PFM
REPORTING FRAMEWORK

AFROSAI-E

Public Financial Management Transversal Risk Report

2023

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ABBREVIATIONS

AFRODAD	African Forum and Network on Debt and Development
AU	African Union
CARI	China Africa Research Initiative
CRBC	China Road and Bridge Corporation
DPA	Deferred Payment Agreement
EPC	Engineering, Procurement and Construction
GIADC	Ghana Integrated Aluminium Corporation
GNI	Gross National Income
HRD	Human Resources Department
IMF	International Monetary Fund
ICBF	Institutional Capacity Building Framework
MDA	Ministries, Departments and Agencies
MOF	Ministry of Finance
MPSA	Master Project Support Agreement
NPV	Net Present Value
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
QA	Quality Assurance
RBPD	Resource Backed Public Debt
RFI	Resource Financed Infrastructure
SAI	Supreme Audit Institutions
SDG	Sustainable Development Goals
SGR	Standard Gauge Railway
SPV	Special Purpose Vehicle
TADAT	Tax Administration Diagnostic Assessment Tool
TNA	Training Needs Analysis
ToT	Training of Trainers
UN	United Nations

1. FROM AFROSAI-E CEO

I am pleased to present the second edition of the Public Financial Management (PFM) Transversal Risk Report. The continuous capacitation of Supreme Audit Institutions (SAI) is essential to improving the professionalism and quality of the audit work of the SAI to contribute to efficiency and accountability in the use of public resources. This is important as SAIs are no longer seen as domestic organisations concerned with the legality and compliance of public spending but as ambassadors and promoters of concepts such as transparency, accountability, governance, and performance at the international level.

This is built on the background of sound PFM and a PFM-RF tool that allows SAIs to report holistically on public financial management risks by focusing on the overall functioning of the system and the related synergies. This is detailed in Chapter 3 of the report.

Following the methodology overview in Chapter 4, the focus is on extrapolating insights from the AFROSAI-E 2022 Institutional Capacity Building Framework (ICBF) Self-Assessment onto SAI's use of broad-based PFM diagnostic tools in performing their audits. This is detailed in Chapter 5, which also complements our Training of Trainers (ToT) concept of training needs analysis (TNA) in establishing the transversal training needs for SAIs at the strategic level, which are required for SAIs to reach the required ICBF levels.

Furthermore, in Chapter 6, we contribute to the discourse by reflecting on public debt in the region, specifically the inherent risk with resource-backed public debt in the event of default by countries. Such loans are often opaque as little information about their contractual terms is disclosed, making public accountability difficult. As auditors, we acknowledge that such loans can benefit poor countries with a wealth of natural resources, but they require a careful cost-risk and debt sustainability analysis—and transparency about their contractual terms. Therefore, in this edition, we advocate for SAI's increased role in promoting transparency, accountability, and the sustainable management of natural resources. SAI oversight can help minimise the risks of corruption, mismanagement, and misuse of such resources, thus ensuring that the benefits derived from resource-backed financing are maximised and effectively used for the country's development.

2. Editors Notes

In today's global economic landscape, effective PFM is crucial for achieving sustainable development and ensuring the efficient use of public resources. With the increasing demands for public support and services and the challenges posed by the COVID-19 pandemic, governments must focus on sound PFM practices to promote fiscal discipline and foster economic growth.

Well-functioning PFM systems are essential for governments to ensure the reliable delivery of public services and implement policies to realise sustainable development goals. SAIs are located centrally in a country's PFM system and are ideally placed to audit the entire PFM system. In the AFROSAI-E region, the PFM-RF diagnostic tool has been used to report on risks and evaluate the PFM system's capacity to support the attainment of sustainable development. Using the PFM-RF tool, auditors can give assurance and advice on the readiness of the PFM system to create an environment that enables the achievement of the Sustainable Development Goals (SDGs).

The tool's significant use is cross-collaboration and synthesis of technical know-how across the different SAI countries in the region through initiatives such as the ToT initiative. Through this and other initiatives, AFROSAI-E members have gradually built experienced expert teams to support capacity building and provide quality assurance (QA) of PFM-RF audits in the AFROSAI-E region while also diagnosing potential risk areas in the PFM process. One such risk is resource-backed public debt (RBPD).

RBPD is becoming a significant source of financing for governments, allowing them to bridge fiscal gaps and invest in critical infrastructure projects. However, it is imperative to ensure that RBPD is managed prudently to avoid excessive borrowing, debt distress, and negative impacts on future generations. To ensure transparency, accountability, and good governance in PFM, recourse to international standards and guidance serve as important benchmarks. While the rise of nationalist sentiments has influenced global dynamics, it is crucial to recognise that aligning approaches to RBPD with international standards ensures the adoption of sound concepts that transcend regional boundaries and jurisdictional specificities. Learning from international experiences and sharing best practices can help countries avoid repeated errors and improve their financial management systems.

3. INTRODUCTION

3.1 Background of the Project

Established in 2005, AFROSAI-E is the English-speaking subgroup of AFROSAI, the African branch of the International Organisation of Supreme Audit Institutions. It is an independent, non-political, and autonomous member-based institution with 26 Auditors-General from English-speaking African states making up the governing board.

AFROSAI-E plays a professional and innovative role in the region by facilitating the sharing of information with and between its members and supporting them towards better execution of their mandates. It is committed to cooperating with and supporting the member SAIs to strengthen their institutional capacity and help them to fulfil their audit mandates successfully, thus making a difference in the lives of citizens.

3.2 The Publication Objectives

The 2023 overall project objectives are to:

a) Empower SAIs for greater audit impact and quality by informing them and creating an awareness of the transversal risk areas within various PFM systems and in the implementation of SDGs.
b) To annually complement other global diagnostic tools, for example, PEFA, TADAT, etc., by contributing to the body of knowledge on improving PFM systems by identifying transversal PFM systems and SDG implementation risks.

