are as follows:

- Set out objectives and operations of country programmes and make these widely available,
- Multi-year programming of aid,
- Use common performance indicators,
- Build a common framework for aid co-ordination,
- Provide full information on aid flows,
- Support leadership in aid co-ordination by partner governments.

In addition it also sets out good practices for improving donor-donor relationships.

To assess and evaluate progress in harmonisation, the OECD-DAC plans to survey the 14 countries associated with its harmonisation work and it is currently testing its questionnaire in 3 countries (Ethiopia, Vietnam and Nicaragua). The results of these initial surveys are expected later this year. The questionnaires ask donors to assess their improvements in aid practices and harmonisation and governments to assess whether donor systems support harmonisation and alignment and whether progress is being achieved. The questionnaires focus on:

- Ownership: whether harmonisation is being government-led and co-ordinated, and donors support is enhancing national capacity to manage and co-ordinate assistance effectively,
- Alignment: whether donor strategies align with PRS priorities, how budget support is programmed and disbursed, and the delivery of project support through recipient country systems,
- Harmonisation: streamlining of conditionalities, donor support for key sectors and issues relating to donor missions and disclosure of information

The responses from these questionnaires will provide useful information on the progress of harmonisation on some policy and procedural areas generally and on a sectoral basis. But the questionnaires do not provide a framework for African countries to assess the overall quality of aid they are receiving from donors.

The **Strategic Partnership with Africa (SPA)** has been making strong efforts at donor harmonisation, in particular with respect to budget support programmes in selected African countries. The SPA's work highlights the key issues in the context of strengthening harmonisation and alignment of multi-donor budget support programmes, all of which are covered by the policy and procedural analysis using the CBP methodology. It also assesses donors' ability to align their budget support behind government priorities and systems. The SPA approach makes recommendations for improving aid delivery on a country-by-country basis, focusing on institutional, policy, procedural, monitoring and reporting issues within a national context. However, its work is largely limited to aspects of budget support, and again does not provide African governments with the tools to assess the performance of donors and creditors and their own priorities for mobilising funding.

NEPAD's mutual accountability approach recognises the need to harmonise donor practices and align donor support to African countries' priorities and plans. In particular NEPAD notes the importance of African countries taking the lead in monitoring progress and not just leaving it up to donors. The key areas NEPAD outlines are all consistent with the CBP methodology:

- Predictability of donor support as reflected in the proportion of aid channelled through the medium-terms expenditure framework (MTEF),
- Alignment of donor support to national priorities,

- Timing of donor assistance to national planning cycles and processes,
- Harmonisation of disbursement cycles and procedures
- Proportion of aid that is untied,
- Alignment of donor reviews to national cycles of sector and financial reviews,
- Streamlining of reporting requirements as measured by a move to common formats.

NEPAD's focus on the need for African governments to lead this process is very important. However, it has not as yet provided a methodology enabling countries to undertake this task.

The **Center for Global Development** has developed an index of donor performance which builds on the standard quantity of aid measure (ODA/GNI) to take into account debt service payments and a few quality of aid aspects, such as type of aid (project, programme, emergency aid), tying of aid, donor selectivity in choosing recipient countries (eg based on size, governance, and level of development), and project proliferation or dispersion within a recipient country. The index does not reflect factors such as effectiveness of conditionalities or realism of project designs[41]. The main conclusions of the latest index are that:

- The Nordic countries and the Netherlands were the most generous countries in terms of the highest proportion of aid/GDP, with the United States being the lowest,
- Japan's aid flows were reduced by half after taking into account debt service payments. France, Germany, Italy and United States were also major recipients of debt service, and the net flows from these countries was reduced accordingly,
- The value of aid from Greece, Italy, Spain and the United States was reduced most by tying,
- Aid provided by Denmark, Ireland, Italy, Sweden, Switzerland and the United Kingdom was the most selective in 2002. Japan scored low because of its focus on the increasingly affluent East Asia, as did the USA for its large transfers to Colombia, Israel and Russia.
- Ireland, New Zealand, Norway, Portugal, Spain and UNICEF are the main funders of small projects.
- Overall, the worst performers are Ireland and New Zealand because they fund a large number of small projects; Portugal, which also funds a large number small projects and has low selectivity; and Spain and Greece because they are also affected by high tying.
- The top performers are Denmark, Germany, Italy, Japan, Netherlands, United Kingdom, Switzerland and Sweden. Italy comes out well, despite tying, because of its minimal proliferation and high selectivity.

Taking into account the different factors used in preparing this donor performance index and the HIPC CBP methodology for ranking donors/creditors, there is a fair degree of consistency in the overall rankings for the majority of donors and creditors – the exceptions being Ireland (which is ranked higher by African governments), and Italy, Japan and Switzerland (which rank lower).

In general, the methodologies of the OECD-DAC and SPA focus largely on procedures and the initiatives for improving harmonisation, and ignore many of the issues African governments think are vital when assessing aid quality. While the Center for Global Development's work does cover some of these issues, it is more focused towards donor preoccupations such as selectivity, and dependent on donor-generated data. On the other NEPAD highlights the need for African leadership but does not provide any methodology for practical assessment of compliance. As a result, there is an urgent need for African governments to take the lead in using and disseminating the results of a methodology which reflects their needs.

[41] See Centre for Global Development's An Index of Donor Performance: 2004 Edition, April 2004

CHAPTER 5: POSSIBLE AREAS OF ACTION

Suggestions for priority actions for increasing the flow of high quality external assistance to Africa, to support the attainments of the MDGs, are presented at two levels:

- International-level steps to improve the quantity and quality of aid to Africa.
- Country-level actions by donors, creditors and African governments.

5.1 KEY INTERNATIONAL-LEVEL ACTIONS

The key international steps to improve aid for Africa will be:

