

# **Donor Co-ordination and Aid Effectiveness in Mozambique**

**Discussion Document: May 2005**

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## **Executive Summary**

The multi-donor budget support system (MDBS) in Mozambique is sophisticated and is functioning reasonably well, for an innovative process. However, there are critical systemic issues which need to be addressed, both with regard to the MDBS system and overall aid management in Mozambique.

Firstly, donors are failing to adequately reduce and streamline conditionality within the Performance Assessment Framework (PAF). There is a lack of clarity around the implications for the Government of Mozambique (GoM) of failing to reach jointly agreed targets or for breach of the underlying principles of the Memorandum of Understanding (MoU). This is compounded by the ongoing proliferation of bilateral conditions and administrative requirements amongst G16 members.

Secondly, the MDBS system appears to be giving the GoM more space to negotiate realistic and achievable performance targets. Yet, despite the rhetoric of mutual accountability, there is still a clear asymmetry of power and accountability between the G16 donors and the GoM. The system is making the GoM more accountable to donors, possibly at the expense of GoM accountability to civil society and Parliament.

Thirdly, civil society and Parliament have limited capacity and need substantial and sustained support if they are to play effective roles in holding the GoM accountable for policy development and implementation. The G16 donors and the international finance institutions have a role to play in ensuring that their processes do not undermine systems of domestic accountability, including budget processes. Trócaire and Christian Aid propose a range of actions to increase space and capacity for civil society and parliamentary engagement and oversight in national planning and financial management.

Finally, the International Monetary Fund (IMF) has failed to align its Poverty Reduction and Growth Facility (PRGF) to both the content and temporal cycles of GoM policy, raising questions as to how far the PARPA can be GoM-owned when it is significantly predetermined by a PRGF. Its dominant role in setting the parameters for GoM policy is given further weight by the inclusion of an off-track IMF programme as potential grounds for suspension of the MoU. This leaves the GoM in a permanent state of vulnerability. We propose that donors affirm that an off-track PRGF will not result in automatic budget support suspension.

Christian Aid and Trócaire also propose the elaboration of macro-economic policy for the government's new poverty reduction strategy - PARPA II - in a multi-stakeholder macro-economic forum, where the IMF would be obliged to share and justify its assumptions and policy advice. Contested policy should be subject to independent analysis. In the longer-term, we propose that the GoM, G16 and other stakeholders should explore options for IMF membership of a MDBS system which would mean that the IMF was mutually accountable to the GoM and its membership at a country level, rather than being accountable only to its Board in Washington.

## **Recommendations**

- **GoM planning and aid management**

The GoM needs to develop an overall external assistance management strategy. This should take the form of a joint agreement with all donors (not just budget support donors) on aid modalities, coordination, harmonisation and conditionality. It should include monitorable

targets for donors' performance and a clear articulation of the consequences for the GoM of failure to comply with the principles of this agreement. The obvious donor coordination framework would be the UNDP-led Development Partners Group.

To address the lack of articulation between line ministry and central government (e.g. Ministry of Planning and Finance (MPF)) harmonisation efforts, the GoM needs to show stronger leadership in developing a coherent planning system to include all ministries. This is linked to the need for donors to subordinate policy dialogue at sector level to the GoM's dialogue with its line ministry. Donors must ensure that their interventions reinforce rather than undermine coherence in overall national policy-making.

As PARPA II is under development, this is an important opportunity to implement the above recommendations.

- **The MoU and PAF**

Predictability is seriously hampered both by donor failure to adhere to disbursement agreements in the MoU and the liberal use of exceptions in Annex 10. Donors must be held to account on their commitment to reduce these exceptions.

The current target in the PAF for eliminating bilateral conditional and administrative and reporting requirements is entirely inadequate. A revised target should be adopted as part of annual transparent reporting on each donor's individual performance under the Programme Aid Partners' (PAP's) PAF.

Conditions attached to projects and programmes which are outside of the MoU also need to be streamlined and harmonised, within an overarching system as in Recommendation 1. Overall PAF conditionality should be reduced and streamlined in accordance with the GoM's priority areas under PARPA. Agreement should be reached on both the criteria for and a reduced upper limit of PAF conditions.

- **The MoU and Mutual accountability**

The imbalance in accountability between the GoM and the G16 in the MoU needs to be addressed.

The underlying principles – and particularly that of adherence to pursuing sound macro-economic policies, with reference to an on-track IMF programme or equivalent judgement, should be clarified. All donors should reach agreement with their capitals best word headquarters that an off-track IMF programme will not result in automatic suspension of budget support. This should be captured in the MoU.

The PAP's PAF needs to be simpler, more progressive in terms of commitments and it should contain targets for each commitment and indicator. Individual donor performance should be tracked, rather than an overall assessment of the performance of the donors as a group.

Further mechanisms to ensure a high degree of commitment of donors under the MoU should be explored – including the suspension of under-performing G16 donors or delivery of a minimum per cent of aid flows in budget support.

Annual reporting on the PAP's performance should be carried out independently and made publicly accessible. At a minimum, the report should be presented to the Parliament and Poverty Observatory. A summary in accessible language should be printed in national newspapers also. Donors should also report to their home parliaments on targets in the Paris declaration on aid effectiveness and against targets set locally – such as those in the PAP's PAF.

- **Capacity Development and the GoM**

There is a need for greater cooperation and the establishment of agreed, coordinated systems (including joint funding mechanisms) for capacity development in the GoM. It is vital that capacity development is long-term and prioritises the government's role in selecting both priorities and processes for capacity development, including the selection of consultants. The commitment of the PAP's PAF to take this issue further needs to be followed up but it also needs to be articulated with capacity development efforts by non-G16 donors. An appropriate forum for discussion may be the UNDP / World Bank-led Development Partners Group.

- **The Role of the IMF**

In the short term, there is a need for a formal agreement between the GoM, parliament and IMF that existing PRGF targets and mechanisms will not predetermine the outcome of the PARPA II.

IMF advice to the GoM on the development of the PARPA macro-economic framework should be subject to scrutiny by other stakeholders, including Parliament, civil society members (non-governmental organisations (NGOs), private sector and academics), and other donors. The IMF should justify its assumptions and policy advice to a multi-stakeholder macro-economic working group and to Parliament. It should illustrate how feedback from this group and Parliament impacts on its policy advice going forward.

The GoM should work together with this multi-stakeholder group to identify areas where independent analysis is warranted, particularly where IMF macro-economic policy proposals are likely to have an impact on poverty reduction.

On finalisation of PARPA II, a new PRGF programme (if one is deemed necessary by the GoM) should be drawn up based only on policy and targets in the PARPA II.

In general, IMF conditionality should be contained in the overall donor conditionality framework, and in the G16 PAF. It should be reduced to include only verifiably macro-critical issues which are drawn from the PARPA / PES.

- **The World Bank**

There are concerns that while the Bank is coordinating Poverty Reduction Support Credit (PRSC)-related conditionality within the G16, the reform agenda promoting privatisation and deregulation is instead being pursued through the Bank's project lending. The Bank should commit to streamlining and alignment of all its lending and activities, under a joint agreement with all donors (not just budget support donors) on aid modalities, coordination, harmonisation and conditionality, as above.

There is a clear need for parliamentary scrutiny of World Bank loan agreements and their policy content. Given the lack of capacity for analysis and debate in Parliament, a broader strategy of scrutiny of Bank lending is required. This should be subject to the same scrutiny suggested for IMF policy under the proposed multi-stakeholder macro-economic group, above.

- **Civil society**

The GoM needs to undertake initiatives to make the PES (annual budget implementation plan) and the annual report on the PES - BdoPES - more accessible and digestible to civil society, using appropriate media and language, along with provincial / district-level consultation. The GoM and PAPs need to agree how to make the PAF accessible in these fora.

With regard to the MDBS, the GoM and G16 should create more space for civil society participation in joint and mid-year discussions, without overloading the process. Dialogue sessions with civil society should be held before and at least twice during these reviews, with access by civil society to draft texts. A civil society declaration at the end of the reviews should be attached to the Aide Memoire.

In the meantime, the GoM must develop a comprehensive and meaningful strategy for participation in PARPA II decision-making, as part of the institutionalisation of democratic governance.

A wider, deeper and more sustained effort by donors to support civil society is needed. This should be based on an agreed approach to capacity development between representative civil society groups such as the G20, and donors with a commitment to supporting civil society.

- **Parliament**

Donors should engage with Parliament under specific programmes to strengthen capacity to carry out their legitimate functions.

There is also a need for donors to create more space for parliamentary oversight through opening up the processes around the MoU to parliamentary scrutiny. The PAF should be formally presented to parliament as part of the PES, while the formal or informal mechanisms to present the PAP's PAF should also be determined.

## 2. Background to this report

Mozambique's multi-donor budget support system is frequently highlighted as a model of good practice and one which is in keeping with the Rome Declaration on Aid Effectiveness<sup>1</sup>. Indeed, the Mozambican model of donor accountability was specifically referred to in the draft Declaration for the Paris High Level Forum on Aid Effectiveness in March 2005, although the reference was subsequently removed.

In order to study this model in more detail, policy staff from Trócaire and Christian Aid undertook a research trip to Mozambique to ascertain the strengths and weaknesses of the Mozambican multi-donor budget support system. It was undertaken to look in particular at: the relationship between the multi-donor arrangement and the PRSP (PARPA); the role of civil society in a policy framework increasingly dominated by a group of budget support donors; and the role of the IMF in the development and implementation of macro-economic policy.

This document is the product of that research trip. It is intended as an informal report to inform policy development in our agencies and to feed into policy and advocacy positions with respect to, inter alia: ongoing reviews of PRSP and conditionality at the World Bank and IMF, debates on aid modalities in the UK & Ireland, and development of strategies for civil society and parliamentary capacity building. It is not a position paper, but aims to develop internal thinking on aid effectiveness, accountability, conditionality and participation, through the lens of a country case study.

### Methodology

The research processes included secondary research and interviews with key stakeholders in Mozambique. This included bilateral and multilateral donors, international financial institutions, government representatives, parliamentary representatives and civil society. A full list of interviewees is in Appendix I and reference documents in Appendix II. Basic reference documents included: a Baseline Survey of donor performance with respect to alignment, harmonisation etc., carried out by Gerster and Harding in 2004; a Learning Assessment of the April 2004 Joint Review carried out by the same consultants; and the results of an OECD Development Assistance Committee (DAC) Survey carried out in preparation for the Paris High Level Forum on Aid Effectiveness on Feb 28 – March 2<sup>nd</sup> 2005.<sup>2</sup>

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<sup>1</sup> The 'Rome Declaration on Harmonisation' was issued in Italy on 25 Feb 2003 by heads of multilateral and bilateral development institutions, international financial institutions and developing countries. Progress in implementation of the Rome Declaration and further commitments to aid effectiveness were developed at the second High Level Forum on Aid Effectiveness and Harmonisation in Paris on Feb 28 – March 2<sup>nd</sup> 2005.

<sup>2</sup> OECD – DAC Survey on Progress in Harmonisation and Alignment 2004 – Mozambique Country Chapter.