The 2023 Transversal Risk report aims to draw insight from the AFROSAI-E 2022/2023 ICBF findings on SAI's use of broad-based PFM diagnostic tools in performing their audits. The ICBF is the basis of the Theory of Change for the 2020–2024 AFROSAI-E Strategic Plan, which positions SAI-focused capacity-building opportunities, i.e., learning, on-site visits, technical advice and assistance, generic and customised audit manuals, and tools with increased SAI professionalisation for greater audit impact and ultimately better governance, increased transparency, and accountability in the public sector.

Furthermore, it also aims to complement the AFROSAI-E ToT concept of TNA in establishing the transversal training needs for SAIs at the strategic level, which is required for SAIs to reach ICBF level 3 in the use of broad-based PFM diagnostic tools when performing their audits annually. Figure 3-1 below shows that these numbers have declined year-on-year.

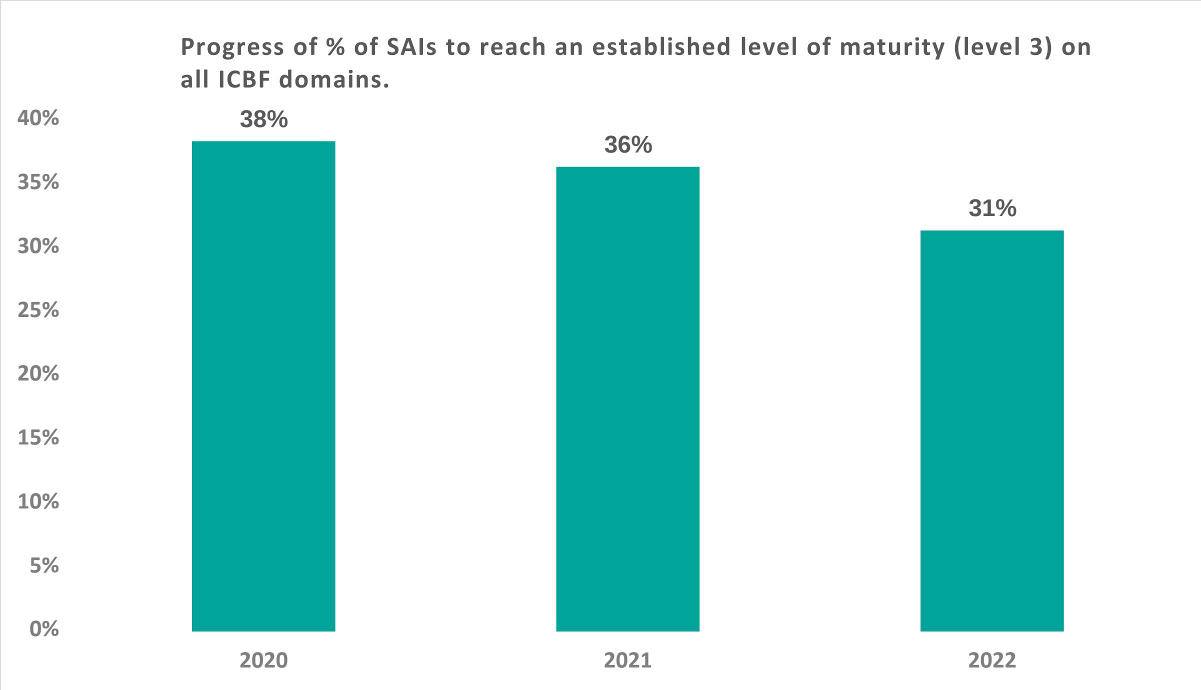

Figure 3-1: Progress of % of SAIs to reach an established level of maturity (level 3) on all ICBF domains

3.3 The PFM Framework Tool

The PFM-RF tool allows auditors to assess the performance of public financial management processes along the whole budget cycle, targeting specifically the readiness of the PFM system to enable the realisation of all SDGs. The assessment tool focuses on core PFM institutions such as the Ministry of Finance, Parliament, and Revenue Authority, as well as important sector ministries and departments.

Consistent and continuous reporting allows SAIs to provide meaningful recommendations to the government and parliament to facilitate a systemic response to identify root causes in the PFM system that impede the SDGs. The five key PFM processes are:

- Macroeconomic Policy, Fiscal Policy, and Strategic Budgeting.
- Budget Preparation.
- Budget Approval.
- Financial Management and Service Delivery.
- Accounting, Reporting and Oversight.

4. METHODOLOGICAL CONSIDERATIONS

This section presents the methodological approach to preparing the PFM-RF Transversal Risk Report. Individual country TNA reports were supplemented with semi-structured interviews with selected train-the-trainer participants, as well as the outcomes of the ICBF report. Participating countries included Gambia, Ghana, Kenya, Mozambique, Namibia, Rwanda, Sudan, Tanzania, Uganda, and Zambia.

4.1 Methodology

Data was sourced from the AFROSAI-E 2022/2023 ICBF findings on SAI's use of broad-based PFM diagnostic tools in performing the audits. This data was assessed for completeness and consistency across the different countries. Furthermore, this was triangulated with the AFROSAI-E ToT concept of 'TNA' and inputs from the ToT champions. Figure 4-1 below provides a high-level thematic of the technical approach and key outputs.

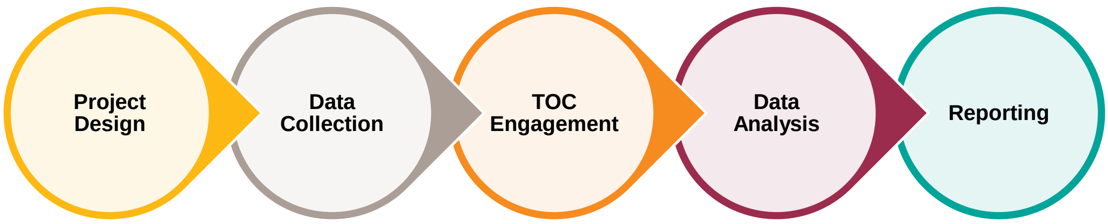

Figure 4-1: Methodological Process

STEP	DESCRIPTION
Project Design	○ Based on the project scope, the following scoping matters were addressed: • Identification of the specific problem/issue. • Review of research questions to ensure they adequately cover the research focus. • Determining the geographic boundaries wherein AFROSAI-E would like to engage expert participants through preliminary engagements with the AFROSAI-E technical team.
Toc Engagement	○ Identified a community of experts from AFROSAI-E's ToT Champions 2022 class as stakeholders and mapped these to ensure no gaps.