- to increase overall disbursements to Africa by at least 60% (US$12 billion) a year, which is at the same time an amount Africa can absorb and in line with its needs to meet the MDGs. In light of the fact that recent pledges of aid would imply global increases of only a maximum of US$20 billion a year, this would mean sharply increasing Africa's share of global aid.
- accelerating a global campaign by civil society, around the 5-year review of the Monterrey Summit, to ensure that "laggard" donors such as G7 members – Canada, Germany, Italy, Japan and the US – and smaller donors such as Austria, Greece, Portugal and Switzerland - increase their pledges and flows as rapidly as possible.
- ensuring that aid flows are allocated on a balanced basis to different groups of African countries (HIPCs, non-HIPC LICs, Sub-Saharan MICs and North African countries), in line with their commitment to the MDGs and poverty reduction rather than strategic interests.
- maintaining or slightly increasing the proportion of multilateral flows in total aid to Africa, in order to maximise transaction cost benefits of coordination and pooling of funds, and reduce "strategic" motives for aid allocation, while retaining the independent funding abilities and policy decisions of bilaterals to keep Africa's funding sources sufficiently diversified.
- dramatically reducing technical assistance and switching to capacity-building programmes
- accelerating the trend to budget support for countries with adequate accountability systems, especially for non-HIPC low-income countries which still receive too many projects.
- sharply increasing the share of project finance which goes to PRSP priority sectors and projects, especially in non-HIPC LICs – while broadening this definition to include all types of basic infrastructure, rural development and micro-credit programmes.
- pushing harder for an agreement to untie all aid to all low-income countries (rather than just the least developed), including stand-alone technical assistance and food/emergency aid.
- regularly (semiannually) monitoring whether Monterrey and subsequent pledges are being fulfilled by actual donor disbursements.
- maintaining the current continent-wide balance between grants and loans in order to support long-term debt sustainability while not undermining the ability of multilateral institutions to support low-income countries using loan reflows (see separate note on grants for details).
- ensuring that all new initiatives and funds (whether independent – eg the Global Fund – or bilateral – eg the MCA - are oriented to enhance harmonisation and simplification of donor procedures, and alignment with African PRSPs, rather than funding separate projects.
- reinforcing efforts to streamline conditionality across the range of donor programmes (avoiding cross-conditionality and pooling of conditions), and establishing a system for regularly monitoring the level and stringency of conditionality across all donor programmes.
- ensuring that government and IMF programme forecasts of aid flows are in line with current trends and therefore allow governments more "fiscal space" to spend to attain the MDGs.
- monitoring aid shortfalls and their causes at a continental and individual country level to tackle causes and reduce shortfalls in a coordinated fashion.
- conducting analysis at a country-level of risks of aid dependency and Dutch Disease, but ensuring that these are balanced with analysis of the growth and anti-poverty benefits of additional aid, and oriented to improving the quality of aid to overcome any risks.
- ensuring that all non-concessional finance is targeted to essential private rather than public sector projects, and finances only "productive expenditure".
- providing independent capacity-building support to African governments to enable them to:
  - improve aid management, via new laws, procedures and coordination structures
  - assess donor (and their own) performance in increasing high-quality flows; and
  - analyse fully their own aid needs, how to improve their procedures, absorptive capacity, and the effects of aid flows on long-term debt sustainability.

  Ideally such a programme would be implemented by exchanging research, information and mutual capacity-building assistance among African governments.

5.2 KEY COUNTRY-LEVEL ACTIONS BY DONORS, CREDITORS AND AFRICAN GOVERNMENTS

At the country level, the main policy implications of chapters 2 and 4 are:

African Government New Financing Policies need to be reviewed in order to:

- establish clear new borrowing policies which go beyond amounts and concessionality to cover all quality issues.
- enshrine policies in law, with supporting regulations for their implementation, and annual financing guidelines for PRSP and budget.

Such new policies would aim to:

- mobilise more aid in real terms over next 5-10 years (even if gradually falling as a percentage of GDP) to allow them to reach the MDGs
- move from loans to grants, to maintain or increase the concessionality of their financing while not eliminating the long-term prospect of accessing non-concessional finance especially for the private sector
- move from projects to budget support, and from TA to capacity-building.
- diversify their group of donors if they are relatively few, given that some donors are sharply increasing flows and may be looking to diversify recipients
- rationalise their donor group if it is too large, by discouraging small and poor quality cooperation programmes.
- insist on including more detailed, justified and growing aid projections in macroeconomic programmes agreed with the IMF
- conduct their own analysis of their macroeconomic and administrative capacity to absorb aid flows
- improve donor policies and further streamline conditionalities in order to reduce programme aid shortfalls
- accelerate efforts to streamline and harmonise donor procedures behind recipient government procedures, which themselves need to be dramatically improved, in order to overcome project disbursement problems.

In terms of Donor/Creditor Policies, the top priorities for action (in order) are:

- Flexibility: provide more grant-based rapidly-available “contingency” resources to fund protection against ‘shocks’ (see separate note on shocks for more details).
- Types of Assistance: maximise multi-donor budget support not closely linked to BWI “trigger” conditions; reduce stand alone projects, technical assistance, food aid and emergency assistance
- Policy Conditionalities: sharply reduce conditionality, and interpret country compliance more flexibly, making the vast bulk of aid dependent only on overall PRSP progress rather than individual policy conditions.
- Sectors and Projects: provide more finance solely for PRSP priority sectors and for priority projects within these sectors, eliminate earmarking of budget and sector support, and organise/report on aid according to government classifications,
- Predictability: make 3-5 year pledges and commitments, take all steps to disburse pledges on time, and adjust disbursement schedules to government budget processes.
- Channels of Assistance: maximise on-budget aid and report regularly to government.
- Concessionality: maximise grants where needed to maintain debt sustainability; offer loans in line with country grant element policy, avoid export or mixed credits for HIPCs.
- Policy Dialogue: improve independent in-country economic analysis capacity and participate in government-led meetings on economic policy and budget support.

To improve donor/creditor procedures the most urgent steps are:

- Disbursement Procedures: simplify and harmonise procedures, including eliminating matching funds requirements (or reducing them below 10%), and providing maximum pooled budget support.
- Disbursement Method: provide more resources through up front cash payments to government, rather than reimbursement or direct payment to suppliers.
- Co-ordination and Evaluation: strengthen harmonisation of procedures, and align with government procedures wherever possible.

- Procurement Procedures: eliminate formal and informal tying, encourage local procurement where possible, and preferably use government procurement procedures.
- Conditions Precedent: eliminate all except legal opinions and ensure timely monitoring.

To encourage donors to follow African Government Procedures, governments need to:

- improve their analysis and forecasting of expenditure plans and funding needs, debt sustainability, absorptive capacity and potential and actual shocks; and
- strengthen approval, signature, disbursement, procurement, reporting and audit procedures (see Table 5.1 below for details).

5.3. Mutual Partnership and Accountability

Finally, it is vital to establish procedures for genuine mutual partnership and accountability between Africa and its donors and creditors. There has been a great deal of talk and launching of initiatives in this area, but so far with relatively practical focus on the ground (a notable exception being Uganda's PEAP Partnership Principles). As a result, there has been relatively little progress in the quality and disbursement speed of external assistance flows to Africa.

As a result, there is an urgent need for African governments to take the lead (supported by like-minded donors) in insisting on a system of mutual partnership and accountability, so that donors and creditors to adapt their assistance more fully to Africa's priorities.

The key issue is how this might be achieved. It could be done at two levels:

1. ***At the country level*.** African countries could present an annual long-term development financing strategy, and the findings of their evaluation of donors, at their annual Consultative Group or Round Table meetings. This presentation would not discuss scores of individual donors, but would focus on the areas in which the donor community as a whole and government were falling short of best practice, compare performance with that of donors and governments in other countries, and also stress new steps taken towards best practice by individual donors and government within each country in order to encourage better alignment by other donors. The meetings would also focus on agreeing a matrix of measures for mutual partnership and accountability between donors and government for improving the quality and accelerating the disbursement of aid, along the lines of Table 5.1 of this paper. This matrix can then be used as checklist by African governments and donors/creditors to monitor progress in improving aid flows. Less detailed updates of progress reports could be presented at mini-CGs or other meetings at which donors and government discuss economic policy issues, and special meetings or task forces could be organised to tackle particular issues revolving around specific policies or procedures.