### 3. Mozambique and aid - background information

The GoM is the recipients of one of the highest per capita ODA in Africa. Net ODA rose sharply in 2002, from 29.8% of GNI in 2001 to 55.4% of GNI in 2002. However it fell again to 25.2% of GNI in 2003. Total disbursements were US\$877m, \$933m, \$2,054m and \$1,033m in 2000 – 03 respectively.<sup>3</sup>

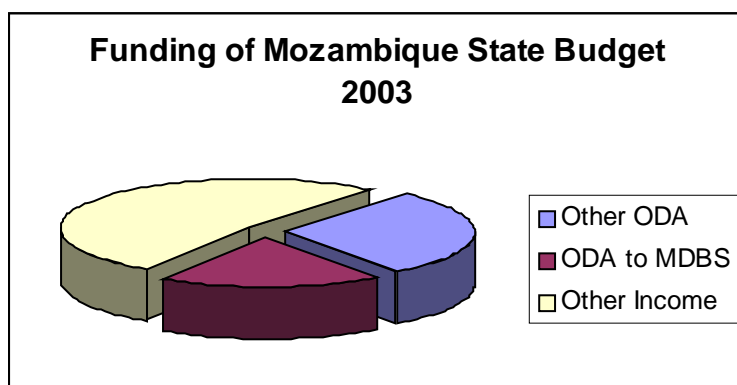
**Table 1: Top ten donors in 2002 - 03<sup>4</sup>**

Donor	US\$ million
France*	240
Italy*	231
IDA*	159
US	148
Germany*	134
EC*	115
Denmark*	60
UK*	56
AfDB	54
Japan	53

\*Budget support donor

Out of total ODA to Mozambique, programme support accounts for c. 33%, leaving two-thirds of all aid delivered through project support.

In 2003, ODA funded 48% of the official state budget<sup>5</sup>. Budget support accounts for 18 – 19% of the state budget<sup>6</sup>. The GoM intends to reduce dependency on aid to around 25% of budget expenditure by 2010. The share has already been reduced from 70% in 1995 – 96.



The GoM also wishes to see programme support take the place of project support. Prime Minister Luisa Diogo stated at the signing of the MoU in April 2004 that the GoM would like to attain a programme aid share (including sector support) of approximately 60% of total aid disbursements in the medium term, with projects and other forms of emergency assistance

<sup>3</sup> <http://www.oecd.org/dataoecd/23/7/1882362.gif> - see Appendix II for detail.

<sup>4</sup> Ibid.

<sup>5</sup> Gerster and Harding (2004, p. 8), 'Baseline Survey on PAP Performance in 2003'.

<sup>6</sup> Interview, Jose Sulemane, MPF, January 2005; informal communication, T.Killick, March 2005.

constituting the remaining 40%.<sup>7</sup> In interviews for this report, GoM representatives pointed out that budget support is still a relatively low share of aid, compared to their optimal level.<sup>8</sup>

### **Budget Support**

As highlighted in Table 2, the financial commitment to budget support varies considerably across all donors. Some are substantially committed, delivering 33 – 50% of their aid through this modality, while other have smaller volumes and shares of aid at stake. Of the ten largest donors (Table 1), the US, AFDB and Japan are not in the G16.

**Table 2: Per cent of donor aid given as direct budget support in 2003**

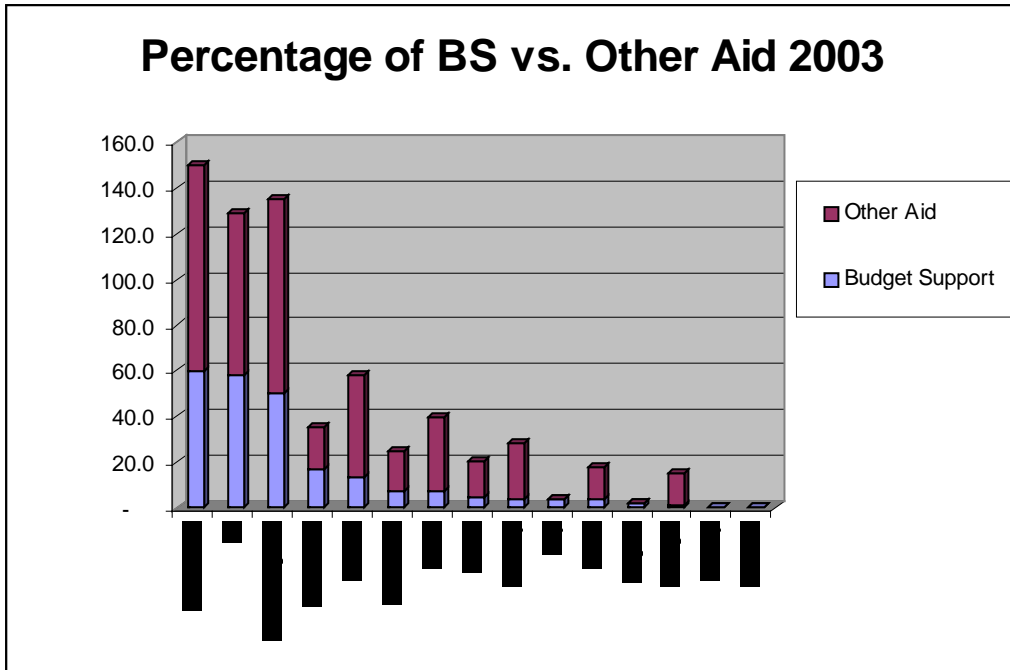
<b>Donor</b>	<b>Budget support given (\$ million)</b>	<b>Percent of total aid given as budget support*</b>
World Bank	60	40%
European Commission	58	45%
United Kingdom	50	37%
Netherlands	16.8	48%
Sweden	13.3	23%
Switzerland	7.4	30%
Ireland	7.2	18%
Finland	4.8	23%
Germany	4.2	15%
Italy	3.8	N/a
France	3.6	20%
Belgium	2.4	N/a
Portugal	1.5	10%
Norway	N/a	20%
Denmark	N/a	N/a
Total budget support	233	

\*Source: Gerster and Harding (Baseline Survey) 2004, p. 9 (approximate figures).

<sup>7</sup> Gerster and Harding (2004a, p.8); Gerster and Harding (2004, p. 6).

<sup>8</sup> Jose Sulemane, MPF, interview, Jan 2005.





### On & off-budget support

A substantial portion (two-thirds) of all donor aid is delivered off-budget (i.e. not spent through or declared in the state budget). This is highly significant and is one of the core issues in relation to aid coordination in Mozambique.

According to Gerster and Harding's Baseline Study (2004, p. 9):

- 2 Programme Assistance Partners (PAPs) in the G16 have all support on-budget (World Bank), or all except NGOs / private sector support (Sweden);
- 7 PAPs intend to increase on-budget share, mainly by strengthening programme aid (Belgium, Denmark, Germany, Italy, Netherlands, Switzerland, UK)
- 4 PAPs require clarifications of reporting requirements (Finland, France, Ireland) or of the implications of moving more on-budget (EC);
- 1 PAP is not considering further measures (Portugal)

### Multi-year arrangements

The commitment to multi-year arrangements also varies considerably among the G16 donors. The 2004 baseline study carried out for the then-G15 found that 12 of the 15 donors have multi-year arrangements in place. However, three donors (Belgium, France, Germany) have arrangements of only two-year durations. A further eight have three-year arrangements and only one (EC) has four years' budget support in place. The World Bank has a four-year Country Assistance Strategy. The three donors that did not have multi-year arrangements in place in 2003 indicated that they would introduce them in the near future. No PAPs have a rolling multi-year arrangement.

The PAP's PAF commits the G16 to improve predictability by committing BS / Balance of Payments support in line with the GoM planning horizon (medium term expenditure framework) and on a rolling basis. There are no specific annual targets set however.

## 4. Brief overview of MDBS system

### 4.1 Evolution of system

There has been donor co-ordination around budget support and programme aid since the mid-1990s, which became more formalised in 2000 with the Joint Donor Programme for Macro-Financial Support which involved 6 donors. By April 2004, a new Memorandum of Understanding signed by 15 donors (known as the G15) and the Government of Mozambique (GoM) superseded this Joint Donor Programme. In February 2005, the number of donors signing up to the MoU increased to 16, with Canada's accession to the group.<sup>9</sup>

A series of events between 2000 – 2003 led to a reframing of the budget support framework and the conditions around it. Firstly, a banking crisis involving serious fraud and recapitalisation of state-run banks led to the suspension of budget support by all donors and a suspension of the IMF programme. Bilateral donors realised that the risks in giving budget support were more related to governance concerns than to fulfilment of structural reforms, which had formed the basis for bilateral conditionality.

Despite having no explicit conditionality on governance issues at the time, bilateral donors nonetheless suspended budget support because of governance issues. It was clear that transparency and prior agreement on conditionality in this area was missing. Donors therefore decided to shift their focus to 'second generation reforms' such as governance and institution-building rather than 'first-generation' adjustment and stabilisation reforms under a new budget support agreement<sup>10</sup>.

Furthermore, the move towards increased budget support on the part of several 'like-minded' donors galvanised the process, whose scale was then significantly increased when the World Bank agreed in 2003 to bring its Poverty Reduction Support Credit (PRSC) programme within the frame of the MDBS. The PRSC amounts \$60m out of a total of c. \$233m in budget support provided to the GoM per annum. This injection of resources, along with the institutional weight of the World Bank, increased the need and momentum to have a formalised process with clear and transparent procedures.

### 4.2 Key characteristics of system

4.2.1 *PARPA*. The PARPA is the Mozambican PRSP, the first of which ran from 2001-2005. A new one is to be formulated during 2005. The PARPA's central objective is to reduce absolute poverty from its 1999 level of 70% to less than 60% by 2005 and less than 50% by 2010. It is based on promoting human development and creating a favourable environment for 'rapid, inclusive and broad-based growth' through six priority areas: education, health, agriculture and rural development, basic infrastructure, good governance and macro-economic and financial management.

4.2.2 The PARPA is operationalised through the annual *Plano Economico and Social* (the PES), which lays out the various economic and social performance indicators (c. 220 in total) and who is responsible for them. The implementation of the PES is evaluated annually through the *Balanco do Plano Economico and Social* (*BdoPES*) together with budget execution reports. These reports are supposed to be presented to Parliament and are accepted by donors as the annual PRSP Progress Report. The IMF and World Bank still carry out an annual Joint Staff Assessment of the PRSP.

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<sup>9</sup> The G16 are: Belgium, Canada, Denmark, the European Commission, Finland, France, Germany, Ireland, Italy, Netherlands, Norway, Portugal, Sweden, Switzerland, the United Kingdom and the World Bank.

<sup>10</sup> Gerster and Harding (2004a).

4.2.3 *Memorandum of Understanding.* The MoU agreed between budget support donors ('Programme Aid Partners' – PAPs) in 2004 clarifies the performance and reporting commitments of both government and donors in supporting the implementation of the PARPA. The MoU was signed in the spirit of NEPAD, the Monterrey Consensus and the 2003 Rome Declaration on Harmonisation.

4.2.4 *Underlying principles:* The MoU is based around six key donor commitments, drawn from the Rome Declaration: alignment to GoM instruments and priorities; increasing predictability of aid flows; ensuring transparency of conditions and funding; eliminating bilateral conditions and reporting requirements; reducing transaction costs; and enhancing GoM capacity by providing appropriate assistance. The MoU sets out underlying principles and stipulates that a breach of any of these principles constitutes grounds for suspension of budget support. Underlying principles are: GoM's commitment to pursuing sound macroeconomic policies (with reference to IMF 'on-track' status or an equivalent judgement; GoM's commitment to peace and to promoting free, credible and democratic political processes, independence of the judiciary, rule of law, human rights, good governance and probity in public life, including the fight against corruption; and GoM's commitment to fight poverty (with reference to the Millennium Development Goals), including through a pattern of public expenditure consistent with PARPA priorities.

4.2.5 *The Group of 15/16.* This is the name for the group of donors who have signed up to the budget support system and the MoU. The G15 included Belgium, Denmark, the EC, Finland, France, Germany, Ireland, Italy, Netherlands, Norway, Portugal, Sweden, Switzerland, the UK and the World Bank. In February 2005, Canada joined the group as well, bringing the total number of donors to 16 and changing the name to the G16. There is a significant variance amongst donors in terms of the proportion of their funds being channelled directly into the government budget.<sup>11</sup> Other donors, such as USA, Japan, the UNDP, the IMF etc., are involved in the process as observers.