	○ Each expert participant's roles and expectations were clarified during the process.
Data Collection	○ Refined research questions, chose and implemented data collection methods, and identified key participants. ○ Designed and developed a primary data collection tool tailored for online interviews via appropriate digital channels, i.e., MS Teams, Zoom or Google Duo ○ An internal focus group with selected experts was established to refine the themes and questions. ○ Collected the relevant data from secondary sources identified by the AFROSAI-E technical team, such as the ICBF reports.
Data Analysis	○ Two main data sources were utilised, i.e., primary (interviews with ToT Champions) and secondary (ICBF reports). ○ Interviewers were requested to make physical notes of the discussion and produce a reflective commentary on it. ○ These interviews were transcribed, and data was analysed according to the different thematic areas.
Reporting	○ A formal written report documented the main findings and drew conclusions. ○ The draft report was disseminated and discussed with selected participants from the community of experts to validate **'ground-truth data'** and was then refined based on inputs**.** ○ Conclusions focused on the priority matrix on implementation with proposed time horizons and key threats and mitigants.

5. PFMs TRANSVERSAL ASSESSMENT OF PERFORMANCE OUTCOME AND RISKS

5.1 Overview

The 2023 Transversal Risk draws insight from the AFROSAI-E 2022/2023 ICBF findings on SAI's use of broad-based PFM diagnostic tools in performing their audits. The ICBF remains a vital regional tool to measure member SAI growth and progress to close maturity gaps as members implement the information acquired from various interventions. The State of the Region Report reflects the ongoing efforts of the SAIs in the region to strengthen their capacity and meet stakeholder expectations.

The information from the ICBF report is complemented by individual country TNA reports concluded in 2022. This also compliments the AFROSAI-E ToT concept of 'TNA' in establishing the transversal training needs for SAIs at the strategic level, which are required for SAIs to reach ICBF level 3 in the use of broad-based PFM diagnostic tools in performing their audits annually.

For simplicity, it is highlighted that PFM rankings stretch from zero (0) to four (4). Across the PFM processes and subprocesses, a zero ranking reflects overall non-adherence with the PFM process as reflected by policy inconsistencies, inadequate data, lack of alignment with relevant legislation, and lack of cooperation, among other things. The report emphasised rankings below three, which reflected areas that needed significant consideration.

5.2 Findings on SAI Use of Broad-based PFM Diagnostic Tools

This section will provide an analysis of the data from the contributing reports on a consolidated basis. It will review data trends across the various PFM-RF tools, the 2022 and 2023 ICBF data, and the ICBF State of the Region Reports, identifying key trends and differentiators or unique aspects while noting the specific peculiarities of individual jurisdictions. The constitutionally enshrined mandate of SAIs places them in a perfect position to take a holistic look at the efficiency and effectiveness of a country's PFM system.

The PFM-RF has been designed to enable SAIs to contribute meaningfully to achieving SDGs at the country level. Using this diagnostic assessment tool, SAIs can regularly audit the performance of the entire PFM system and give assurance on country-level implementation policies and programmes towards achieving the SDGs.

The section will thus assess the identified PFM risk areas and institutional capacity needs by comparing entity performance and exploring and unpacking the root causes simply and clearly.

5.2.1 Internal Quality Assurance Processes

To maintain their effectiveness, SAIs must have robust internal QA processes. These processes help to uphold international standards, enhance the credibility of audit reports, and ensure the overall quality of their work. This section will explore the importance of internal QA processes for SAIs and discuss their key elements based on the provided search results. Implementing rigorous internal QA processes enables SAIs to provide accurate and reliable information to legislatures, governments, and other stakeholders. It also helps them identify improvement areas and enhances their performance and effectiveness.

During the period under review, QA management systems to promote an internal culture of quality performance were observed as not being established or needing improvement. In instances where a policy may have been developed, it is not translating into systems to support implementation. Key to this is setting an appropriate tone by top and senior management to demonstrate organisational values.

Implementing rigorous internal QA processes enables SAIs to provide accurate and reliable information to legislatures, governments, and other stakeholders. It also helps them identify improvement areas and enhances their overall performance and effectiveness, as reflected in Figure 5-1. According to the 2022 ICBF findings, SAIs generally believe that their internal policies and procedures are developed and adequate, with half indicating that they are satisfied with their internal governance and oversight mechanisms, which is consistently contradicted by quality review

procedures as well as by an analysis of the cross-cutting issues, which strongly allude to gaps in the planning and implementation capacity at SAIs.

Figure 5-1: Elements of Internal QA Processes for SAIs

Of importance to the SAIs is the need to implement an institutionalised process to collect and validate their self-assessment responses before submitting them. Furthermore, SAIs must allocate adequate time and resources to complete the annual questionnaire and perform the necessary internal QA reviews on the responses.

5.2.2 Independence and Legal Framework

The dimension of independence and legal framework relates to the operational, financial, and administrative independence of the SAI, the head of the SAI, and its staff, as stated in the laws. The ICBF framework measures independence and legal frameworks over eight (8) elements, namely:

a) Independence of the Head of the SAI.
b) A sufficiently broad mandate.
c) Access to information.
d) Right and obligation to report on the SAI's work.
e) Effective follow-up mechanisms.
f) Financial independence of the SAI.
g) Administrative independence of the SAI.
h) Oversight and accountability.

During the period under review, it was observed that legal frameworks that comply with international guidance and best practices are lacking in many of the SAIs. Unfortunately, there have been marginal decreases in average scores across the elements of this domain, as shown in Figure 5-2 below.