2. ***At the international level*.** The country-specific results could also be synthesised into continent-level assessments of donor performance, on an annual or semi-annual basis and presented at continent-wide meetings between donors/creditors and African governments such as the UNECA Big Table, joint DAC-ECA, SPA meetings, or NEPAD meetings. It would be interesting, for example, for Africans to compare their priorities and findings with those of the DAC and the SPA. Such findings could also identify individual donors without identifying the recipient countries. If wanted, Africans and donors could agree on continent-wide priorities for immediate action and voluntary or binding targets with deadlines for donors to improve the quality of the aid. The results could also be used for informing bilateral discussions between African Ministers and individual like-minded donor Ministers, or joint discussions between groups of African Ministers and groups of like-minded donor ministers.

Ultimately such a system of mutual partnership, evaluation and accountability would be an excellent basis for establishing monitorable indicators for the aid component of MDGs and ensuring that Africa's donors and creditors genuinely live up to their Monterrey promises, so that Africa can fund and attain the Millennium Development Goals.

Table 5.1

INDICATIVE MUTUAL ACCOUNTABILITY MATRIX

POLICY AREA	African Government Objectives	Donor Objectives
Concessionality	• Seek grants in preference to loans and maintain minimum 35% (or higher) grant element • Reject all export /suppliers/mixed credits	• Maximise grants rather than loans and offer loans with minimum grant element of 35% (or more) • Do not offer export/suppliers/mixed credits
Amount of Assistance	• Provide accurate/early forecasts of PRSP funding need • Establish borrowing limit to maintain sustainable debt • Strengthen legislation and institutional procedures to ensure all new external assistance is analysed and ratified in timely manner	• Provide sufficient resources to fund PRSP • Ensure new lending is in compliance with government limits. • Ensure government institutional procedures are followed for new external assistance
Type and Channel of Sssistance	• Maximise budget support through the establishment of a multi-donor budget support programme • Negotiate maximum debt relief from all creditors • Negotiate reduced technical assistance in favour of capacity building support	• Increase budget support and work with government to set up multi-donor budget support programme. • Deliver maximum debt relief as additional budget funding • Minimise technical assistance. Ensure TA projects include budget and time allocation for capacity building
Sectors and projects	• Negotiate aid only for PRSP sectors, and within these sectors prioritise budget projects. • Refuse stand-alone projects • Reject donor ear-marking of sectors and projects	• Ensure donor country programmes are organised and classified around PRSP priority sectors and line ministries • Refrain from financing stand alone projects • Refrain from ear-marking sectors and projects
Flexibility	• Establish early warning systems for tracking and analysing shock and report rapidly to donors on shocks	• Provide maximum possible resources to finance protection against external shocks, through multi-donor facility
Predictability	• Provide clear medium-term expenditure and financing plans	• Provide government with projected commitments and disbursements for 3 to 5 years, in time for annual budget
Policy Conditionality	• Negotiate minimal donor conditionalities. • Seek donor flexibility in interpreting the implementation of conditions.	• Interpret flexibly the implementation of conditions to ensure that disbursements are not delayed or suspended if agreed PRGF/PRSP outcomes are basically on track
Policy Dialogue	• Brief donors/creditors on policy updates and progress at semi-annual (or quarterly) meetings	• Participate in semi-annual (or quarterly) meetings with government
PROCEDURE AREA		
Conditions Precedent	• Negotiate minimum conditions and monitor implementation on timely basis	• Reduce conditions precedent to legal opinion only and monitor implementation in timely manner

	• Streamline parliamentary approval processes which are causing significant delays	• Minimise cross-financing conditions, whenever possible
Disbursement Method	• Seek disbursement of funds through direct cash payments, rather than reimbursement claims • Establish mechanism to determine value of all aid-kind, especially food aid	• Provide programme (budget support) to minimise disbursement delays • Provide information on value of all aid-in-kind, especially food aid
Disbursement Procedures	• Seek reduced donor matching fund requirements to below 10% of loan/grant amount • Work with donors to harmonise disbursement procedure • Exclude donor funds for non-priority projects form tax exemptions and do not provide matching funds for them	• Reduce donor matching fund requirements to below 10% of loan/grant amount • Work with government to harmonise disbursement procedure • Review tax exemptions requested and count government contributions in kind and tax exemptions as matching funds
Procurement Procedures	• Reject tied funds and encourage local procurement • Ask donors to use government procurement procedure	• Eliminate all forms of tying, and encourage local procurement • Comply with government procurement procedures
Co-ordination and Evaluation	• Survey donors annually to assess compliance with government policy and report at CG meetings • Ask donors to minimise review missions and meetings and to conduct jointly whenever possible • Work with donors to harmonise reporting and financial accounting formats	• Report annually to government on progress with above objectives. • Reduce demands on government officials by synchronising review missions and meetings with other donors • Work with government to harmonise reporting and financial accounting formats

ANNEX 1

DEFINING EXTERNAL ASSISTANCE, AID AND CONCESSIONALITY

External assistance is comprised of aid or concessional finance, also known as 'official development assistance (ODA)', and market-related or non-concessional finance. The distinction between aid and market-related finance reflects the actual cost of funds to the recipient, which is characterised using the concept of concessionality. For HIPCs, aid flows account for the majority of external assistance for development purposes. However, many developing countries also use export credits and other types of non-concessional funding.

Aid (also known as ODA) is comprised of grants, which are transfers that do not have to be repaid, and loans, which qualify as 'official development assistance (ODA)' to developing countries. **Official development assistance** is grants or loans, which are:

- lent by the official public sector – that is by any government or government related body, or guaranteed by a creditor government body such as an export credit agency;
- intended to promote economic development and welfare. As a result, grants and loans for military purposes are excluded from ODA; and
- on concessional financial terms. For the Organisation of Economic Co-operation and Development (OECD), ODA concessionality is defined as loans having a grant element of at least 25%.

Loans, which are lent by the public sector but do not qualify as ODA because they are not primarily aimed at development or are not concessional, are known as **Other official flows (OOF)**. These include exports credits extended by donor governments or guaranteed by them. Military grants and loans are also classified as OOF.

Loan concessionality is determined by the **grant element** (GE) calculation, which is defined as:

$$\text{GE }(\%) = \frac{\text{(nominal loan amount – present value of projected debt service)}}{\text{(nominal loan amount)}} * 100$$

The calculation reflects the loan terms at the time of commitment, when the loan is agreed. The **present value** is the discounted stream of future debt service payments assuming the loan is fully disbursed on the date of contract. In other words, the calculation of future interest payments is on the total loan amount and does not take into account that disbursements can take place over a number of years.

Since a grant is not repaid nor is there any interest charge, the present value of future payments is nil and therefore the grant element of a grant is 100%.

For loans, the length of the grace and maturity periods and rate of interest will determine the present value of future debt service payments and hence the grant element. In general, loans with longer grace and maturity periods and lower interest rates have a smaller present value and therefore they have a larger grant element and are more concessional. For example, an IDA loan with grace and maturity of 10 years and 40 years respectively and a service charge of ¾% has a grant element of approximately 70%. This means that over the life of the loan, the borrower will only be repaying, in present value terms, about 30% of the nominal loan amount, the other 70% being equivalent to a grant. Loans with shorter grace and maturity periods and/or higher interest rates will have lower grant elements and therefore be less concessional or more costly to service.