4.2.6 *Performance Assessment Framework.* The PAF, which is drawn from the PES, is a multiyear monitoring framework that includes specific indicators and benchmarks by which to measure government performance for the first year and indicative indicators and benchmarks for the following two years. It acts as a matrix of conditions against which the GoM is prepared to be held to account. Donors would consider reducing or suspending aid should the government fail to meet any of the benchmarks contained in the PAF. However, it is hoped that this will be avoided as benchmarks in the PAF are negotiated with the government, so should be achievable. The first version of the PAF was agreed at the April 2004 Joint Review. The PAF is to be used at the Joint Review meetings as the basis for assessing GoM performance in year n-1 and for donors to make indicative commitments for year n+1. The PAF for year n+1 is negotiated at the time of the mid-term reviews (September).

4.2.7 *Response mechanism:* there are two mechanisms for disbursement and commitment – donors can choose a single response where all funds are committed simultaneously, or a split response, involving fixed and variable tranches. Under the single response, donors make commitments for year n+1 within four weeks of the Joint Review, which takes place in April. They are obliged to confirm this commitment by the 31st of August. The commitment can only be changed if there is a breach of 'underlying principles'.

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<sup>11</sup> For example, the EC puts in 45% of their overall aid budget for Mozambique into the budget, equivalent to \$58m, while Portugal puts in only 10%, or 1.5m. See Table 2 for a breakdown of donors and the proportion they are putting into the budget.

4.2.8 Under the split response donors commit a fixed tranche as above – making commitments within four weeks of the April Joint Review and confirming by 31<sup>st</sup> August. Indicative commitments for the variable tranche for year n+1 also have to be made within four weeks of the Joint Review, but, unlike the single response allocations, this commitment is subject to change on the basis of further information on GoM performance on certain indicators in year n-1, or on performance up to the time of the Joint Review. Commitments have to be confirmed by 31<sup>st</sup> August in year n.

4.2.9 *Programme Aid Partners' Performance Assessment Framework (PAP's PAF)* The PAPs' PAF sets out benchmarks for monitoring donor performance based on commitments laid out in the MoU and derived essentially from the Rome Declaration. The PAPs' PAF was drawn up in September 2004, following a baseline study by independent consultants. It was reviewed in early 2005 by independent consultants, however a formalised plan for further reviews has yet to be agreed. There are currently no sanctions for donors who do not meet the commitments in the PAP's PAF, and at present performance targets are aggregate across all donors involved.

4.2.10 *Calendar* The **joint review** is backward looking and takes place in March / April. It occurs after the Ministry of Planning and Finance (MPF) reporting on the Balanço do PES for the previous year. It is focused on coming to a joint view on GoM performance, which serves as a basis for donor commitments for year n+1. The **mid-year review** is forward-looking, and focuses on budgeting and agreeing on the PAF matrix for the following year. It takes place in August / September. This should happen prior to the MPF sending the annual budget and PES to parliament by September 30. To avoid confusion, it is probable that the mid-year review will be renamed a 'planning exercise'.

4.2.11 *Poverty observatory* The Poverty Observatory is an annual consultative forum composed of representatives of the GoM, the donor community and domestic civil society. The purpose of the Poverty Observatory is to monitor the GoM and other development actors' implementation of the PARPA. Civil society is represented through a group called the G20, which includes churches, labour unions, networks of NGOs, the private sector and academics. The G20 has a steering committee of five member organisations, which coordinates the efforts of these organisations to contribute to the Poverty Observatory.

4.2.12 *Government–Donor Joint Budget Support Steering Committee:* This Committee is composed of the MPF and a troika of the current chair, previous and next chairs of the G16, as well as the EC and World Bank, due to their level of budget support.

4.2.13 *Development Partners' Group:* Headed jointly by the UNDP and World Bank, this was traditionally the coordination forum for all donors. However, its role has been substantially weakened with the emergence of the MDDBS system.

## 5. Analysis of key components of MDBS system

In this section we analyse the key issues in the framework of donor commitments under the MoU. We begin by commenting on ownership and then discuss: alignment to GoM instruments and priorities; increasing predictability of aid flows; ensuring transparency of conditions and funding; eliminating bilateral conditions and reporting requirements; reducing transaction costs; enhancing GoM capacity by providing appropriate assistance; and mutual accountability.

### 5.1 Ownership

#### 5.1.1 Coordination and ownership

The 2004 DAC Survey noted that the aid coordination in Mozambique was essentially donor driven and that it was complicated by the lack of a coherent agenda to cover all modalities (project, sector and general budget support).<sup>12</sup> This appears to remain true, although several donors interviewed for this research commented that GoM ownership and confidence in tackling budget support donors who failed to meet policy commitments was increasing.

The GoM felt that although there were some difficult discussions over the MoU / PAF the outcome was equal in the end. It was felt that under this new system there is a better balance of power, with the government's capacity to negotiate improving and donors not dominating as much as they did in the past. The GoM feel that they have to argue for practical, feasible targets, but that donors are flexible enough to accept these targets. This is corroborated by the SPA report on the 2004 Joint Review (March 28 – April 5). The SPA mission found that the joint donor / GoM review of government performance led to an agreed and balanced assessment of progress.

The context is significant though. The joint and mid-year reviews take place in a forum involving many technical working groups, in all of which the GoM is likely to be heavily outnumbered by donor experts. One GoM representative noted that decisions can be taken in a situation where there is a 20:1 ratio of donor to government technical staff.<sup>13</sup>

**Risk to GoM:** From our analysis, the MoU is tilted in favour of the donors. Donor commitments to aid effectiveness targets are weaker, they can opt out of any provisions by including exceptions in Annex 10 and there is no effective sanction for failing to deliver on their commitments. Furthermore, the 'underlying principles' lack clarity and budget support is notoriously volatile, leaving the GoM in a permanent state of vulnerability. GOM confidence in donors' commitment is key therefore and must be further built through increased evidence of donor commitment to the MoU and a strengthened PAP's PAF.

**Risk to donors:** Donors in the G16 are taking a clear gamble, as there is a risk that public corruption could see aid funds diverted. However, continuing to fund projects that leave government sidelined and unaccountable is also a gamble. Donors should be encouraged for taking a risk in providing budget support as one of several modalities, but they must find ways of supporting and encouraging domestic accountability and allowing themselves to be held to account for failing to meet pledges they make.

**Non-BS aid:** the current share of budget support in overall aid is 35 – 40%, leaving the bulk of aid being delivered outside of the MDBS system in project form. Given the proliferation and lack of coordination of projects, this raises questions around overall aid effectiveness

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<sup>12</sup> OECD – DAC Survey on Progress in Harmonisation and Alignment 2004 – Mozambique Country Chapter. (para. 2.1.5 – 2.1.7)

<sup>13</sup> J. Sulemane, interview, Maputo, Jan 2005.

and the potential for country ownership. It is possible that the MDBS system is increasing coordination around budget support at the expense of coordination of aid delivered under other modalities. As noted by the DAC, there is no overall mechanism to cover all modalities.

Furthermore, the role of line ministries and sectoral working groups needs to be clarified and articulated within a global strategy for aid management. As discussed below, there is a tension between these and the budget support process, which becomes a burden on effective aid management (Section 5.2).

**Role of the IMF:** The Fund continues to impose its own agenda, in spite of the PARPA. It is therefore not clear how far the PARPA is, or can be, a nationally-owned document when macroeconomic policies are agreed outside of the PARPA process (see Section 6).

We believe that the GoM needs to develop an overall external assistance management strategy. This should take the form of a joint agreement with all donors on aid modalities, coordination and harmonisation. It should include monitorable targets for donors' performance and a clear articulation of the consequences for GoM of failure to comply with 'underlying principles'.

### **5.1.2 Broad country ownership: Parliament and civil society**

Broad country ownership is not limited to government alone, however. It also means ownership by other stakeholders, including the Parliament and civil society.

**Parliament:** Parliamentary involvement in the PARPA, PES and PAF system is very limited and as a result their ownership of these processes remains minimal. Parliament was not consulted on the first PARPA and the PAF has not been submitted to the Parliament for debate heretofore, but this may change in future. Poor parliamentary involvement is due to both the capacity of MPs and the lack of will by elected representatives to scrutinise the government effectively. The parliament is selected through a list-system and MPs do not have constituencies. This means the incentives of parliamentarians are entirely focused on their party, not on the individuals that elect them in their constituencies. It is unlikely that domestic accountability will be developed via the legislature without electoral reform, Nevertheless improvements can be made and we propose means of supporting greater accountability and ownership through increased transparency and capacity building (Section 5.6).

**Civil society:** civil society ownership of the PARPA and PES is weak and understanding of the MoU and system very limited. It is clear that there are still serious problems with government accountability to civil society, particularly in terms of provision of information and insufficient time for consultation (as was seen with the previous PARPA and there is a risk of the same happening again for the PARPA II). Both donors and the government have collectively failed to communicate to civil society groups how the donor co-ordination process works, and how the PAF relates to the PES.

Civil society organisations are invited to the sector working groups – indeed this may be their main avenue for influencing GoM policy. However the main meetings between donors and the government about the PAF are not open to civil society. The Poverty Observatory has not proven to be an effective forum for policy discussion so far. There is a need for clarity around how the Poverty Observatory relates to the Joint Review, as both cannot meaningfully continue in parallel without giving the message that the real decisions are taken by donors with the GoM.

In fact, it could be argued that the setting up of powerful donor-GoM policy fora in parallel with domestic accountability processes could actually be counteracting civil society's (and Parliament's) ability to hold government accountable in the longer term. A number of initiatives need to take place to build civil society participation and ownership. A long-term approach to civil society capacity building is necessary (see Section 5.6), along with accessible systems of local government.

In the meantime, we recommend that the GoM and G16 give priority and appropriate resources to a strategy to engage with civil society around the PES, BdoPES and PAF. The GoM needs to undertake initiatives to make the PES and BdoPES more accessible and digestible to civil society. Material must be in language that people can understand and disseminated through media accessible to the poor, notably radio. Consultations and feedback sessions on the PES and BdoPES should be held at district – or at least provincial - level. The GoM and G16 should create more space for direct civil society participation in Joint and Mid-year discussions, without overloading the process. We propose a minimum step of holding dialogue sessions on implementation of the PES and on PAF content as negotiations unfold, i.e. at least twice in the review periods (which last up to 10 days). Civil society should be invited to make a declaration at the end of the joint and mid-year reviews, stating their assessment of the outcome of these meetings. The civil society declaration should be attached to the Aide Memoire.

In the meantime, the GoM needs to adopt a comprehensive strategy for participation in PARPA II decision-making, with donor and CSO support as necessary. It must make sure that it reaches the poor and marginalized, notably those living beyond Maputo, and includes widespread use of meetings at district / regional level and media such as radio, newspapers etc. The GOM could work with civil society partners, including religious organisations, members of the G20 group, to disseminate and gather civil society inputs from consultations. This should not be seen as a once-off activity however, but as part of an institutionalisation of democratic governance.

## **5.2 Alignment with the GoM's agenda and systems**

The MoU committed donors to align to Mozambican instruments, processes and systems of financial management, including: (1) providing assistance for and undertaking dialogue around the PARPA, PES, PAF, medium term expenditure framework and state budget; (2) using government processes and documentation; and (3) following the government cycle for planning implementation, monitoring reporting and funding.

- Alignment within the MDDBS

Assistance for and dialogue around the PARPA, PES and PAF has been effective, to the degree that a PAF has been developed which draws indicators from the PARPA, based largely on government priorities. However, there were significant tensions in the process of developing the PAF.

Firstly, the Ministry of Planning and Finance had the primary role in developing and negotiating the first PAF over a 12-month period to April 2004 but there was an essential difference in negotiation capacity between the different parties. As noted above, one or two adequately trained Government officials faced up to donor experts from up to 20 missions in each area of policy design. This imbalance in capacity inevitably had an influence on the degree of GoM control exercised over the design of the PAF. However, it also signals a need for the GoM to focus on capacity development.