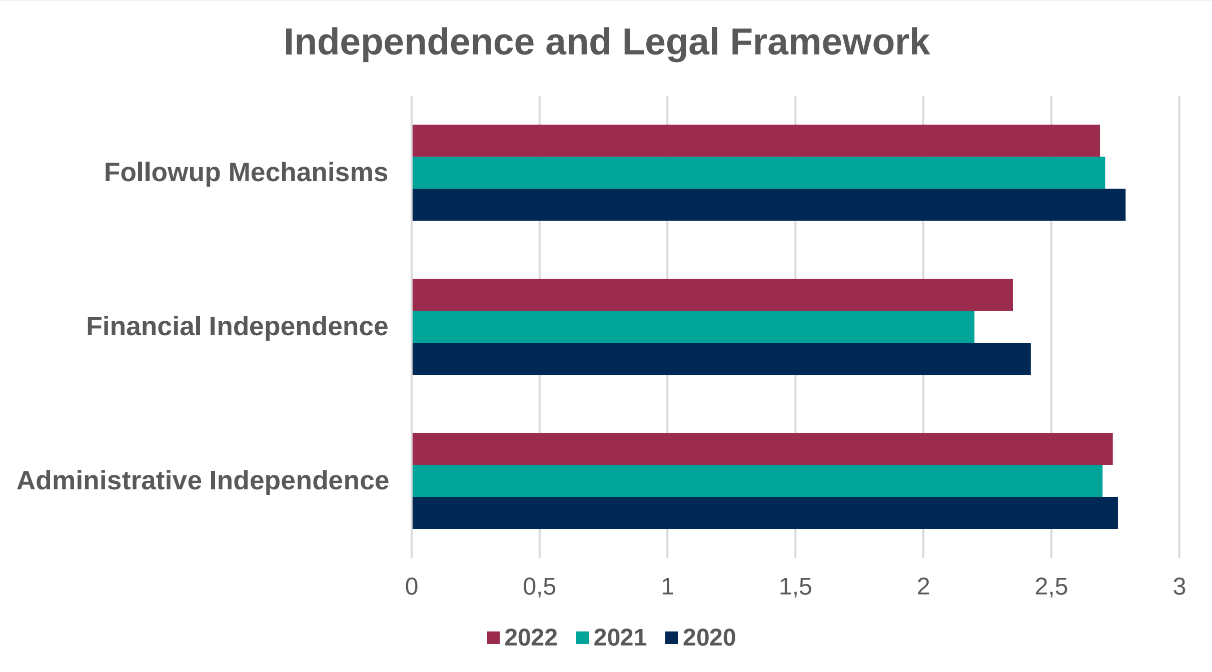

Figure 5-2: Independence and Legal Framework

Key challenges necessitating further coordinated capacitation work include strengthening the mandates and independence of SAIs, mechanisms to follow up on audit recommendations, oversight and accountability mechanisms of the SAI, and independence from an administrative and financial perspective. This is well emphasised in the 2022 ICBF report, which highlights that pressures on SAI independence remain on the organisational level and at individual heads of SAIs, partly due to outdated legislation, a failure to clearly define the independence of the Auditor General and administrative and financial autonomy.

5.2.3 Organisation and Management

The domain of organisation and management is about quality management, organisational planning processes, and management tools relating to leadership, management information, governance, and internal control systems. The elements included are:

a) Integrity and a Code of Conduct
b) Resource Management
c) Governance of the SAI
d) Organisation of the SAI
e) Strategic and Operational Planning

As shown in Figure 5-3 below, SAIs continued to improve in this domain, reflective of enhanced capacitation work targeted at leadership direction, strategic and operational plans, resource management, the establishment of good corporate governance structures, and other relevant internal control policies. However, the lack of or inadequacy of various systems and frameworks for quality management, risk management, monitoring and evaluation, integrity and ethics remain concerning.

Figure 5-3: Organisation and Management

5.2.4 Key Capacity Issues Identified in the ICBF Report

Following the issues highlighted in the preceding section of the ICBF report, we examine SAI capacity development issues as enunciated in the report. These are cross-cutting issues relating to SAIs enhancing their planning, implementation, and communication of audit results practices. These are clustered according to the three highlighted areas of internal QA processes: independence, legal frameworks, organisation, and management.

Internal QA processes.	• Prioritising capacity building for the QA function, as competent persons are often used to conduct audits rather than performance reviews. • Training competent quality assurance reviewers who can focus on all types of audits. • Appointing of IT audit QA reviewers. • Funding to address budget constraints to fill vacancies. • Planning by smaller SAIs, who do not have resources for full-time reviewers, for auditors to do reviews on a rotational basis before audit reports are issued. • Reviewing of all audit types by the internal QA function.

	• Information systems audit strategies that ensure SAI compliance (supporting other audits or conducted as compliance or performance audits).

Independence and Legal Framework	• Continuous engagements with continental bodies to prioritise and elevate SAI independence and raise awareness of the challenges. • Legal prescriptions for periodic reviews of the performance of heads of SAIs and/or (where relevant) members of jurisdictional control institutions by parliament or appropriate bodies. • Advocacy on the legal right to address parliament or the relevant parliamentary committee(s) on audit arrangements of any public financial operations not within their audit mandate. • There is a need to establish follow-up mechanisms to implement audit recommendations. • Limited oversight and accountability of the SAIs. • Engagement of external stakeholders, such as donors, development partners, the media and civil society organisations, is needed to understand the importance of an independent Auditor-General.

Organisation and Management	• There is an absence of established robust QA management systems. • Mechanisms must be developed to measure the extent to which top and senior managers demonstrate the values of their SAIs. • Development of one's own integrity and ethical frameworks is needed. • There must be robust strategic coordination of stakeholder engagement.

5.3 PFM-RF SAI Level TNA

TNA in SAIs involves systematically identifying the knowledge, skills, and competencies required by audit staff to perform their duties effectively. This analysis helps to identify areas where training interventions are needed to enhance the capabilities of audit professionals and strengthen the overall performance of the SAI. The AFROSAI-E 'ToT' concept of 'TNA' establishes the transversal training needs for SAIs at a strategic, managerial, and operational level. These are required for SAIs to reach ICBF level three in using broad-based PFM diagnostic tools to perform their audits annually.