The Development Assistance Committee (DAC) of the OECD defines concessional loans as having a grant element – calculated on the basis of a uniform 10% discount rate for all loans, of at least 25%. This is the current basis used for defining ODA. The difficulty with this definition is that at times of low interest rates, it is possible for a commercially priced loan in a low-interest rate currency to be concessional.

In 1996, the OECD changed the way in which it determined concessionality for export credits, but not for ODA. Instead of a flat 10%, the discount rate for calculating the grant element of an export credit is the market-related Commercial Interest Reference Rates (CIRR)[42]. Using CIRR discount rates, an export credit is considered to be concessional if it has a grant element of at least 35%.

[42] For the latest CIRR rates issued by the OECD, see www.oecd.org.

However, for the 49 low income countries falling within the United Nation's classification of least developed countries (LLDCs), the concessionality threshold for export credits is a grant element of 50% or higher. This means that LLDCs should only be borrowing export credits which have a grant element of 50% or more. LLDCs is a sub-group of low income countries, established by the United Nations as falling below thresholds for income, economic diversification and social development[43]. Most, but not all, HIPC countries are LLDCs subgroups[44].

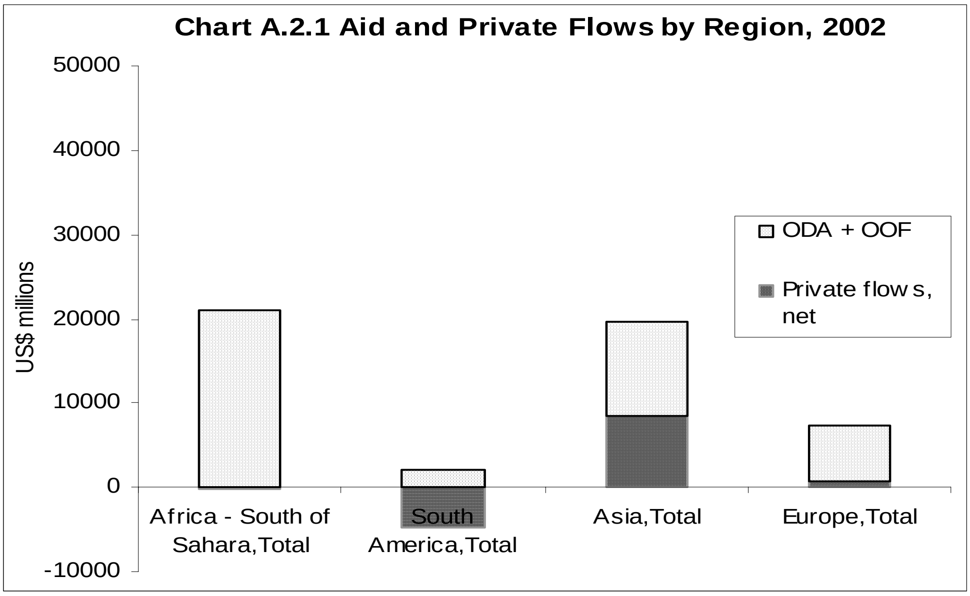
For the purpose of the HIPC Initiative, the IMF and the World Bank use the six-month average currency-specific CIRRs as the discount rates for calculating the present value of debt[45].

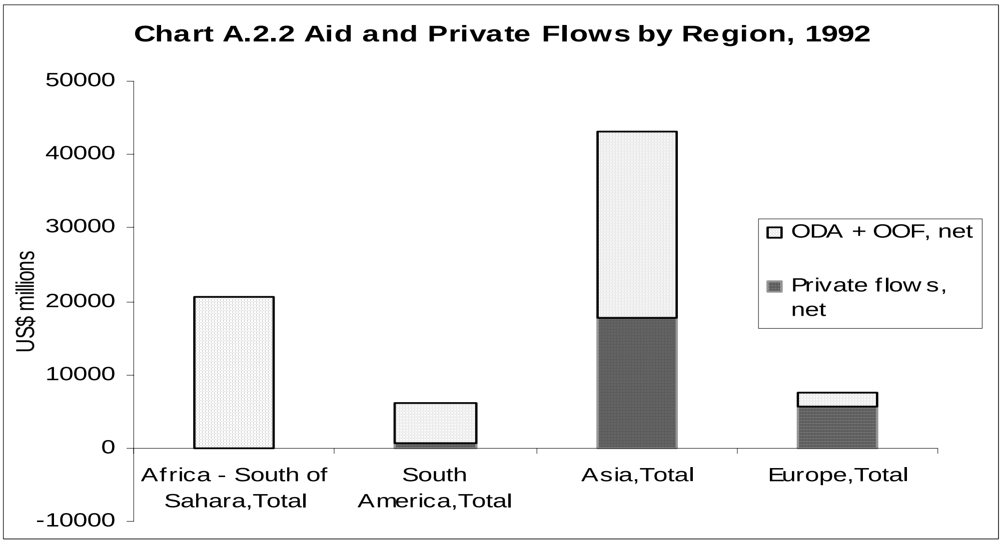
The International Monetary Fund has adopted the 35% grant element as the threshold for the concessionality of loans to be excluded from borrowing limits in Fund Poverty Reduction and Growth facility (PRGF) programmes However, the discount rate used by the IMF to calculate the grant element for new borrowings is not the six-month average CIRR rates used to calculate for the PV of debt under the HIPC Initiative. Instead it is an average CIRR rate (6 monthly average or ten-year average) plus a margin, varying with the maturity of the new borrowing. So effectively this means the IMF is using a higher discount rate to compute the grant element of new borrowings for compliance with PRGF programmes.

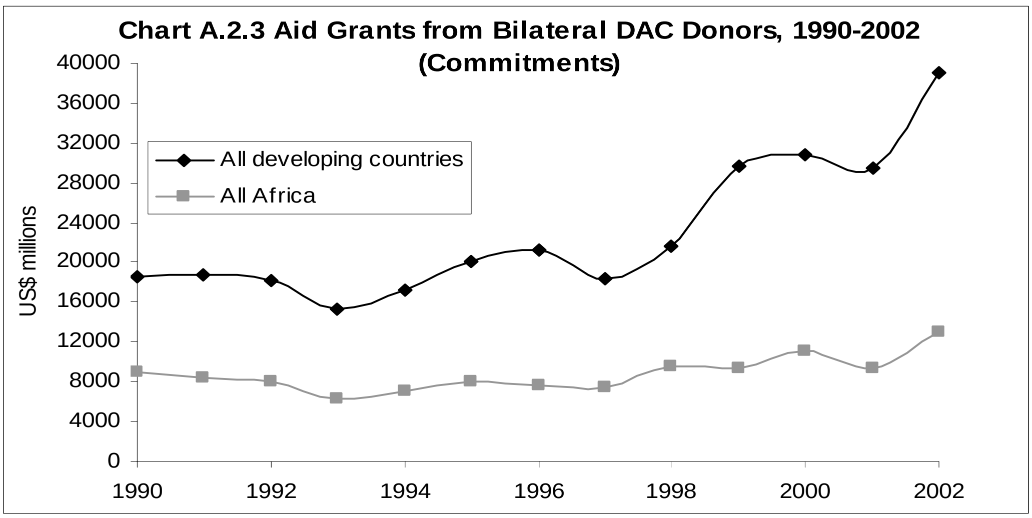
Table 4.2 (see Section 4.1.1) provides examples of lending terms for some major multilateral and bilateral creditors and illustrates the concessionality of lending with alternative discount rates. This table illustrates the difference in loan concessionality of using a standard 10% or the currency specific CIRR rates as the discount rate. For example, the IMF's PRGF loan is concessional, with a grant element of 49.1% using a 10% discount rate, and yet using its own methodology, a PRGF loan is non-concessional with a grant element of 27.9%.