Secondly, there was tension as a result of a lack of effective government mechanisms to develop indicators consistent with line ministries' policy priorities. Although internal dialogue between line ministries and the MPF increased during the course of the development of the PAF, line ministries nonetheless expressed grave concern that the priorities contained in the PAF agreed in April 2004 were not their priorities. This relates to a critical systemic issue in Mozambique: the high level of direct funding of sectors and off-budget support means that many line ministries engage primarily in dialogue around policy and finance with the donors rather than with the Ministry of Planning and Finance. Nonetheless, both donors and officials interviewed recognised that the PAF process had highlighted the weaknesses in internal government dialogue and led to an increased resolve for stronger internal planning processes.

Thirdly, the national budget process should see budget discussions between line ministries and the MPF taking place in July – September. The development of the PAF (at the Joint review in April, with a revision in September at the mid-year review) was seen to be out of step with this process, weak though it may be. Government officials reiterated the need for improved internal dialogue, but also for donors to respect national planning and budgeting cycles. However, the cycles set in place by the GoM are not immune to disruption from party politics, as illustrated by the 6-month hiatus in finalising the 2005 budget. The budget was only agreed in the 1<sup>st</sup> quarter of 2005, instead of September 2004. This was due to elections in December 2004. Clearly, the state budget systems must be strengthened to make them function independently of electoral cycles.

The design of the PAF is a fundamental issue in Mozambique because it de facto becomes the prioritised implementation plan for the PES / PARPA. Several interviewees in Government and civil society had strong reservations about this system of donor-driven prioritisation. The PES has around 220 indicators and the PAF has 50. The PAF targets and indicators are subject to rigorous discussion between the MPF (mainly) and donors. Criteria for indicators include availability of data for measurement, criticality of the issue, degree of government and donor prioritisation of the issue etc. While the PES is presented to Parliament under normal reporting procedures, the PAF isn't.<sup>14</sup> The quality of the parliamentary debate around the PES is low however, reflecting low parliamentary capacity. It may also reflect the quality of the PES. Donors have stated that the PES is too general to be used for detailed budget allocation. Only 24% of donors use the BdoPES to influence their resource allocation decisions.<sup>15</sup>

Nonetheless, the failure to present PAF to Parliament or ensure that the process is more open has led to a perception, notably among some civil society representatives, that the PAF was undermining country ownership. It is viewed as leading to the development of a parallel monitoring system with only some performance benchmarks taken from the PES. Clearly, indicators included in the PAF are going to be of higher priority to the government because of the implications if they are missed. This means that it is very important for all stakeholders to understand how the indicators for the PAF are selected and how far the government is really in driving seat in this process.

- PARPA alignment beyond the MDDBS

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<sup>14</sup> It appears that the PES for 2005 has not been presented to Parliament, which is probably linked to the disruption to the budget cycle as a result of elections in December 2004.

<sup>15</sup> OECD-DAC Survey on Progress in Alignment and Harmonisation – Mozambique Country Chapter, p. 5, para 3.1.4.



A notable issue is the amount of funding that is outside of the MDDBS framework and the degree to which this funding is outside of MPF processes. At present, a large proportion of ODA (c. 66%) is still delivered in the form of project support, including support that is delivered by G16 members.<sup>16</sup> Much of this funding is off-budget and is therefore not captured in the budget execution report. This means that it is not possible for the GoM to evaluate alignment of donor expenditure to government priorities. Many donors, including the World Bank and USAID, say that their projects are aligned with the PARPA. However, they note that the PARPA is very broad and that therefore almost anything can be said to be aligned to it.

It is notable that the indicator chosen for monitoring donor alignment to the national development strategy under the Paris declaration is the amount of donor aid which is on-budget. The interim target agreed was 85% of aid flows to be reported on-budget by 2010. Achieving even a less ambitious target will present considerable challenges for donors in Mozambique and highlights a key weakness in broad donor alignment to policy and procedures in this country.

- Alignment at sector level

Donor alignment at line ministry or sectoral level is an important issue. The treatment of sectors varies enormously and there are a plethora of off-budget, non-harmonised, uncoordinated interventions at this level. A history of relying on direct donor funding has led to a fracturing of the government system in Mozambique. Policy is developed, budgets administered and services delivered by 23 different ministries that are only weakly coordinated by the centre. A government representative noted that of those 23, only 7 have visions and medium-term plans while none have anywhere near adequate levels of qualified personnel.

The OECD-DAC Survey (2004) found that while good dialogue existed between the line ministries and donor working groups, these were poorly harmonised with the budget support process. There are reasonably strong donor-ministry working groups in health, education and agriculture, which is not surprising perhaps as these account for a large percentage of government funds. However, even in these sectors, neither the line ministry nor the donors appear to communicate the arrangements made at sectoral level to the MPF or Government–Donor Joint Budget Support Steering Committee.<sup>17</sup> The DAC found that there was an overlap between review processes at sector level and reviews that take place under the PARPA.<sup>18</sup>

The DAC Survey (2004) reported that: *‘The Govt articulates the need to be stronger in demanding a more holistic process with a prioritisation (and harmonisation) of the national budget and plan over individual sector efforts. It is hoped that this will become easier as the performance assessment framework becomes more institutionalised’*. Indeed, there are some indications that this may happen. The sector working groups were more closely involved in developing the PAF for 2005 than heretofore. This is potentially important for financial as well as integrated programming reasons. Certain donors were clearly of the view that the GoM needs to fulfil the specific PAF targets, rather than making general progress on all of them, to justify budget support (see Section 5.4). Therefore, PAF objectives which are not drawn from sector plans may result in disruption to some donors’ budget support flows.

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<sup>16</sup> See Table 2.

<sup>17</sup> This Committee is composed of the MPF and a troika of the current chair, previous and next chairs of the G16, as well as the EC and World Bank, due to their level of budget support.

<sup>18</sup> OECD – DAC Survey on Progress in Harmonisation and Alignment 2004 – Mozambique Country Chapter, p. 7, para 3.4.1.

Overall, it is clear that this systemic problem of a lack of articulation between budget support and sector support is a critical risk factor for aid effectiveness in Mozambique. The Government needs to show stronger leadership in developing a coherent planning system to include all ministries. However, this is linked to the need for donors to subordinate policy dialogue at sector level to the GoM's dialogue with its line ministry. Donors are under obligation to ensure that their interventions reinforce rather than undermine coherence in overall national policy-making.

### 5.3 Predictability of aid flows

Predictability of aid flows is possibly the linchpin of the success of the multi-donor budget support system, as this is the criterion on which the GoM judges donor commitment. Many donors stated that they hoped to see an increase in GoM confidence to take leadership of the aid effectiveness process and face down under-performing donors. However, that confidence can only be based on the knowledge that most donors are prepared to commit resources in a timely manner, in accordance with the MoU and PAP's PAF.

There are three main elements to predictability: multi-annual commitments, timely commitments and timely disbursement. The MoU and PAP's PAF sets out a clear framework for improvement on all levels.

- Multi-annual commitments

Overall, only 28% of donors in Mozambique provide 3-year indicative commitments, according to the DAC.<sup>19</sup>

The PAP's PAF indicates that, in 2003, 60% of PAPs had an indicative commitment to multi-annual (though not rolling) indicative commitments. It commits PAPs to increasing this share to 90% by 2006. The 3 donors without a multi-annual commitment at the time of the 2003 baseline survey of PAPS indicated that without multi-year arrangements in place indicated that they intended to introduce such multi-year arrangements in the near future.<sup>20</sup> (Gerster and Harding (Baseline Survey) 2004).

However, the value of the multi-year commitments to GoM planning varies, as several donors give only two-year commitments (Belgium, France & Germany), while the EC and World Bank have four-year indicative commitments. Furthermore, while multi-year arrangements are significant, if they are not rolling this limits their value to the GoM, as pointed out by one donor.

Finally, as noted above the vast majority (72%) of the overall donors' group (including non-G16 members) do not provide multi-year indicative commitments. Therefore, there is a clear need to improve multi-annual commitments, both within the G16 - in terms of reaching 3 year minimum and rolling commitments - and amongst non-G16 donors.

- Timely commitments

The biggest problem in relation to timely commitments appears to rest with the 'split response' mechanism allowed for in the MoU. Three donors avail of this split response mechanism: the EC, Sweden and Switzerland.

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<sup>19</sup> OECD – DAC Survey on Progress in Harmonisation and Alignment 2004 – Mozambique Country Chapter. (para. 4.4.2 – 4.4.3).

<sup>20</sup> Gerster and Harding (2004, p. 6). This includes Finland and also Sweden, which has recently moved budget support under the control of SIDA, rather than the dept of Foreign Affairs, in order to allow it to make multi-annual indicative commitments, potentially up to five years.

As outlined above (Section 4.2), under the 'split response' mechanism, donors commit a fixed tranche for year n+1 within four weeks of Joint Review, which takes place in April, and they confirm this fixed tranche by the 31st of August. The commitment can only be changed if there is a breach of 'underlying principles' (Section 4.2). This part of the process is the same as for the 'single response'.

Indicative commitments for the variable tranche for year n+1 have to be made within four weeks of the Joint Review, but, unlike the fixed, or single response allocations, this commitment is subject to change on the basis of further information on GoM performance on certain indicators in year n-1 or on performance up to the time of the Joint Review. Commitments have to be confirmed by 31<sup>st</sup> August in year n.

Problems arise here for several reasons. Firstly, the GoM begins its budget process in June – July, and the budget is normally presented to Parliament in September. The 'split response' means that the GoM potentially finds itself having to introduce contingency elements in its budget, as the disbursement of the variable tranches from some donors is uncertain until very late in the process (August 31<sup>st</sup> in theory but possibly later in practice – see Sweden below). The actual impact will of course depend on the size of donors' variable tranches. Nonetheless, even if variable tranches are relatively small, this system is contrary to the principle of strengthening the budget as an effective instrument for implementing the PARPA. It introduces an element of unpredictability which is counter to the purpose of the MoU also.

Donors employing the split response justify it by emphasising that the GoM is fully aware of the concerns of donors and the basis on which the variable tranches will be confirmed. They note that this allows time for dialogue and for resolving the issues in question. However, this clearly creates an added burden which the MDDBS is meant to avoid – protracted and detailed donor-by-donor discussions around specific conditions.

The Swiss note that they take a broad view of the GoM's progress and if it is generally exhibiting a willingness to address the issues they raise, they will commit the variable tranche by end-August. The EC on the other hand, takes a more mechanistic view, and reduces the amount of the variable tranche based on a formula which assesses the degree to which the GoM has missed the target. The EC argue that this is preferable as the GoM knows exactly what is at stake and what the donor response will be – we return to this below (Section 5.4).

The Swedish mechanism has been subject to considerable controversy, as the Swedes' budget support is under the control of the Ministry of Foreign Affairs, rather than SIDA. Budget support decisions are made by the Swedish Government very late in the process (officially in September, but possibly in the year when the budget is under implementation) and funds are often disbursed at year-end. This should be resolved in 2005, as budget support will be delegated to SIDA in 2005, who will have the power to devise 5-year strategies. These strategies will be contingent on Swedish parliamentary approval.