To effectively implement the PFM-RF tool, a TNA was undertaken on the audit staff at the various SAIs based in target institutions, i.e., the key PFM implementing entities and critical ministries. The aim of the TNA was to:

a) Identify and review any previous training provided to the auditors on the PFM-RF tool.
b) Design the TNA framework and methodologies for the audit staff.
c) Identify and analyse the gaps in information, knowledge, and skills using the PFM-RF tool.
d) Formulate training strategies based on the assessment of training needs.
e) Identify the auditors, including the potential target groups, priority training topics, type of training, and appropriate timing and durations.
f) Identify and analyse any factors that may facilitate or prevent the provision and implementation of effective training for the target groups.
g) Identify non-training needs during implementation.

By conducting a TNA, SAIs can tailor their training programmes to address specific areas of improvement and enhance the overall professional development of their audit staff. This enables SAIs to build a skilled and competent workforce capable of fulfilling their roles in promoting accountability, transparency, and good governance.

Each country in the study submitted individual TNA reports, which were assessed at a consolidated level to determine underlying themes. The TNA process included surveys using electronic questionnaires, focus group discussions, interviews with PFM-RF experts and a review of secondary information such as the strategic plans and previous training data. A key output from the experts concerning training needs was the willingness to integrate the PFM-RF into regular audit work. This included the framework's inclusion in strategic planning or other related documents. However, this willingness did not necessarily translate into practical implementation. This calls for a greater focus on creating strong links between PFM audits and regular auditing.

Concerning the tool itself as well as its supporting documents, the findings on the weak engagement of auditees and the often-lacking inclusion of SMART recommendations in the PFM audit reports point to an imbalance in how the tool is communicated to user SAIs, focusing on the technical side of the tool with less consideration for engagement of and communication with stakeholders.

5.3.1 Underlying Themes

a) Execution Plan

Across the different SAIs, ToT champions are at various stages of implementing the key learnings from the ToT programme using an implementation plan. However, this was compounded by some champions not having the PFM-RF tool. Furthermore, challenges remained concerning awareness of the PFM tools at an institutional level, with strong advocacy required to conscientize executives or senior management to maintain that level.

> *…we had plans to implement the actual plan but had to move away from those plans and develop a new plan to raise awareness of the PFM-RF tool and how to use the tool within the SAI. We are mostly from performance audit and were not using the PFM-RF tool in our audits unlike the financial auditors…*

At least 40% of the respondents alluded to having been trying to schedule such an awareness session with senior management for over six months without much progress. In addition, timing constraints also proved to be a hurdle as resources were allocated earlier in the first half of the year, while the intended training intervention was in the second half, and this training was not foreseen in the budgetary processes, adversely affecting the implementation process.

> *…the team has had challenges with getting management together to do the awareness session with GIZ and AFROSAI-E to come in for a PFM-RF Retreat. As there were public hearings and the dates clashed with the dates of the planned sessions. …*

Similarly, in instances where awareness was conducted, it proved challenging to get buy-in from management, and the champions recorded low response rates from within the SAI on the awareness survey on the PFM-RF tool.

b) Levels of TNA Performance

TNA is generally carried out at three levels, that is, at the SAI, division/team, and individual level. It must be carried out at all three levels to achieve organisational and individual objectives. All respondents confirmed that the TNA was conducted at an institutional level, as this was the identified gap before addressing the other levels. Consequently, there is scope for additional TNA at the divisional and individual levels. An interesting dynamic that continued to be brought up was the SAI's human resources department's (HRD) role in the TNA process. For instance, in one of the SAIs, no one from the team that attended the training works in HRD or as part of the learning and development department took part; typically, the custodians of training and development. Consequently, implementation depended on getting buy-in from HRD to push through the activities in implementing changes.

c) Identifying Performance Gaps

When doing a TNA, evaluating the SAI's performance against, for example, the ICBF and SAI PFM reports regarding training and development is important. However, only 20% of SAIs could draw a clear link between the SAI's strategic goals, indicating the SAI's need to adopt and perform PFM audits using the PFM-RF tool. Inconsistencies on the ground at the SAIs evidenced this. For instance, at a strategy level, SAIs wanted to adopt and use the PFM-RF tool. However, in practice, the SAIs could not implement the tool, nor were there clear mechanisms to enforce implementation. The inability to fully implement the PFM-RF tool was widely acknowledged as a weakness, resulting in SAIs failing to meet their strategic objectives to ensure audit service excellence, quality, and institutional capacity and capability.

d) Skills Level and the Training Gap

Regarding the current SAI skills gap in understanding the performance of the PFM-RF tool, across the SAIs in the study, it was clear that awareness levels of the PFM-RF tool were very low and that most of the staff were either not aware of the tool or had not been trained to use the tool. Thus, most of the staff did not know the importance of the tool and its impact on PFM audits. For example, at one of the SAIs, out of an audit pool of 300, only 12 auditors had been trained on the tool – showing a very low 4% penetration level.

To improve awareness and usage, the target for training should be not only the auditors but every department within the SAI so that everyone contributes to the performance/objective of the tool.

The need for additional coaching and mentoring covering audit team leaders and the audit team cannot be overemphasised. Mentorship will be essential as they interact with the audit team leader daily. This will create an environment for easy communication and sharing perspectives and experiences, which can save time. Regarding training interventions, as shown in Figure 5-4, there is a strong preference for a mix of on-the-job training and formal learning across all three levels of the SAIs.

Priority Capacitation Areas to Enhance the PFM-RF Process

- Understanding of the interdependency between government plans, budgets, and SDGs.
- Stakeholder engagement and client relations.
- General Macro Economic Analysis and forecasting.
- Understanding of SDGs implementing agencies and the SAI role in ensuring the successful implementation of SDGs.
- Root Cause Analysis.