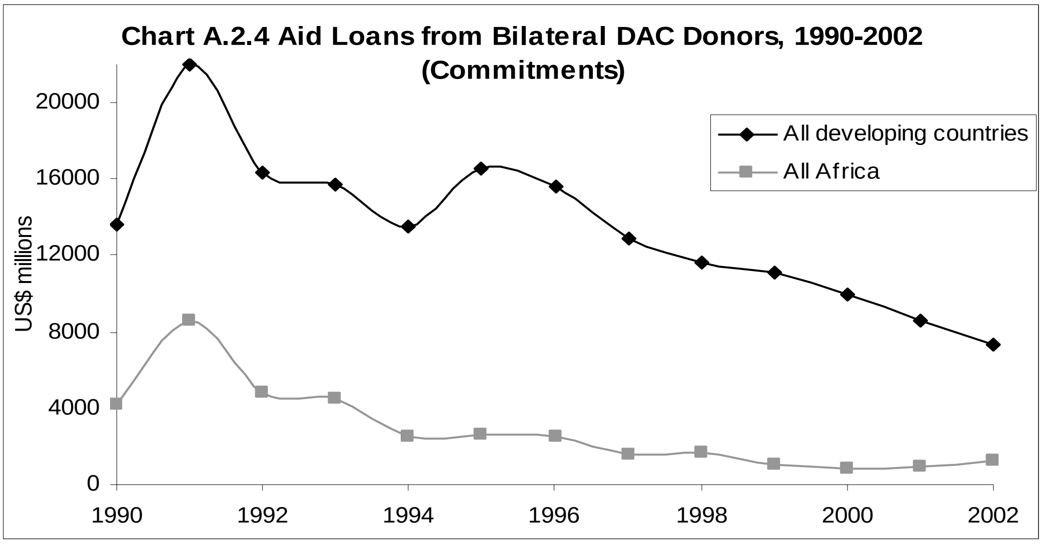
[43] For more details on LLDCs, see UNCTAD (2000) or website www.un.org.special-rep/ohrlls
[44] The exceptions are Bolivia, Cameroon, Congo Republic, Côte d'Ivoire, Ghana, Honduras, Kenya, Nicaragua, Nigeria, Tanzania and Vietnam.
[45] For more details on the HIPC Initiative and its implementation, see Martin and Johnson (2001).