- Timely disbursement

There are still serious disbursement problems, with many donors failing to make disbursements when they have pledged to do so. This is partly because bilateral accords still take precedence over the MoU.<sup>21</sup> The MoU's 'Annex 10' details the exceptions by many donors to the processes outlined in the main text of the MoU. These are invariably around

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<sup>21</sup> 'Bilateral agreements ... have precedence over this MoU', Art 2, MoU.

the disbursement process. There is an implicit, albeit weak, objective for such exceptions to be reduced over time.<sup>22</sup>

Failure to disburse on time is very serious because it undermines GoM confidence in donors, weakens the budget as an effective instrument of national policy making, impacts negatively on programme implementation (a GoM representative noted that they would not begin a project if they were uncertain as to the fulfilment of donor commitments) and because it can lead to domestic or commercial borrowing, with high costs for the GoM. There were severe macroeconomic (inflation) and PARPA implementation consequences in late 2003 when four donors (EC, Netherlands, Sweden and Switzerland) disbursed some or all of the budget support on the last quarter. The DAC found that a considerable number of donors continue to disburse at the end of the budgetary year and that this is one of the factors contributing to very low budget execution rates in key PARPA-priority sectors.<sup>23</sup> According to Gerster and Harding's Baseline Survey, in 2003, only 6 donors' disbursements took place according to the schedule of commitments. These were Denmark, Finland, France, Ireland, Norway, UK.

A critical factor is that G16 country offices still only have limited influence to ensure punctual disbursement. Sweden is a particularly strong example, where until this year, the country office had no delegated decision-making power over budget support, though that is due to change in 2005 as noted above. However, the problem is quite a generalised one. The Baseline Survey in 2003 found that only one country had fully delegated decision-making power over disbursement and conditionality to the country office (France). While other countries emphasise that the actual practice is more delegated than the formal processes indicate, this is still an important weakness in donors' budget support systems.

The tranche release process can create significant predictability and disbursement problems. An example is the EC's system, where the variable tranche is based on the achievement of outcome indicators. Lack of availability of information in relation to these outcome indicators meant that 2003 funds could not be disbursed on time. Furthermore, for bureaucratic reasons, the EC's 2002 and 2003 disbursements were delayed until the following years (January 2003 and March 2004 respectively).

Gerster and Harding (2004a) include a summary of specific disbursement-related problems in 2003 – 04.<sup>24</sup> It is important to note that the reason for some delayed disbursements actually lies with the government, who have on occasion failed to request and administer disbursements as required. This raises capacity questions, as the procedures were mere formalities according to governments, involving minimal paperwork (i.e. the MPF signing a letter requesting transfer of resources).

However, despite concerns about the true commitment of the G16 to ensure prompt disbursement, the government does feel that donors are improving in this regard. Changes have been made by donors which illustrate commitment to aligning with the GoM's budgetary cycle. Gerster and Harding found that several donors intended to become 'early disbursements', moving disbursements forward into the first two quarters. Belgium, the EC, Germany and the Netherlands intended to join the existing early disbursements – Finland, France, Ireland, Italy, Norway, Portugal, Sweden, Switzerland and the UK.<sup>25</sup>

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<sup>22</sup> 'PAPs are committed to providing Programme Aid in a way that... improves harmonisation by eliminating bilateral conditions and bilateral administrative and reporting requirements (as far as possible given existing legal and statutory requirements, which should also be reduced over time', Art 13, MoU

<sup>23</sup> OECD – DAC Survey on Progress in Harmonisation and Alignment 2004 – Mozambique Country Chapter (p. 6).

<sup>24</sup> Gerster and Harding (2004a, p.25).

<sup>25</sup> Gerster and Harding (2004, p. 11 – 13). The EC, Sweden and Switzerland planned to disburse the fixed tranche in the first two quarters, with variable tranches depending on provision of indicators.

Nevertheless it must be remembered that disbursements are intrinsically linked to development policy in donor headquarters, which, due to changes in national governments may affect donors' ability to respect their indicative and practical commitments. This is potentially the case with Denmark. After a change of government it may not be able to align to the response and disbursement mechanism in the MoU.<sup>26</sup> This was still unresolved at the time of research.

Some donors noted that the GoM is becoming more confident and is challenging donors on the issue of predictability and disbursement. However, the GoM has had mixed experiences – both positive and negative – with donors and the commitment of individual donors to fulfil agreed arrangements for the delivery of aid.

In a recent case a donor needed to fulfil its own technical disbursement rules and attempted to go outside of an agreement for aid delivery in a particular sector (health). The line ministry objected and insisted that the donor commit to the multi-donor sectoral agreement. The donor in question took the issue directly to International Cooperation in the Ministry of Foreign Affairs. As a result, the health ministry came under considerable pressure to accept a modification to the original multi-donor agreement. Other donors vigorously challenged this departure from the original agreement but left the final decision to the ministry in question, who finally agreed to the modification.

In other cases, it appears that donors have worked as a group to encourage other donors to abide by the MoU and PAF. This appears to have occurred when the World Bank attempted to add its own conditions to the agreed PAF, when joining the G16.

Overall, there is a strong sense from most interviewees – GoM and donors - that the level of exceptions in Annex 10 are unacceptable. Donors have made a commitment to reduce these exceptions, but they must be held to account to ensure they do so. This should be part of annual, transparent reporting on the PAP's PAF.

#### **5.4 Conditionality, transparency and elimination of bilateral conditions**

The system for developing and agreeing upon conditions under the Performance Assessment Framework (PAF) is outlined above (Section 3.2), together with some of the faults in the process (Section 4.2). This reduced framework of agreed conditionality is one of the key features of the MDDBS system in Mozambique and as such offers the potential for learning lessons relevant to other countries' work on MDDBS frameworks.

- **Extent of Conditionality in the PAF**

The PAF has deliberately and with significant effort been kept to a maximum of 50 indicators. However, there is some creative interpretation of this agreement apparent, as indicator 49 is actually a set of five indicators, i.e. 49a – 4. It appears that ownership of the PAF from the GoM side was limited to the MPF mostly, when the 2004 PAF was drawn up. The process issues outlined above (Section 4.2) indicate the lessons learnt from that experience.

It is also clear that the rapid growth in the G16 has put the process under strain. Donors are keen to see their priorities included in the PAF's performance indicators and it takes a high degree of collective restraint to develop a reasonable number of PAF indicators. Nonetheless, these should be reduced even further, in order to allow the GoM both implement critical reforms and programmes and deal with coordination of the 60 – 65% of

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<sup>26</sup> Gerster and Harding (2004, p. 12).

aid which is not delivered in the form of budget support. The performance indicators should be limited to those which are critical for poverty reduction and which are supported by all members.

A potential pitfall from such a reduced set of PAF indicators however, is the likelihood that donors that do not find their priorities reflected in the G16 PAF, may seek to impose additional conditionalities through other avenues – project support for example, or via ongoing bilateral agreements. It is imperative that all donors implement Article 13 of the MoU, which commits donors to ‘eliminating bilateral conditions and bilateral administrative and reporting requirements’. The target under the PAP’s PAF is entirely inadequate and needs to be revisited. It aims to reduce the share of donors with bilateral exceptions in Annex to less than 55% in 2006, which allows for a disimprovement over 2004’s figure of 53% of donors with exceptions.

- **Transparency**

Transparency around disbursement and conditionality is vital to making this system work, particularly if donors and the government are to be accountable to each other. The PAF system has helped increase transparency between the MPF and the G16. In our research, there was general consensus amongst government (i.e. MPF) and donor representatives about how the system was working and the reasons for previous halts in disbursements, whether due to government or donor underperformance.

However, both the contents and process of the PAF remain opaque to other domestic stakeholders, such as Mozambique Debt Group and the parliamentary committee on budget and planning. Information about the PAF process, if not the process itself, needs to be opened up to domestic stakeholders.

There is a fundamental debate about the degree to which donors should be clear and transparent around their ‘ownership’ of specific conditions within the PAF. The MoU indicates that the Joint Review (which focuses on performance under the PAF for year n-1) should come to a *‘joint view on performance, which serves as the basis for commitments’*. Some donors appear to take this at face value and believe that a holistic view, illustrating a general trend towards fulfilment of the PAF indicators should be sufficient for all donors to make their commitments.

Others however, believe that donors are in reality only really concerned about the indicators which relate most closely to the programmes they support. Donors may well come to a ‘joint view’ based on the PAF (though the MoU allows divergent opinions to be reported separately), but ultimately, decisions around commitments and disbursement are bilateral decisions. Therefore, some donors (for example the EC) believe that all donors should be upfront about the conditions that are critical to them. This transparency is necessary to give the GoM an adequate handle on the consequences of failure to reach targets.

This creates its own risk of course, which is that – given the sizeable difference in funds allocated by different donors under the MoU - there would be a diversion of GoM attention towards achieving those targets which were of importance to the larger donors. While transparency is critical, it is not clear how the G16 and GoM will resolve tensions arising out of a situation where there is an imbalance in incentives to achieve different indicators.

- **Elimination of bilateral conditions**

In 2003 – 04 several donors were still insisting on implementation of conditions which were not in the PAF. While for some donors, this was due to existing bilateral agreements, the World Bank attempted to add conditionality to the PAF from its new Poverty Reduction and Support Credit (PRSC). Some Bank staff were strongly in favour of having Bank-specific conditionality additional to the PAF. This was apparently debated at length internally in the

Bank and was resisted by the MDBS donors and GoM. The outcome in late 2004 was an agreement by the Bank that its PRSC would align fully behind the conditions in the PAF, though it has its own response mechanism (outlined in Annex 10 to the MoU).

The debate noted above on bilateral conditions *within* the PAF is significant, but there are also questions to be addressed with respect to conditions attached to projects and programmes which are *outside* of the remit of the MoU. The most contentious are those of the Bank and Fund, which are discussed below (Section 6).

There is a clear need for an overarching system which would oversee a reduced level of global donor conditionality. Overall conditionality should be reduced and streamlined, in accordance with the GoM's priority areas agreed under the PARPA. As PARPA II is under development, the time would seem to be right to work towards a 'global donor' alignment and harmonisation agreement.

## 5.5 Administrative burden / transaction costs

The burden-sharing of transaction costs is not being explicitly monitored, so it is difficult to assess with accuracy what the impact has been on GoM. It is clear, however, that transaction costs for donors have increased. World Bank officials, for example, said they spent up to  $\frac{3}{4}$  of their week in donor co-ordination meetings and sector working groups, with a similar response from the IMF. Most donors expressly commented on the increased work involved in donor coordination, but noted that the burden was shifting in the right direction – i.e. increasingly onto donors rather than onto GoM.

Transaction costs from total aid (budget and non-budget support) are still very high, particularly given the extremely limited capacity of the Mozambican government.

- **Projects:** Project spending still accounts for over 60% of aid. A recent analysis by the MPF showed the government had 1200 different bank accounts, most of which were set up for administration of donor projects.

One reason for continued project-oriented or uncoordinated support was a continued vying for visibility among donors on certain projects. It was reported that some donors are still inclined to conclude agreements on projects with the GoM alone, excluding other donors, for 'prestige' reasons. The DAC Survey concluded such behaviour leads to duplication and burdensome management costs and that *'there is going to be a need for open and honest assessment of the tensions that this appears to indicate if harmonisation and alignment are going to progress'* (DAC 2004, p. 13).

- **Sector support:** the management of sector- or geographically-based projects and their articulation with the state instruments for planning, budgeting and monitoring is one of the critical challenges facing development partners in Mozambique. This will need to be addressed more consistently in the future, with both G16 and non-G16 donors.
- **MDBS:** There is a lot of ground to cover on the G16 side in order to fulfil commitments to reduce transaction costs. The 2003 Baseline Study and the DAC Survey carried out in 2004 give details of the transaction costs burden on the GoM. For example, in 2003, there were 134 reported donor missions from the then-G15 –

or an average of 2.5 missions per week from only 15 donors. Delegated cooperation was used only by 4 of the G15 donors in 2003.<sup>27</sup>

Meanwhile, the evolution of the budget support system has created some different burdens, such as preparing for the joint review each year. The GoM finds the preparation for reviews difficult and highlights an imbalance in capacity, in terms of numbers of qualified specialists, between the G16 and the GoM. The government asked for sector reviews to happen prior to the joint review in order to streamline the planning process. This was agreed to and should begin to take effect in 2005. The GoM are setting up a central secretariat to facilitate inter-departmental coordination.