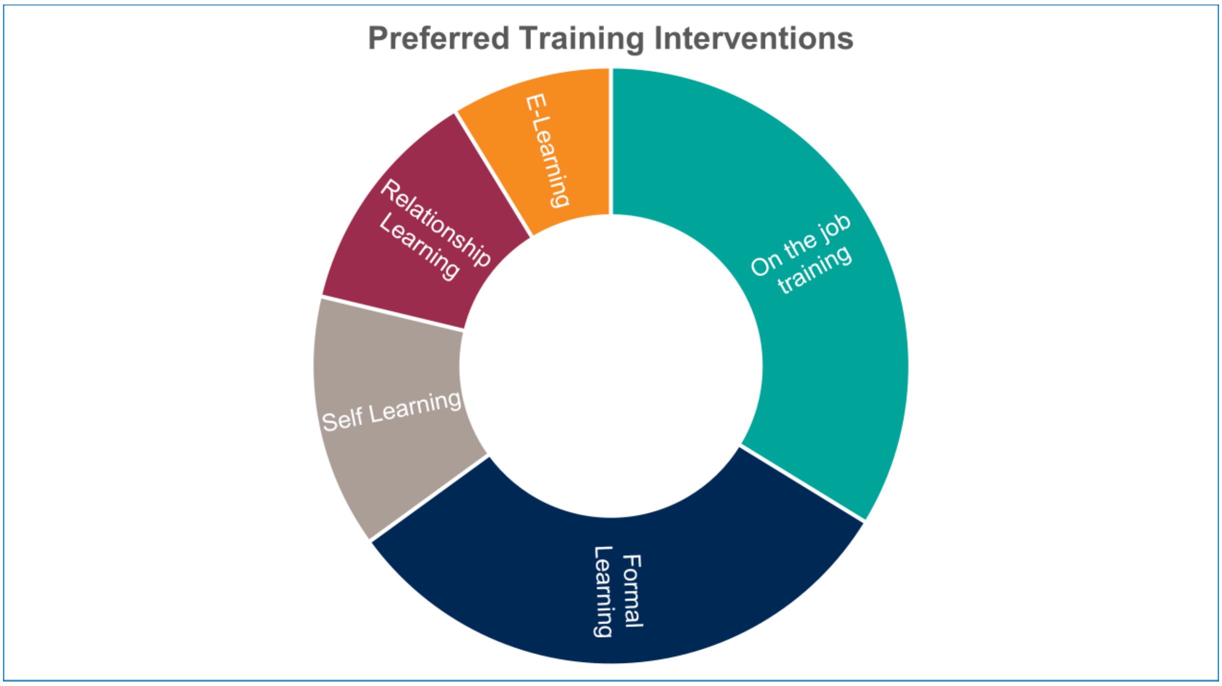

Figure 5-4: Preferred Training Interventions

6. RESOURCE-BACKED PUBLIC DEBT - CURSE OR A BLESSING IN DISGUISE

6.1 Introduction

The effect of government interventions on economic growth through taxes, public debt and spending continues to be a central subject of economic policy in the global economy[1,2]. According to the International Monetary Fund (2013)[3], public debt refers to the contractual financial commitments whereby the central government has pledged to repay creditors in the future, including the principal amount and accumulated interest.

Public debt is subdivided into domestic and foreign public debt based on the location of debt holders, the currency in which the debt is denominated, and whether the debt was issued on the international or domestic debt market. A 2023 publication by the African Forum and Network on Debt and Development (AFRODAD) raised warnings that the proportion of African governments' revenue devoted to debt payment is rising due to a rise in debt service costs, with at least 20 African states committing at least 20% of their yearly income to repay public-sector external debt.

[1] Alzghoul, A., Al_kasasbeh, O., Alsheikh, G., & Yamin, I. (2023). The Relationship Between Savings and Investment: Evidence From Jordan. International Journal of Professional Business Review, 8(3), e01724-e01724.
[2] Al-kasasbeh, O., Alzghoul, A., & Alghraibeh, K. (2022). Global FDI inflows and outflows in emerging economies Post-COVID-19 era. Future Business Journal, 8(1), 1-9.
[3] International Monetary Fund. (2013). Public sector debt statistics: A guide for compilers and users. Washington, DC.

Although the causes and influences of foreign public debt have been extensively discussed in the past, the recent emergence of RBPD in both developed and emerging economies, as well as the wide variation in economic growth rates across world economies, have sparked renewed interest among development economists in the impact of such RBPD on economic growth.

6.2 What is Resource-Backed Public Debt (RBPD)?

RBPD refers to a form of public debt where a country pledges its natural resources, such as oil, gas, or minerals, as collateral for a loan. Essentially, the lender provides financing to the country, and in exchange, the government guarantees the loan by pledging its natural resources.

> *Public debt refers to the amount of money that a government owes to its creditors, which can include individuals, companies, and other countries. RBPD debt, on the other hand, is a type of debt where a government pledges natural resources or other assets as collateral for the loan.*

Thus, RBPD describes using a country's natural resources to serve as either a direct source of repayment or an underlying guarantee of repayment regarding the loans[4]. This kind of borrowing is typically undertaken by a central government or a state-owned company with lending from another government, a state-owned company, the private sector and/or international financial institutions. The COVID-19 pandemic has generated considerable focus on these types of transactions when considering widespread debt sustainability challenges in developing countries and volatility in commodity prices.

The World Bank report titled Resource Financed Infrastructure: A Discussion on a New Form of Infrastructure Financing[5] focuses on the financing of such debt through a resource finance infrastructure (RFI) arrangement, whereby a loan for current infrastructure construction is securitised against the net present value (NPV) of a future revenue stream from oil or mineral extraction, adjusted for risk. The emergence of the RFI model can be partially understood as a reflection of the gap in risk tolerance and expected return between the extractive and the infrastructure sectors. The potential benefits of RBPD for African countries include the following:

a) *Lower Borrowing Costs*: RBPD can potentially reduce the cost of borrowing for African countries. This is because lenders may be more willing to provide financing if they have collateral they can fall back on in the event of default.

b) *Diversification of Financing Sources*: RBPD can provide African countries with an alternative source of financing that is not solely reliant on traditional debt financing. This can help reduce the risks associated with overreliance on external borrowing.

[4] Mihalyi, D., Hwang, J., Rivetti, D. and Cust, J., 2022. Resource-Backed Loans in Sub-Saharan Africa.