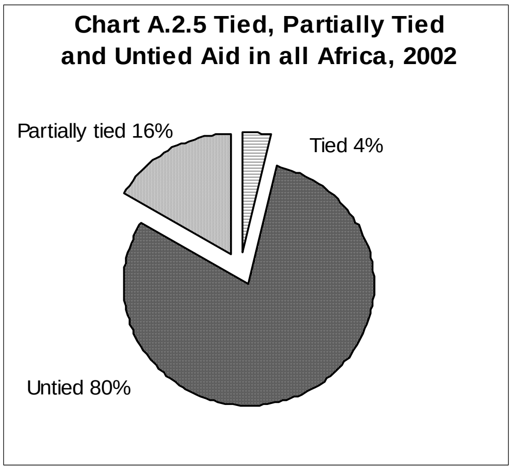
ANNEX 2 OVERALL TRENDS AND COMPOSITION OF AID FLOWS TO AFRICA

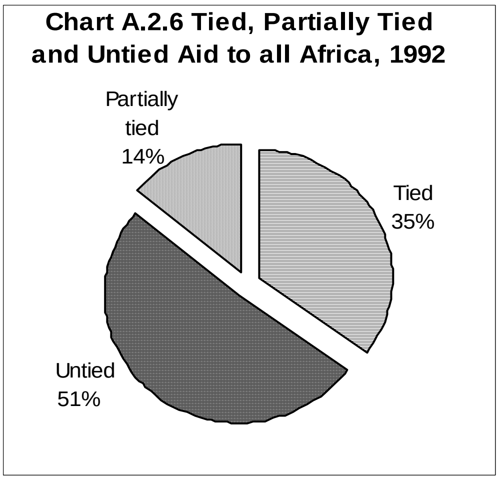








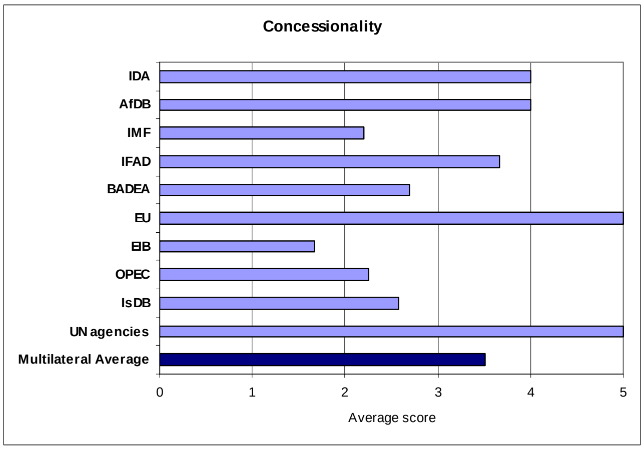


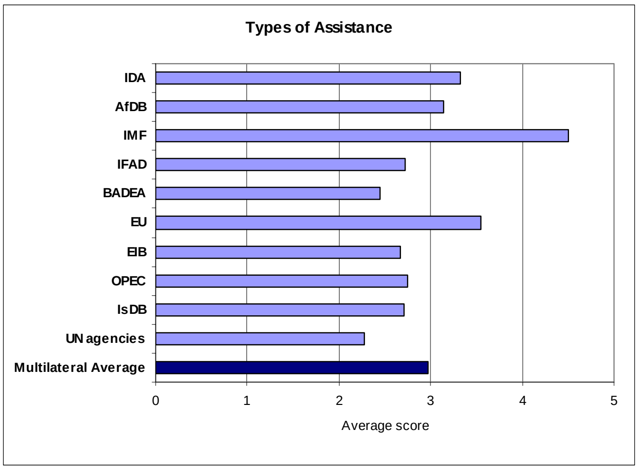


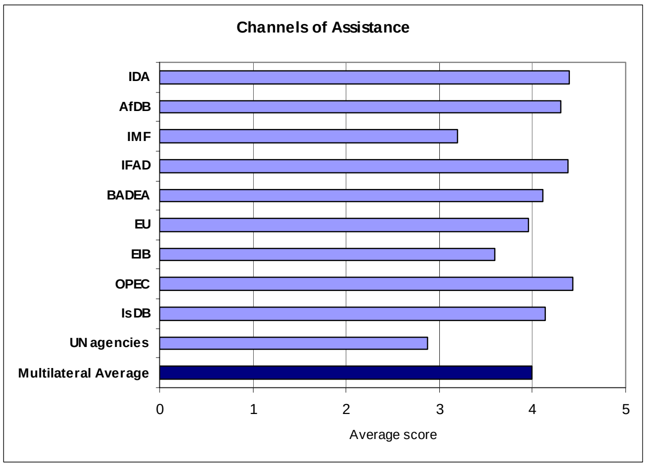
Source: OECD DAC for all charts

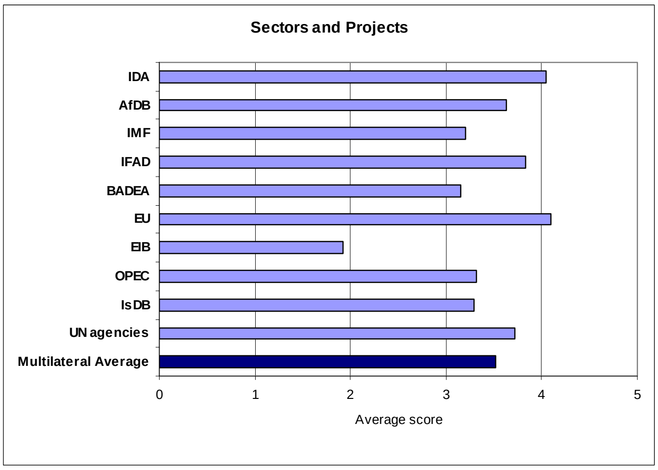
ANNEX 3 DETAILS OF ANALYSIS OF DONOR/CREDITOR POLICIES AND PROCEDURES

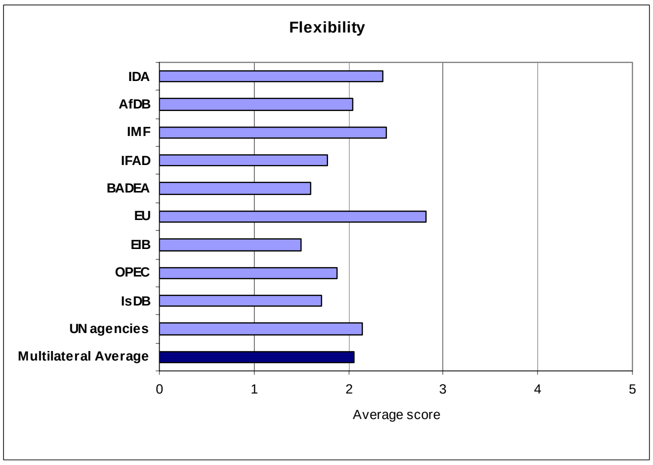
Analysis of Multilateral Donor/Creditor Policies