The G16 has further work to do to fulfill their commitment to reducing transaction costs under the MoU. However, there is also the critical issue of the extent and proliferation of other approaches which fall outside the MOU and which place demands on an over-stretched government, in terms of project and sector support. The coordination of budget, sector and project support both among donors and with the state instruments for planning, budgeting and monitoring is one of the critical challenges facing development partners in Mozambique.

The G16 should place immediate emphasis on achieving their targets in the PAP's PAF but also increasingly work with the GoM to identify how coordination beyond budget support should take place.

## 5.6 Capacity building

In a country where capacity is ruinously weak, this is an obvious concern for government, donors and other stakeholders. Donor support for capacity building is not adequate at present, with respect to the GoM, parliament or civil society.

- **Support for GoM:** Gerster and Harding's Baseline Survey of donor performance in 2003 outlines then-G15 members' involvement in capacity building initiatives.<sup>28</sup> They find that while there is a lot of support for capacity building there is a need for greater cooperation and the establishment of joint funding arrangements, such as a Common Fund for Technical Assistance. The PAPs' PAF includes an objective to strengthen capacity around PARPA design, implementation and monitoring, with a commitment to explore the possibility for a long term joint strategy for Technical Assistance. An Issues Paper and discussions on the topic were planned for 2005.

This needs to be treated as a priority, but there are questions as to where such a strategy should be housed. Obviously, the GoM need to lead, optimally through the development of an overall strategy for capacity development as agreed under the Paris Declaration (para. 19). Thereafter, non-BS donors need to be involved in discussions on capacity development, suggesting the need to agree such a strategy outside rather than inside the G16.

There appear to be some tensions between different donors on the nature and function of technical assistance. Some are concerned with long-term skill and knowledge transfer, while others – the IMF was mentioned – are concerned only to get a particular job done. A coherent capacity building strategy would have to include agreement among donors on approaches which would support the GoM's wishes and needs as a priority. While specific circumstances will dictate needs for

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<sup>27</sup> Gerster and Harding (2004, p. 17).

<sup>28</sup> Gerster and Harding (2004, p. 18 – 19).



any capacity building project, it appears that the GoM has a preference for genuine capacity building of its staff rather than straight 'technical assistance' to do a job instead of, or for, staff.

- **Support for Parliament:** Bilateral support to parliament is weak and fragmented. The UNDP is the main agency working with the parliament, and at present the scope for working with parliament is limited by the electoral system in Mozambique. Representatives are drawn from party lists and therefore have no real constituencies. The incentives to hold government to account are thin. Parliamentary and electoral reform is probably the only real solution to a lack of accountability and dynamism in parliament. While difficult, this is an area where joint or coordinated G16 efforts could be effective. Donors should engage with parliamentarians under specific programmes around strengthening capacity to carry out their legitimate functions as a legislature. However, donors should also create more space for parliamentary oversight of, inter alia, budget processes and donor- GoM agreements. This should include opening up the processes around the MoU to parliamentary scrutiny – particularly the determination of the PAF and reporting on the PAP's PAF. The PAF should be formally presented to parliament, while the PAP's PAF should be formally or informally presented also.
- **Support for Civil society:** All donors recognised the need to build the capacity of domestic stakeholders to demand accountability from the government. Some said they were not really being pressed by these stakeholders to support them in this, while some donors are more active in seeking opportunities to do so. The over-riding factor is capacity weakness, which limits the breadth and depth of civil society activity. There are a small number of organisations that attract a lot of support in such a weak environment, for example the Grupo Mozambicano da Dívida (Mozambique Debt Group). Frequent reference was made by donors to the role of the G20 group of civil society organisations, academics and religious organisations, whom it was hoped would be able to rise to meet the challenges and opportunities present in the PARPA, PES and PAF frameworks. However, the G20, while important, cannot yet deliver on this expectation.

A wider, deeper and more sustained effort to support civil society is needed. Donors could choose different levels of sophistication in delivering a coordinated and coherent strategy for CS support – from joint funding mechanisms, to information sharing of existing activities around civil society capacity building. A simple and regular mapping would possibly highlight key areas of weakness and potential which could be taken into account by a group of similarly-minded donors (G16 or non-G16) in developing programmes for civil society capacity building. We believe that an appropriate approach would be one which includes a set of objectives agreed at such a joint donor level with members of the G20 and regular review and planning activities.

## 5.6 Mutual accountability

There is no doubt that the existence of the PAP's PAF has moved international debate on aid effectiveness forward, particularly in the area of mutual accountability. However, when looked at in more detail, there is a significant imbalance in accountability between donors and government in the MoU. As one senior government official said: 'the MoU is based on what the government 'will do' and what the donors 'may do'.

This is illustrated in part through the liberal use of Annex 10. Indeed, the commitment to reduction of bilateral conditions, bilateral administrative and reporting requirements and

bilateral legal and statutory requirements is very weak. As noted above, the target for 2006 is for fewer than 55% of donors to have bilateral exceptions in Annex 10, down from 53% in 2004.

It is also illustrated by the qualitative differences between the PAPs' PAF and the PAF. The PAP's PAF lacks clarity. It is in two parts: 'Indicators on core MoU donor commitments' and 'Monitorable Indicators'. The part on monitorable indicators lacks **any** targets for monitoring against however. Each of the 10 specific indicators is followed by 'to be monitored' for years 2004 – 2006. The PAP's PAF needs serious reform – it should be simpler, more progressive in terms of commitments and contain targets for each commitment and indicator. It is possible that the rapid growth in membership has created obstacles achieving broad agreement on targets for monitoring against. This is an important issue which will be addressed under 'systemic issues' below (Section 7).

Most people interviewed for this research felt that the system has made government more accountable to donors, rather than to other stakeholders (such as Parliament, civil society etc.). Some said this was perhaps inevitable 'whilst setting up systems', including systems of financial management. However, it's not clear if these increases in government accountability to donors have been reciprocated. Certainly, there are several recent examples of G16 donors acting outside the MoU, either using their aid disbursements to force the government on an issue that fell well outside the PAF or implementing its own disbursement procedures in spite of MoU / sectoral agreements.

As a result the government does not seem to feel it can fully trust the donors yet. Most donors acknowledged this risk and felt that 2005 was a critical year. By 2005, the system should have become more bedded down and G16 members should have phased out old bilateral agreements and made any necessary changes to headquarters procedures. Government confidence appears to be on the increase however, and possibly will increase further if donors reach all their commitments to further align disbursement to MoU standards.

However, the GoM still has no form of redress; there is no mechanism to penalise donors who do not meet their commitments. In fact, all of those interviewed agreed that the only way donors were monitored was through peer review and the only effective sanctions on donors who break the MoU commitments was peer pressure.

During our research we tried to identify some incentives and sanctions that both the donors and government could use to ensure good donor performance. Some options were to suspend badly performing donors from the G16 (either immediately or after '3-strikes') but the government would be loath to do such a thing as this would mean money being held back. Another option would be to deny the under-performing donor access to policy dialogue<sup>29</sup> and influence, as it is this that motivates most donors to join the G16. However it is unclear how this would work as currently many non-budget support donors have observer status and sit on the sector working groups. A more practical option is to incorporate individual donor targets into the PAPs' PAF, so individual donor performance can be tracked by the government, parliament and civil society in both the donor and host country.

We believe that individual donor targets should be introduced as an immediate measure and that annual reporting on the PAPs' performance be carried out independently and made publicly accessible. At a minimum, the report should be presented at the Poverty Observatory and to the Parliament. Ideally, donors would report to their own home

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<sup>29</sup> For example, Gerster and Harding recommended that 'PAPs which fail to disburse for period of 2 years should be considered to have defaulted on their commitments under the MoU, and should be denied the right to voice opinions on policy issues or PAF indicators in Joint Review meetings and processes'. Gerster and Harding (2004a, p.26).

parliaments, as part of an effort to raise awareness on the use of budget support as a modality.

## **6. The role of the IMF**

The role of the IMF in Mozambique, as elsewhere, is very important. The IMF is an observer at the G16 and actively attends relevant meetings, including the weekly G16 macroeconomic working group meetings.

Mozambique's current programme arrangement (Poverty Reduction and Growth Facility - PRGF) dates from July 2004 and should run to June 2007. Its previous PRGF arrangement was initiated in 1999, experienced an interruption in 2001 due to a banking crisis and expired in 2003. PARPA I was agreed in 2001, with this PRGF already in place.

### **6.1 IMF and Alignment**

The IMF has failed to align its programmes to both the content and temporal cycles of GoM policy.

In 2004 the IMF's Independent Evaluation Office (IEO) carried out an evaluation of IMF support to the PRSP process and implementation of the PRGF in Mozambique as part of a broader study with the World Bank. The report uncovered manipulation by Fund staff of the language in the GoM's PARPA, to suit Fund objectives. In the fourth semi-annual review of the PRGF, Fund staff said that the GoM was determined to reduce aid dependence in support of measures designed to enhance domestic revenue mobilisation. The PARPA actually stated that its objective was to 'strengthen coordination with international partners to ensure that the flow of external finance remains at US\$600 million per annum' (para. 197.2).<sup>30</sup>

The Fund is failing to live up to its commitments on aligning policy cycles to the national system. Not only was PARPA I predated by an ESAF / PRGF, but the present PRGF was agreed in July 2004 to last until June 2007, predating the process of drawing up a new PARPA by one year and essentially predetermining the macro-chapter.

Another example of temporal misalignment was the insistence of Washington-based Fund staff to carry out a three-week mission for their 'Joint Staff Assessment' of PARPA implementation shortly before both the Joint Review between government and donors in March-April 2004 and the CSO – GoM Poverty Observatory, which is meant to be the key annual domestic monitoring and dialogue event on the PARPA.

Gerster and Harding (2004a, p. 39) recommend that the Joint Staff Assessment of the PRSP / PARPA be closely coordinated and combined with the Joint Review. The purpose of the JSAN is questionable, as the GoM does not need a mechanism for feedback given its domestic and donor-oriented processes. However, in the event that the JSAN's remain IMF policy, coordination and combination with the Joint Review is recommended. However it should also coordinate with the Poverty Observatory as this is the event where, in principle, civil society gets to air its views on the fulfilment of PARPA commitments. In order to provide IMF Board members with a full account of experiences with the PARPA, the JSAN should have the Aide Memoire from the Joint Review, and civil society responses to the Aide Memoire and / or declarations from the Poverty Observatory appended to it.

### **6.2 IMF Transparency & openness:**

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<sup>30</sup> IEO IMF / OED World Bank, 'Republic of Mozambique – Evaluation of the PRSP and arrangements under the PRGF' (July 6, 2004, p. 42).

A serious problem in the Mozambican external assistance system is the lack of IMF transparency when negotiating the PRGF with the government, which is not only off-limits to local stakeholders, including parliament and CSOs, but is also a source of frustration for donors.

Visiting missions carrying out the six-monthly PRGF reviews meet with donors at the beginning, middle and end of each two-week mission. The Resident Representative attends the weekly macro-economic meeting, as noted above, and all other relevant meetings. A new IMF staff post in the Resident Representative's office has recently been approved, given the extraordinary demands on the office of participating in donor harmonisation meetings and of carrying on regular work with the GoM.

Nonetheless, donors, the GoM and civil society express frustration at the lack of transparency and openness of the IMF. The G16 regularly draw up comments on macro-economic issues through the economists' working group. They prepare comments for the meetings with the IMF missions, which are discussed at those meetings. However there was frustration at being 'briefed' by Washington-based IMF staff on agreements over which the BS donors had no influence.

A member of the G16 also described the frustration among the economists group at the time of the interview, as they were waiting for the IMF staff to send the report of the first review of the PRGF (carried out several months earlier) so that they could prepare a comment for their Executive Directors on the Board of the Fund. Ten days before the presentation of the Letter of Intent to the Board, the economists still had not received this document. They would have only a few days therefore to prepare their comments on the proposed agreement and circulate it to Board members. This was viewed as wholly inadequate and deeply frustrating.