[5] Harvard Halland; John Beardsworth; Bryan C Land; James Schmidt. 2014. Resource financed infrastructure: A discussion on a new form of infrastructure financing. A World Bank Study. Washington, DC: World Bank Group. http://documents.worldbank.org/curated/en/394371468154490931/Resource-financed-infrastructure-a-discussion-on-a-new-form-of-infrastructure-financing

c) *Increased Transparency*: RBPD can increase transparency in debt management by providing a clear and tangible asset that can be tracked and valued. This can help reduce the risk of corruption and mismanagement of funds.

d) *Enhance Sovereign Ratings*: RBPD can potentially enhance the sovereign ratings of African countries, which can lead to lower borrowing costs in the future.

6.3 Implementation Challenges

Given the various issues and governance challenges, overreliance on external borrowing and the associated risks of debt sustainability have led to a call for increased oversight of these project financing arrangements. The governance challenges related to such funding projects include a lack of transparency and accountability, a lack of respect for human rights, limited capacity to assess the risks and manage the issues associated with these projects, the presence of corruption, a lack of observance of the legal concept of the rule of law, restrictions on freedom of speech and limited community engagement.[6]

Furthermore, some specific concerns include the process used to select the construction companies, including no bid or direct assignment contracts, increased national debt, inflated pricing, shoddy work by construction companies, and poor working conditions.[7] In addition, the valuation of natural resources is also a challenge, given the volatility of commodity prices. This can make it difficult to value the collateral being pledged accurately.

As if this is not enough, in many African countries, the ownership of natural resources is often unclear, thus making it difficult to provide a clear and tangible asset as collateral. This is compounded by political instability, resulting in traditional lenders being reluctant to fund such projects, which can impact the valuation of the collateral. There are also environmental concerns associated with RBPD[8]. The extraction of natural resources can have a negative impact on the environment, which can lead to social and environmental costs.

6.4 Transversal Risks and RBPD

RBPD can also be vulnerable to corruption, as it is often negotiated behind closed doors and may involve large sums of money changing hands. Mihalyi *et al.* (2022) reviewed data on ten Sub-Saharan

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[6] Ma, H.; Zeng, S.; Lin, H.; Chen, H.; Shi, J. The societal governance of megaproject social responsibility. Int. J. Proj. Manag. 2017, 35, 1365–1377.
Stevens, P.; Glada Lahn, G.; Kooroshy, J. The Resource Curse Revisited; Chatham House: London, UK, 2015.
Vanclay, F.; Hanna, P. Conceptualising company response to community protest: Principles to achieve a social license to operate. Land 2019, 8, 101.

[7] IMF. Guide on Resource Revenue Transparency; International Monetary Fund: Washington, DC, USA, 2005; Available online: https://www.imf.org/external/pubs/ft/grrt/eng/060705.pdf
Lin, J.; Wang, Y. New structural economics and resource financed infrastructure. Pac. Econ. Rev. 2016, 21, 102–117.

[8] Purwins, S., 2023. Same Same, but Different: Ghana's Sinohydro Deal as Evolved 'Angola Model'. Insight on Africa, 15(1), pp.46-70.

African countries on the World Bank's Debt and Transparency Heatmap. They concluded that countries that borrow using resource-backed loans have weaker debt disclosure practices.

This can lead to a lack of transparency and accountability, making it challenging to ensure the funds are used for the country's benefit. The lack of transparency on RBPDs has several implications. Firstly, these deals are often highly complex and are therefore susceptible to a poor evaluation of their risks. Secondly, given the limited competition for providing such loans (few lenders offer them), there is also a risk of poor negotiation outcomes. In both cases, the risk is higher when the outcome is subject to limited scrutiny. Finally, RBPDs may use transaction structures not reflected in standard debt statistics or confer undisclosed seniority or payment advantages to their lenders, leading to other creditors' mispricing of the country's risk.

RBPD agreements must become more transparent and be subjected to the same oversight mechanisms as other infrastructure development projects to maximise the benefits they yield for host countries' populations. Finally, as this paper highlights, the broad gamut of risks associated with these agreements must be fully considered by their respective parties and the third-party actors who analyse them, such as SAIs.

SAIs play a crucial role in RBPD arrangements by ensuring transparency and accountability in managing the pledged resources and associated revenues. SAIs conduct audits to verify whether the revenue generated from the specified resources is accurately accounted for, collected, and used for debt repayment, as intended. They examine the legal framework, contracts, financial statements, and other relevant documents to assess compliance with applicable laws, regulations, and contractual obligations.

Additionally, SAIs assess the efficiency and effectiveness of the government's resource-backed debt management, including utilising funds borrowed through RBPD. They evaluate the government's capacity to monitor and control the pledged resources, assess the risks associated with RBPD arrangements, and provide recommendations for improvement to enhance governance and mitigate potential risks.

By conducting independent audits of RBPD, SAIs promote transparency, accountability, and the sustainable management of natural resources. Their oversight helps minimise the risks of corruption, mismanagement, and misuse of resources, ensuring that the benefits derived from resource-backed financing are maximised and effectively used for the country's development.

7. RECOMMENDATIONS AND CONCLUSIONS

The recommendations are as follows:

Adopting and awareness of the PFM-RF tool remains a challenge across the SAI. While there is evidence of the use of the tool, it is not always clear that the tool is being adequately integrated into the strategic decision-making process of SAIs.

There is a need to prioritise specific capacitation areas to enhance the PFM-RF Process. This includes a focus on the following:

a) Understanding of the Interdependency between government plans, budgets, and the SDGs,
b) Stakeholder Engagement and Client Relations.
c) General Macro Economic Analysis and Forecasting.
d) Understanding of SDGs implementing agencies and the SAI's role in ensuring the successful implementation of SDGs.
e) Root Cause Analysis.

Regarding RBPD, there is a need for SAIs to be capacitated to audit resource-backed loans. This would go beyond assessing the documentation, agreements, and financial records related to the specific resource backing the debt by determining the money's value for such transactions. Increased advocacy on RBPD and incentives for debt transparency through dialogue between SAIs and the national government should be encouraged.