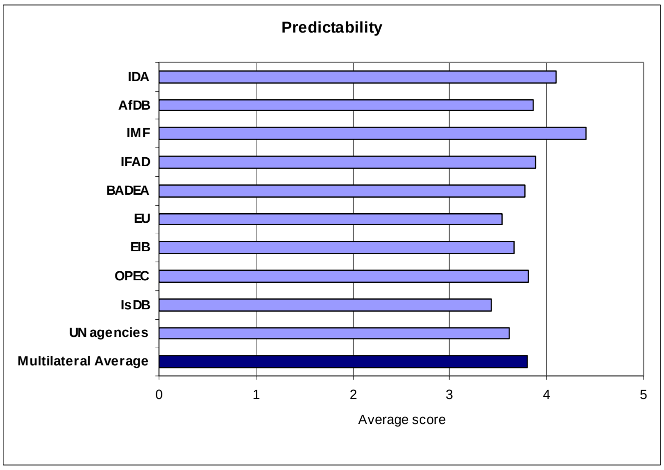


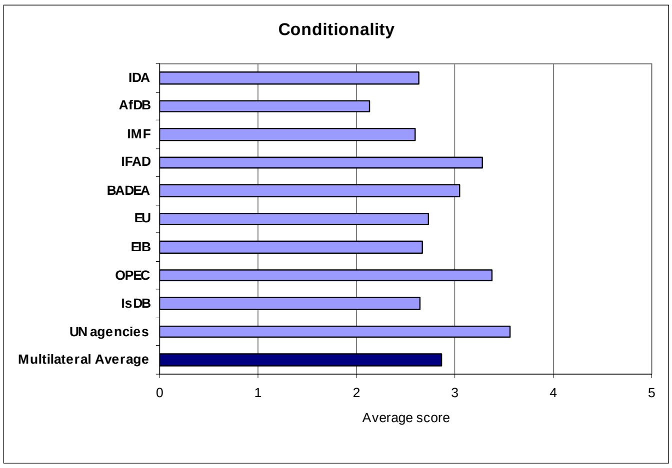




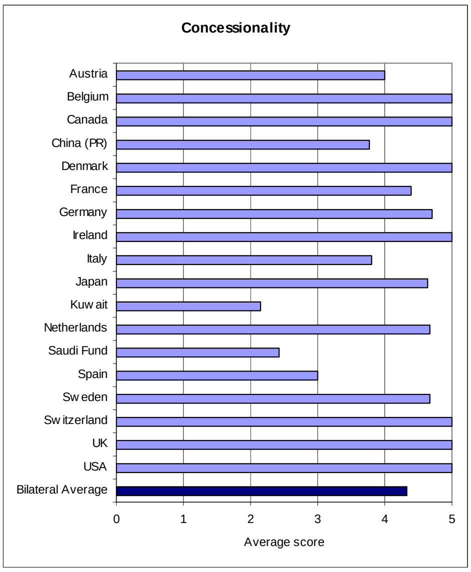


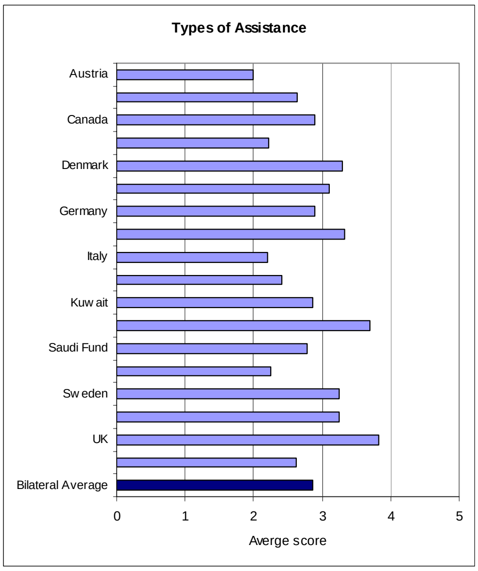


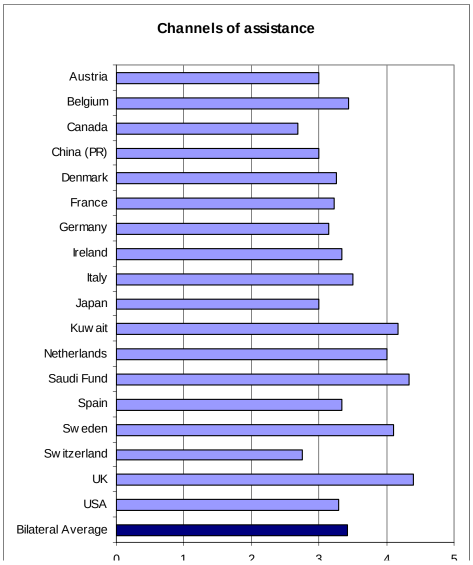


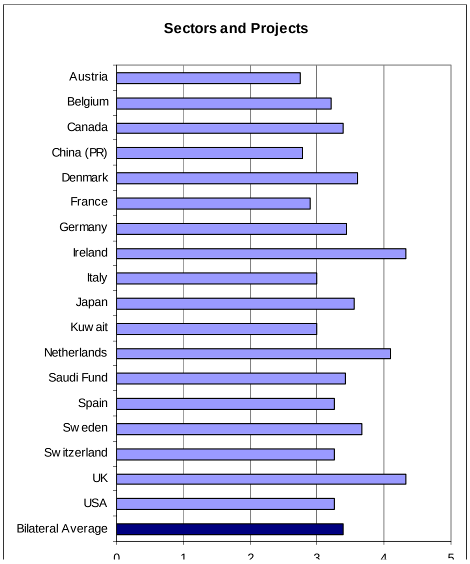

Conditionality
IDA
AfDB
IMF
IFAD
BADEA
EU
EIB
OPEC
IsDB
UN agencies
Multilateral Average
0
1
2
3
4
5
Average score

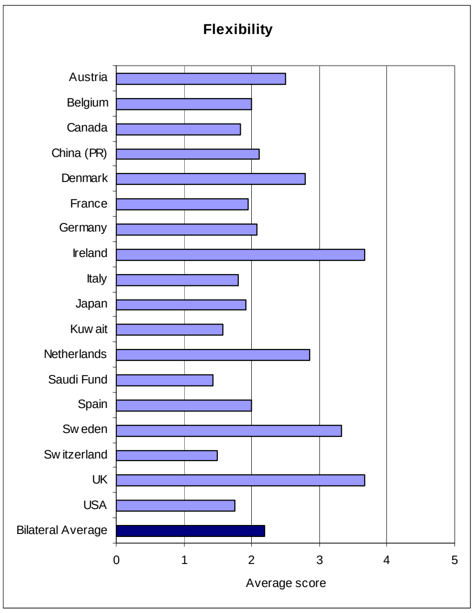
Analysis of Bilateral Donor/Creditor Policies