The critical problem is the insular role of the Fund with respect to other development partners and local stakeholders when it designs and negotiates macro-economic conditions. Donors felt disempowered relative to the IMF, given its capacity for macro-economic analysis. Some donors said that there was no room for discussion, as the macro-philosophy of the Fund is so deeply entrenched.

### **6.3 IMF conditionality**

All stakeholders – GoM, donors and civil society – expressed difficulties with the role played by the IMF in the setting of macroeconomic targets. Some of the general process issues are described above. There were also frustrations around some of the targets set by the Fund. There were two serious areas of contention: ceilings on public sector pay and limits on the fiscal deficit and aid levels (see Box 1).

One of the 'underlying principles' of the MoU is *'GoM's commitment to pursuing sound macroeconomic policies (with reference to IMF 'on-track' status or an equivalent judgement'*. However, it is not clear in practice what 'an equivalent judgement' means and what donors would do if the IMF were to suspend its PRGF programme. This leaves the GoM in a very vulnerable position and the IMF in a very powerful one.

Given the failures by the IMF to align policy content and process to domestic priorities, there is a need for the GoM and donors to evaluate how macro-economic conditions are set and to put in place a system which reduces vulnerability to 'aid shocks' and which is based on broader sources of analysis.

### **6.4 Alternative frameworks for macro-economic performance assessment**

Ultimately, the judgement on appropriate macro-economic targets should be left to the GoM with approval by Parliament. The PARPA and PES have to be more explicit therefore, on what the macro-economic frameworks and targets are. The IMF must commit not to

interfere in this process but to provide impartial advice.<sup>31</sup> Donors in the G16 will obviously scrutinise these targets and hold dialogue with the GoM. They also need to use their leverage as shareholders to gain the transparency that will allow them to monitor the IMF's agreements with the GoM, to ensure that these are not counter to poverty reduction.

Where issues are disputed, such as the introduction of macro-economic policy with evident poverty reduction implications, an independent Poverty and Social Impact Analysis (PSIA) should be carried out.

There appears to be some thinking around how the frameworks for macro-economic performance assessment could be opened up. The IMF's Independent Evaluation Office (IEO) and World Bank's Operations Evaluation Division (OED) recommended a macroeconomic working group, which would be government-led but could be opened out to all stakeholder groups.<sup>32</sup> This is an idea which had support from some other members of the G16. However, it is not clear how far this thinking will translate into action.

One option is to broaden the G16 macroeconomic working group into a forum which would include the other non MDDBS donors, GoM, academics and civil society. However, this would change its function somewhat, as the group currently develops joint responses to the IMF as budget support donors. There is little reason why debates could not happen here however, with donors convening separately to work on common responses to IMF / GoM proposals and making those responses available to the wider group.

Gerster and Harding recommend that the conditionality of the PRGF should be 'as far as possible aligned to the PAF' (2004a, p. 39). We believe that PRGF conditions should come from the broader PES, as it represents a holistic view of government intentions and is presented to Parliament under current procedures, whereas the PAF is not.

We recommend therefore that a multi-stakeholder macroeconomic working group should be constituted to develop PARPA II macroeconomic policy. It should include the GoM, IMF, World Bank, G16 and other donors, academics, representatives from Parliament and civil society. This group should then oversee the macro-economic targets underpinning the PES annually, from which the macroeconomic section of the PAF would be drawn. PRGF conditionality – which is reviewed and amended every six-months as a matter of course – should be strictly limited to the macroeconomic targets in the PARPA and PES.

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<sup>31</sup> IMF interference in systems of domestic democratic decision-making is not uncommon. In Tanzania, the draft budget has been presented to the IMF before being sent to Parliament.

<sup>32</sup> IEO IMF / OED World Bank, 'Republic of Mozambique – Evaluation of the PRSP and arrangements under the PRGF' (July 6, 2004).

**Box 1:  
IMF conditionality in Mozambique**

**Public sector wage bill**

The IMF's PRGF includes a target to reverse the 'unduly large wage adjustments' seen between 1999 and 2003 when the wage bill grew from 6% to 7.5% of GDP. However, at the same time many donor assessments of Mozambique have highlighted the need to substantially invest in the public sector to ensure the country can achieve the MDGs. Arguably, this level of public expenditure is not excessive and is broadly in line with or under an acceptable level. World Bank interviewees indicated that generally macroeconomic stability required the wage bill to be under 10% of GDP – giving Mozambique flexibility of up to 2.5% of GDP to reform the public sector through recruitment and improved salaries.

The argument for the condition to reduce the wage bill was that the IMF wanted the government to ensure public sector expansion was partnered by public-sector reform, including removing ghost-workers and improving inefficient systems.

A major debate on public sector employment, pay and IMF conditionality was catalysed by a proposal by the GoM to employ a further 10,000 civil servants, primarily teachers. The IMF, along with the World Bank objected, ostensibly on the grounds that it was not clear whether so many trained teachers could be found and also on the basis that the public sector reform programme has not been developed (a study on public sector salaries is underway but not yet completed).

Donors held the view that the IMF is relatively nuanced on this issue – that it would not restrict increases in public sector pay provided these were accompanied by investment in the infrastructure that would enable improved impact. However, these are assumptions rather than IMF policy positions as reflected in PRGF documentation.

The 'unknowns' include: what would happen were the individuals involved on the IMF side to change – the institutional bias is still towards restricting the deficit and targeting public sector pay in particular. What would happen were the GoM to find itself unable to implement the public sector reforms recommended, given the fact that the current reform agenda is stretching the GoM to capacity already? The high risks involved demand a clearer position on the degree of flexibility that the GoM can expect from the IMF.

Fiscal deficit and aid absorption

The IMF has set a ceiling for the fiscal deficit of 3% of GDP and has said that this can be increased by a maximum of 0.5% to accommodate increased aid flows. This was contested by GoM interviewees, who felt that this ceiling was undermining the potential to invest in development programmes.

The IMF in Mozambique argues, and donors accept, that unless donors make longer-term commitments on aid flows – up to 10 years (as the UK has recently done in Tanzania) – the Fund must take a conservative view of external finance flows. However, there is sufficient cause for concern about the impact of such a restrictive policy, for this condition to be subject to external analysis. Such analysis (Poverty and Social Impact Assessment – PSIA) has not been carried out on the fiscal deficit or public sector wage bill.

Overall, a broader view must be taken with respect to such policies. When poverty reduction is so reliant on the public sector, excessively stringent conditions on public

sector reform and the fiscal deficit could turn out to be significant obstacles to MDG achievement. It is important that the IMF, GoM and donors determine means to carry out Poverty and Social Impact Assessments (PSIAs) on macro-economic policies which have such profound implications for poverty reduction.

**Box 2:**  
**World Bank conditionality in Mozambique**

On joining the then-G14, the Bank attempted to have extra conditions attached to the PAF, but this was not accepted. The Bank have now pledged not to have any PRSC conditions that are additional to the PAF. They are instead focusing on promoting the privatisation and commercialisation of the country's infrastructure through several project loans, as described in the current PRGF:

'The projects envisage private sector participation in electricity distribution; privatisation of the telecommunications company and the national airline...; management contracts for water systems in several systems in several cities, and private concessions to operate some ports. In addition, the government is considering options for the possible divestiture of Petromoc, the state-owned petroleum distributor'.

There are clear concerns that whilst the Bank is coordinating conditionality with the G16 through the PAF, it is using project lending to promote and encourage significant structural reforms. It can be argued that the Bank is therefore getting the best of both worlds – participating in G16 policy discussions and using individual project loans to promote specific reforms.

The Bank decision to align fully with the PAF has implications for Bank support for trade liberalisation also, as they want to see a reduction in Mozambique's highest tariff from 30% to 25%, in line with incoming SADC targets. Yet trade liberalisation is not in the PAF, therefore it appears that this will have to be pursued through policy dialogue or project-associated conditions.

Both examples point to the need to monitor the extent of project-based conditionality which falls outside of the PAF and which may make attempts to limit the PAF to critical and universally agreed performance targets meaningless.

## 7. Systemic Issues

There are a number of serious systemic issues around the MDBS and wider systems of aid delivery in Mozambique.

These include:

- G16 members have made radically different levels of financial commitment to the MDBS system. Some donors appear to have paid in the minimum respectable amount in order to get a seat at the table of this forum, which has effectively replaced the UN / World Bank-led Development Partners' Group as the primary forum for donor – GoM dialogue. This calls into question the genuine commitment of some donors to the MoU. It may also lead to a hierarchy of PAF conditions, with the government prioritising the policy recommendations and targets of major donors over others whose contributions are lower.
- There is a fundamental debate within the G16 about the degree to which donors should be clear and transparent around their 'ownership' of specific conditions within the PAF. This illustrates the deep differences in approaches by donors to multi-donor budget support. Some take a holistic view of government commitment, while other demand rigorous fulfilment of each individual target.
- Observers (non G16 members) can participate in almost all discussions (bar voting) in the G16. There is therefore a lack of clarity on the incentives for donors to commit to the MoU as well as a lack of internal cohesion amongst G16 members.
- The level of exceptions in Annex 10 is unacceptably high and threatens to weaken the MoU to the point of being meaningless. The PAP's PAF sets an inadequate target for achieving the commitment of eliminating bilateral conditions and bilateral administrative and reporting requirements.
- The current share of budget support in overall aid is 35 – 40%, leaving the bulk of aid being delivered outside of the MDBS system in project form and on a single-year basis. Given the proliferation and lack of coordination of projects, this raises questions around overall aid effectiveness. It is possible that the MDBS system is increasing coordination around budget support at the expense of coordination of aid delivered under other modalities. There is no overall mechanism to cover all modalities.
- The high level of direct funding of sectors and off-budget support means that many line ministries engage primarily in dialogue around policy and finance with the donors rather than with the Ministry of Planning and Finance. Policy is developed, budgets administered and services delivered by 23 different ministries that are only weakly coordinated by the centre. There is reluctance by line ministries to move away from this system.
- There has been a lack of effective government mechanisms to develop PAF indicators which are consistent with line ministries' policy priorities, although having sector reviews in advance of the Joint Review should help resolve this.
- The PES is too broad to be an operational development plan, according to donors. The PAF has become the de facto tool for prioritised implementation of and reporting on government programmes, displacing the national instrument (Balanco Do PES)



for reporting to Parliament on implementation of the PARPA. This reinforces government accountability to donors rather than to its citizens.

- Recent experience shows that the state budget systems must be strengthened to make them function independently of electoral cycles and to allow the MDBS system to work effectively alongside them.
- The 'split response' mechanism means that the GoM may need to have contingency elements in its budget, as the disbursement of the variable tranches from some donors is uncertain until very late in the process. Even if variable tranches are relatively small, this system is contrary to the principle of strengthening the budget as an effective instrument for implementing the PARPA. It also clearly creates an added burden which the MDBS systems is meant to avoid – protracted and detailed donor-by-donor discussions around specific conditions.
- G16 country offices still only have limited ability to ensure punctual disbursement due to lack of delegation of power from head office to country office.
- With an MDBS, the GoM is potentially more vulnerable to donor volatility, given that donors may act collectively 'in response to perceived violations of the 'underlying principles' (which are difficult to define and predict in advance). This clearly means that, unless there is greater clarity around how the macro-economic and other 'underlying principles' are to be interpreted and donor responses implemented, the GoM will constantly be in a state of vulnerability.
- There have been creative means used to increase the number of PAF indicators beyond agreed levels (50 indicators). Agreement on even this number was very difficult to achieve. There is a need to reach further agreement on both the criteria for and a reduced upper limit on PAF conditions.
- There is a significant imbalance in accountability between donors and government in the MoU. The use of Annex 10 exceptions is prolific and PAP's PAF lacks adequate targets for almost half of the commitments it contains. The GoM has no form of redress if donors fail to meet their commitments.
- Parliamentary oversight is limited. The PES and Balanco do PES are presented to Parliament but not the PAF (although there are plans to attach the PAF to the PARPA and the PES, which will make it a public document). It was not consulted on the original PARPA. There are internal reasons for weak parliamentary involvement including the capacity of MPs and the lack of will to scrutinise the government effectively due to the 'list' electoral system. It is highly unlikely that domestic accountability will be developed via the legislature without electoral reform, although donor support may engender some improvements.
- Civil society capacity is also extremely limited. While an important group, the G20 has not yet been able to rise to meet the challenges and opportunities present in the PARPA, PES and PAF frameworks. There is a clear need for long-term approaches to civil society strengthening. This goes for both urban-based groups such as members of the G20 and their affiliates / other organisations at provincial and district levels
- The IMF has failed to align its PRGF to both the content and temporal cycles of GoM policy. Its dominant role in setting the parameters for GoM policy is given further weight by the inclusion of an off-track IMF programme as potential grounds for

suspension of the MoU. This leaves the GoM in a permanent state of vulnerability. The local IMF office engages as far as possible with other donors but institutionally, the IMF operates in a narrow, closeted manner with a limited group of GoM / Central Bank officials.