Annexure 1: Selected Case Studies on Resource-Backed Debt in Sub-Saharan Africa

A. Zambia and Resource-Backed Public Debt

Zambia has the second-largest number (after Angola) of Chinese construction firms with contracts to work on and operate Chinese loan-financed projects. Moreover, Zambia has agreed lines of credit with at least 18 distinct Chinese lenders. Access to natural resources plays a central role in the repayment conditions of some Chinese loans. China often offers resource-backed loans to resource-rich countries, using commodities as a repayment method or collateral. This type of loan is often predicated on the future production of natural resources such as cocoa, tobacco, oil, or copper.

The large number of stakeholders means this debt has little or no top-down coordination or strategic oversight[9]. The China Africa Research Initiative (CARI) estimated that Zambia's loan commitments to all Chinese creditors at the end of 2019 amounted to close to 43% of 2019's gross national income (GNI). By contrast, the average for Africa was 10%. This multiplication of stakeholders has created fierce competition for infrastructure contracts in Zambia. Zambia has had more bailouts from the Paris Club (an informal cartel of official bilateral creditors) and China than most other African countries. Zambia's history of debt cancellations probably exacerbated its moral hazard risks.

As of 2021, Zambia has $6.4 billion in resource-backed debt. This debt is backed by the country's mineral resources, particularly copper. The repayment schedule for this debt varies, depending on the specific loan agreements, but some of the debt is due to be repaid in the next few years. However, Zambia has been struggling with its debt burden and has already defaulted on some of its loans. The government is in talks with creditors to restructure its debt and find a sustainable path forward.

Under the Common Framework, with China as the co-chair of the creditor's committee, all of Zambia's creditors, both governments and the private sector, are negotiating debt restructuring together.[10]

B. Kenya's Resource Debt Woes

The $5.3 billion Standard Gauge Railway (SGR) project, completed in two phases between 2013 and 2019, was funded by three loans from China's Exim Bank on semi-concessional terms and constitutes 68% of Kenya's bilateral debt and just under one-fifth of its total external debt stock[11].

[9] IMF (2022), 'Zambia: Request For An Arrangement Under The Extended Credit Facility', press release, 6 September 2022, https://www.imf.org/en/Publications/CR/Issues/2022/09/06/Zambia-Request-for-an-Arrangement-Under-the-Extended-Credit-Facility-Press-Releasclass="•-No-break">e-Staff-523196.

[10] https://issafrica.org/iss-today/zambia-on-the-brink-of-historic-debt-relief-deal

The SGR connects Nairobi with the port town of Mombasa on the Kenyan coast and Naivasha in the Great Rift Valley. Constructed by the China Road and Bridge Corporation (CRBC), Kenya received a loan of Sh324 billion (USD 3.2 billion) from China's Exim Bank – the largest item in Kenya's external debt. SGR operations started in 2017. The SGR project has been criticised for its opaque contractual arrangements and repayment terms. Moreover, the economic viability of the project has been questioned. The railway continues to be operated partly by the Chinese contractor AfriStar, which CRBC owns.[12]

Lack of transparency on the deal resulted in rumours that Kenya Ports Authority revenues and assets would be used to guarantee repayment to Exim Bank in case of a default on the SGR project loans. However, in 2022, the new administration released the financing agreements to allay the fears. It was highlighted that Kenya had agreed to waive its sovereign immunity, a standard clause in case of disputes in such deals. This was widely interpreted to mean that the key strategic port of Mombasa was at risk of seizure by China.

A 2021 study by the Chinese Research Africa Initiative highlighted that funding was concentrated on transport and power due to the resource-backed model of lending policy that China applies to most of its loan commitments. This policy requires that borrowing countries commit future revenues earned from projects commissioned by China to pay loans secured by Chinese creditors. Therefore, bigger projects, especially in transport and power, are more likely to secure the projected revenues. The lending model has helped high-risk borrowing countries secure loans, complete large-scale projects, and assure the creditors of repayment. In the event of erratic economic phenomena, such as commodity price fluctuations that may lead to defaulting repayment, the lender bears the risk of debt default since the range of price fluctuations is calculated in the loan.

C. Ghana's Sino-hydro Deal

In 2018, the Government of Ghana and China's Sinohydro arranged loans to fund infrastructure projects, with Ghana using revenue from refined bauxite to repay the loan. In terms of the deal, Sinohydro is investing US$2 billion in infrastructure development in return for refined bauxite over 15 years. Ghana committed to expanding its bauxite-mining activities and building refineries over three years. Purwins (2023) asserts that Ghana's bauxite gained importance between World War I and World War II, and it played a major role in the Volta River Project, which included a hydroelectric dam, an aluminium smelter to process Ghanaian-mined bauxite, new cities, a deep-sea harbour, and other infrastructural investments.

safrica.org/iss-today/zambia-on-the-brink-of-historic-debt-relief-deal"https://issafrica.org/iss-today/zambia-on-the-brink-o

Ghana's parliament approved the project in terms of the master project support agreement (MPSA). The parliament also approved deferred payment agreements (DPAs) and engineering procurement and construction (EPC) contracts (IMF 2019[13]). Under the MPSA, the government defined priority areas that need to be developed and executed by Sinohydro. Separately, through an Act of Parliament, a special purpose vehicle (SPV), the Ghana Integrated Aluminium Corporation (GIADC), was set up to develop and manage the country's bauxite reserves (IMF 2019). Under the DPAs, all financial obligations to Sinohydro will be transferred from the Ministry of Finance to GIADC. Therefore, 'in theory' under this structure, the government has no financial liability to Sinohydro, and the Chinese company is not directly involved in bauxite mining or the sale of refined resources (Purwins, 2023).

f-historic-debt-relief-deal

nd Eighth Reviews Under the Extended Credit Facility Arrangement and Request for Waivers of Nonobservance of Performance Criteria.' IMF Country Report No. 19/97. https://www.imf.org/~/media/Files/Publications/CR/2019/1GHAEA2019001.ashx