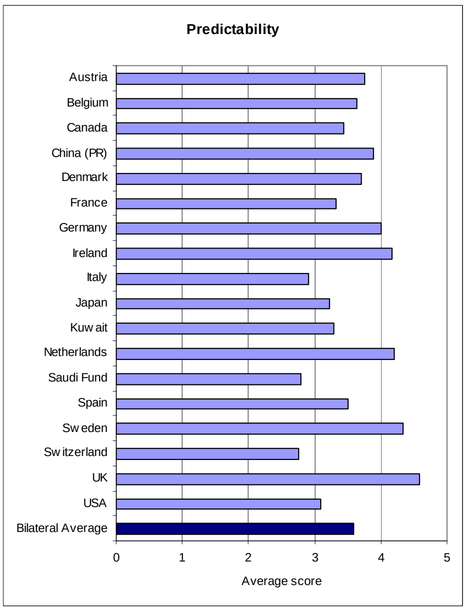


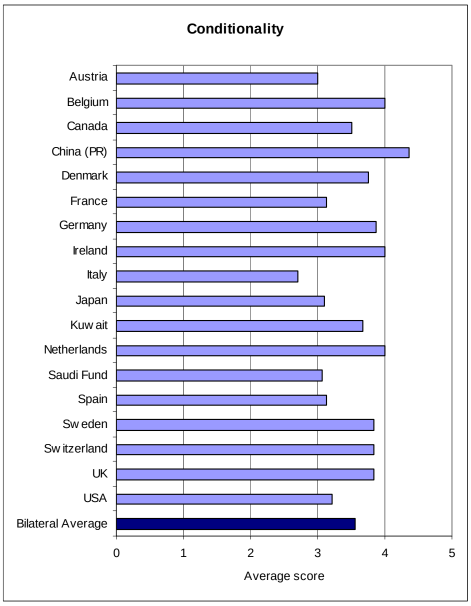




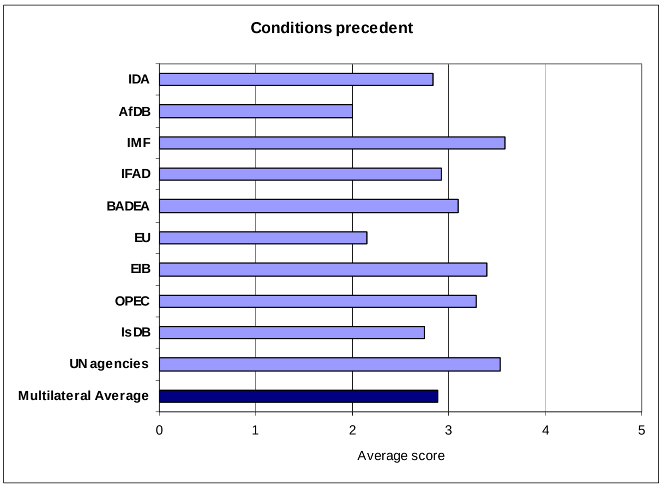


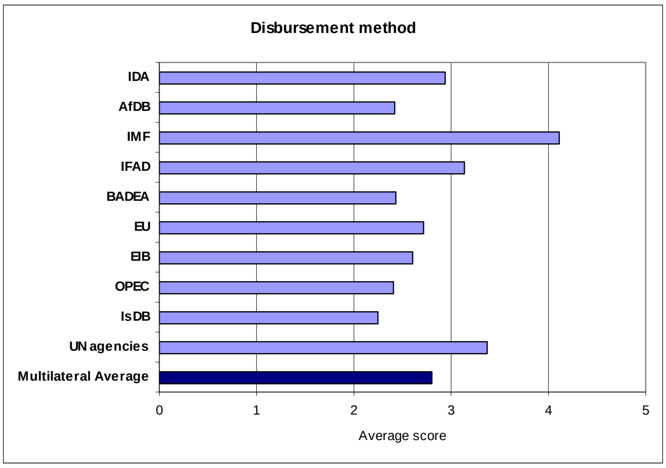


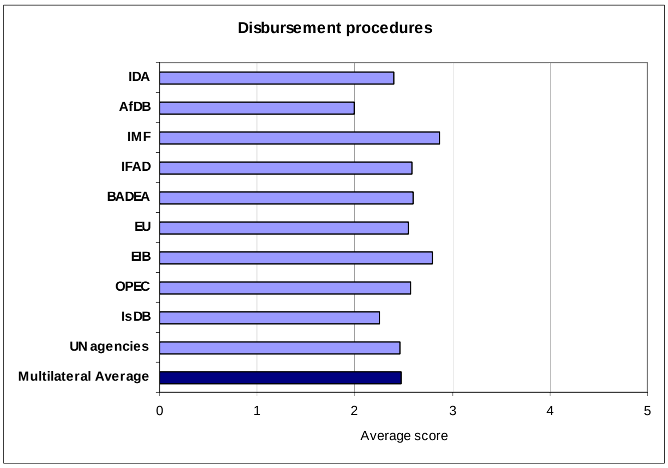


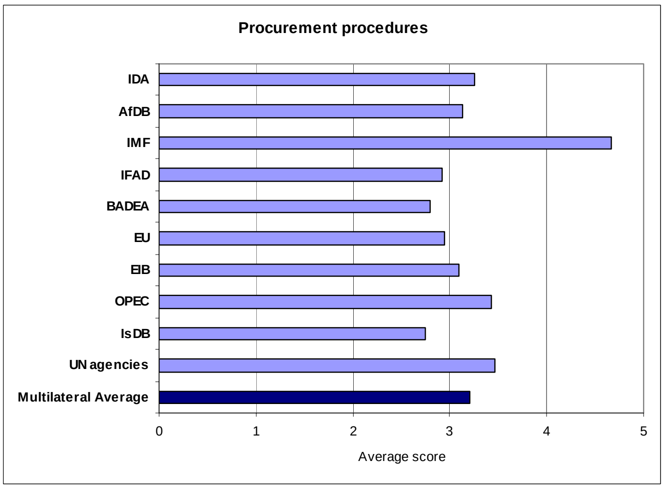

Conditionality
Austria
Belgium
Canada
China (PR)
Denmark
France
Germany
Ireland
Italy
Japan
Kuwait
Netherlands
Saudi Fund
Spain
Sweden
Switzerland
UK
USA
Bilateral Average
0
1
2
3
4
5
Average score

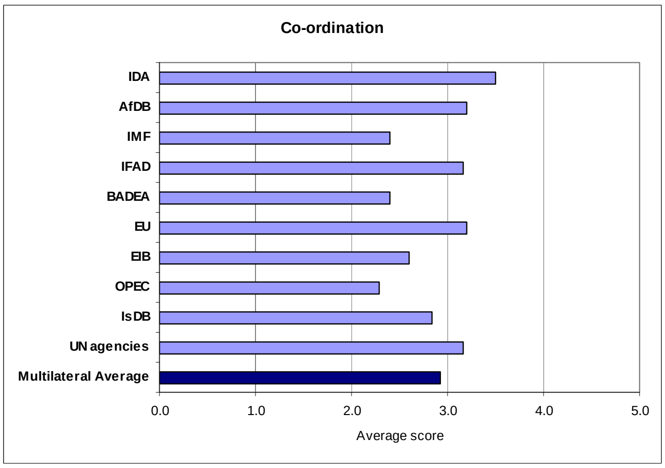
Analysis of Multilateral Donor/Creditor Procedures



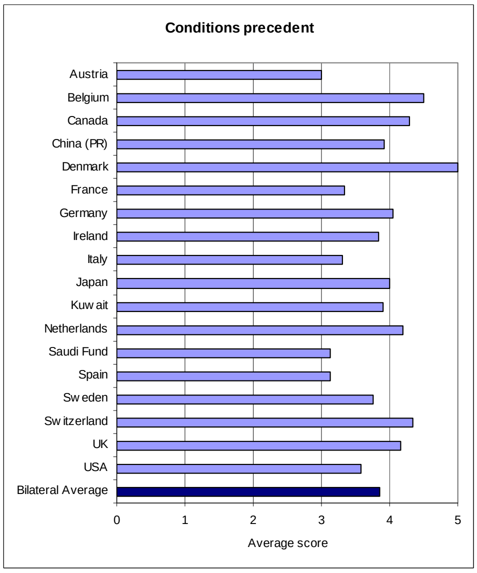


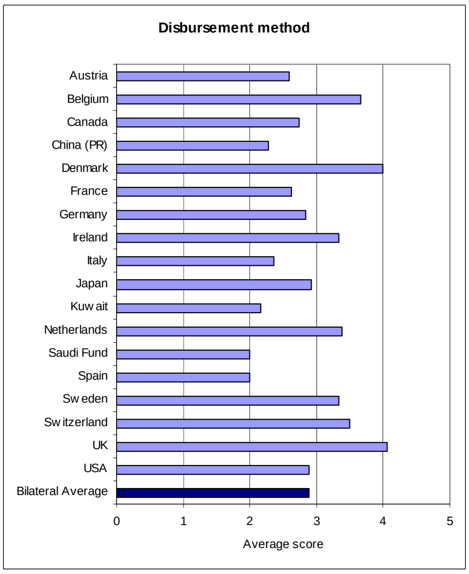


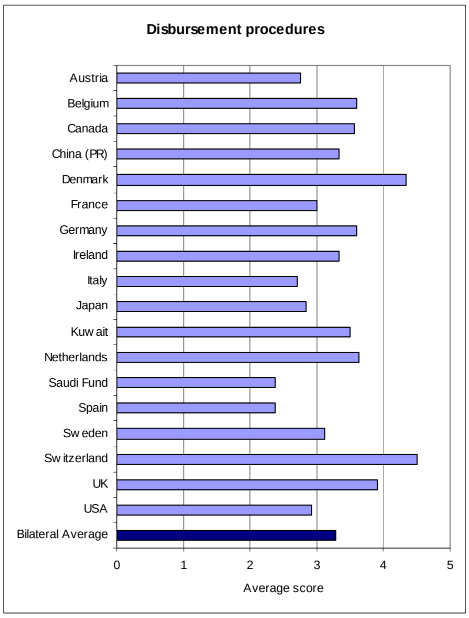


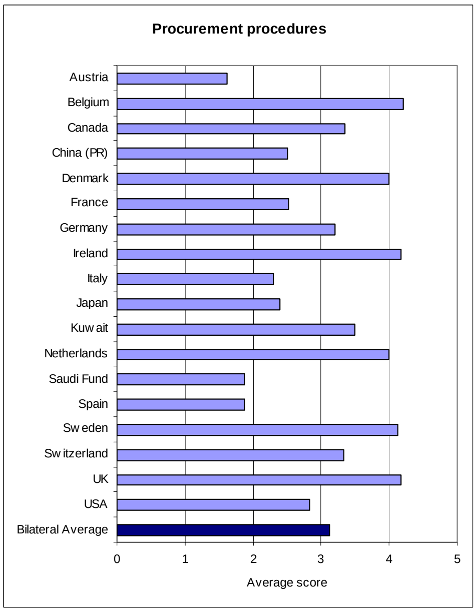


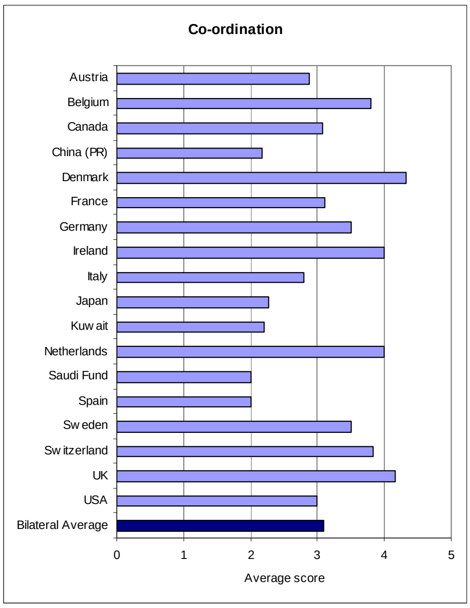
Analysis of Bilateral Donor/Creditor Procedures











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