- There is a clear need to align IMF policy and processes with PARPA and PES processes, and to increase transparency and multi-stakeholder dialogue on macro-economic policy, including the PRGF.

## **8. Recommendations**

- **GoM planning and aid management**

The GoM needs to develop an overall external assistance management strategy. This should take the form of a joint agreement with all donors (not just budget support donors) on aid modalities, coordination, harmonisation and conditionality. It should include monitorable targets for donors' performance and a clear articulation of the consequences for the GoM of failure to comply with the principles of this agreement. The obvious donor coordination framework would be the UNDP-led Development Partners Group.

To address the lack of articulation between line ministry and central government (e.g. Ministry of Planning and Finance (MPF)) harmonisation efforts, the GoM needs to show stronger leadership in developing a coherent planning system to include all ministries. This is linked to the need for donors to subordinate policy dialogue at sector level to the GoM's dialogue with its line ministry. Donors must ensure that their interventions reinforce rather than undermine coherence in overall national policy-making.

As PARPA II is under development, this is an important opportunity to implement the above recommendations.

- **The MoU and PAF**

Predictability is seriously hampered both by donor failure to adhere to disbursement agreements in the MoU and the liberal use of exceptions in Annex 10. Donors must be held to account on their commitment to reduce these exceptions.

The current target in the PAF for eliminating bilateral conditional and administrative and reporting requirements is entirely inadequate. A revised target should be adopted as part of annual transparent reporting on each donor's individual performance under the Programme Aid Partners' (PAP's) PAF.

Conditions attached to projects and programmes which are outside of the MoU also need to be streamlined and harmonised, within an overarching system as in Recommendation 1. Overall PAF conditionality should be reduced and streamlined in accordance with the GoM's priority areas under PARPA. Agreement should be reached on both the criteria for and a reduced upper limit of PAF conditions.

- **The MoU and Mutual accountability**

The imbalance in accountability between the GoM and the G16 in the MoU needs to be addressed.

The underlying principles – and particularly that of adherence to pursuing sound macro-economic policies, with reference to an on-track IMF programme or equivalent judgement, should be clarified. All donors should reach agreement with their capitals best word headquarters that an off-track IMF programme will not result in automatic suspension of budget support. This should be captured in the MoU.

The PAP's PAF needs to be simpler, more progressive in terms of commitments and it should contain targets for each commitment and indicator. Individual donor performance

should be tracked, rather than an overall assessment of the performance of the donors as a group.

Further mechanisms to ensure a high degree of commitment of donors under the MoU should be explored – including the suspension of under-performing G16 donors or delivery of a minimum per cent of aid flows in budget support.

Annual reporting on the PAP's performance should be carried out independently and made publicly accessible. At a minimum, the report should be presented to the Parliament and Poverty Observatory. A summary in accessible language should be printed in national newspapers also. Donors should also report to their home parliaments on targets in the Paris declaration on aid effectiveness and against targets set locally – such as those in the PAP's PAF.

- **Capacity Development and the GoM**

There is a need for greater cooperation and the establishment of agreed, coordinated systems (including joint funding mechanisms) for capacity development in the GoM. It is vital that capacity development is long-term and prioritises the government's role in selecting both priorities and processes for capacity development, including the selection of consultants. The commitment of the PAP's PAF to take this issue further needs to be followed up but it also needs to be articulated with capacity development efforts by non-G16 donors. An appropriate forum for discussion may be the UNDP / World Bank-led Development Partners Group.

- **The Role of the IMF**

In the short term, there is a need for a formal agreement between the GoM, parliament and IMF that existing PRGF targets and mechanisms will not predetermine the outcome of the PARPA II.

IMF advice to the GoM on the development of the PARPA macro-economic framework should be subject to scrutiny by other stakeholders, including Parliament, civil society members (non-governmental organisations (NGOs), private sector and academics), and other donors. The IMF should justify its assumptions and policy advice to a multi-stakeholder macro-economic working group and to Parliament. It should illustrate how feedback from this group and Parliament impacts on its policy advice going forward.

The GoM should work together with this multi-stakeholder group to identify areas where independent analysis is warranted, particularly where IMF macro-economic policy proposals are likely to have an impact on poverty reduction.

On finalisation of PARPA II, a new PRGF programme (if one is deemed necessary by the GoM) should be drawn up based only on policy and targets in the PARPA II.

In general, IMF conditionality should be contained in the overall donor conditionality framework, and in the G16 PAF. It should be reduced to include only verifiably macro-critical issues which are drawn from the PARPA / PES.

- **The World Bank**

There are concerns that while the Bank is coordinating Poverty Reduction Support Credit (PRSC)-related conditionality within the G16, the reform agenda promoting privatisation and deregulation is instead being pursued through the Bank's project lending. The Bank should commit to streamlining and alignment of all its lending and activities, under a joint agreement with all donors (not just budget support donors) on aid modalities, coordination, harmonisation and conditionality, as above.

There is a clear need for parliamentary scrutiny of World Bank loan agreements and their policy content. Given the lack of capacity for analysis and debate in Parliament, a broader strategy of scrutiny of Bank lending is required. This should be subject to the same scrutiny suggested for IMF policy under the proposed multi-stakeholder macro-economic group, above.

- **Civil society**

The GoM needs to undertake initiatives to make the PES (annual budget implementation plan) and the annual report on the PES - BdoPES - more accessible and digestible to civil society, using appropriate media and language, along with provincial / district-level consultation. The GoM and PAPs need to agree how to make the PAF accessible in these fora.

With regard to the MDBS, the GoM and G16 should create more space for civil society participation in joint and mid-year discussions, without overloading the process. Dialogue sessions with civil society should be held before and at least twice during these reviews, with access by civil society to draft texts. A civil society declaration at the end of the reviews should be attached to the Aide Memoire.

In the meantime, the GoM must develop a comprehensive and meaningful strategy for participation in PARPA II decision-making, as part of the institutionalisation of democratic governance.

A wider, deeper and more sustained effort by donors to support civil society is needed. This should be based on an agreed approach to capacity development between representative civil society groups such as the G20, and donors with a commitment to supporting civil society.

- **Parliament**

Donors should engage with Parliament under specific programmes to strengthen capacity to carry out their legitimate functions.

There is also a need for donors to create more space for parliamentary oversight through opening up the processes around the MoU to parliamentary scrutiny. The PAF should be formally presented to parliament as part of the PES, while the formal or informal mechanisms to present the PAP's PAF should also be determined.

## Appendix I: List of Interviewees

Karin-Annette Anderson, Economist, SIDA  
Paula Assibuji, PAP Secretariat  
Michael Baxter, Country Director, World Bank  
Gregor Binkert, Lead Economist, PREM, World Bank  
Luisa Capelao, Senior Policy analyst / Economist, USAID  
Eamon Cassidy, Head of Cooperation, UK Department for International Development  
Carlos Chenga, Comissão de Plano e Orçamento, Assembleia da República  
John Coughlin, Programme manager, Trócaire  
Ian Dolan, Country Director, Trócaire  
Keith Gristock, Head of Cooperation, Development Cooperation Ireland  
Alicia Herbert, Social Development Adviser, UK Department for International Development  
Telma Loforte, Economist, Swiss Agency for Development & Cooperation  
Sylvie Millot, Head of Section, Political/Economic Affairs, Delegation of the European Commission  
Alison Milton, Programme Officer, Development Cooperation Ireland  
Matt Pickard, Country Representative, Christian Aid  
Perry Perone, Resident Representative, International Monetary Fund  
Eufragina dos Reis Manoela, Coordenadora, Grupo Moçambicano da Dívida  
Graça Samo, Coordenadora, Fórum Mulher  
Carsten Sandhop, Director, German Development Bank (KFW)  
Heidi Sedleczi, Ministry for Economic Cooperation and Development  
Clara de Sousa, Banco de Moçambique  
José Sulemane, Director Nacional, Direção Nacional Plano e Orçamento  
Adriano Ubisse, Assistant Director, National Economic Research Bureau, MPF  
Simon Vanden Broeke, Economic Advisor, DFID  
James Watson, Programme Officer, USAID  
Bridget Walker Muiambo, Education Advisor, Development Cooperation Ireland  
Teodosio Wazella, Bank of Mozambique

## **Appendix II: Reference Documents**

Gerster and Harding (2004), 'Baseline Survey on PAP Performance in 2003'.

Gerster and Harding (2004a) 'Learning Assessment of Joint Review 2004';

Memorandum of Understanding Between the Government of the Republic of Mozambique and the Programme Aid Partners for the Provision of Direct Budget and Balance of Payments Support, April 2004

OECD – DAC (2004) Survey on Progress in Harmonisation and Alignment 2004 – Mozambique Country Chapter.

## Appendix III: Aid levels in Mozambique

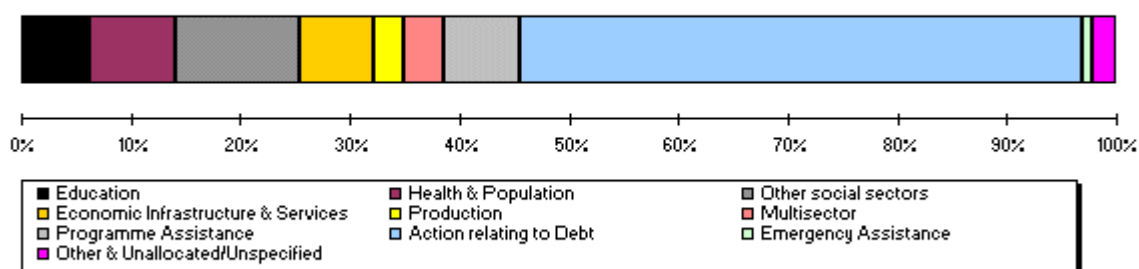
### Mozambique

Receipts	2001	2002	2003
<b>Net ODA (USD million)</b>	933	2 054	1 033
<b>Bilateral share (gross ODA)</b>	75%	81%	66%
<b>Net ODA / GNI</b>	29.8%	60.3%	25.2%
<b>Net Private flows (USD million)</b>	115	70	- 60

<i>For reference</i>	2001	2002	2003
<b>Population (million)</b>	18.1	18.4	18.8
<b>GNI per capita (Atlas USD)</b>	200	200	210

Top Ten Donors of gross ODA (2002-03 average) (USD m)	
1	France 240
2	Italy 231
3	IDA 159
4	United States 148
5	Germany 134
6	EC 115
7	Denmark 60
8	United Kingdom 56
9	AfDF 54
10	Japan 53

**Bilateral ODA by Sector (2002-03)**



Sources: OECD, World Bank.