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## Sovereign Wealth Funds in Africa: Taking Stock and Looking Forward

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# Abstract

This paper provides a primarily qualitative analysis of sovereign wealth funds (SWFs) on the African continent. It explores SWF mandates, including macro-economic management, savings and development, and their ability to combat the so-called resource curse. Case studies in Angola, Botswana, Ghana and Nigeria assess SWFs' institutional structure, investment performance, and accountability and oversight mechanisms in order to determine their effectiveness in fulfilling these mandates. The findings highlight policy priorities for developing countries looking to establish SWFs, as well as policy adjustments for existing SWFs on the continent. Key findings include the importance of designing SWFs with robust fiscal rules, targeted investment mandates and accountability mechanisms that divert political incentives to misuse funds, as well as integrating SWFs within broader public financial management reform. Managing soft issues such as political and public expectations, awareness creation and buy-in are also critical and often overlooked in the technical design of SWFs.

## Introduction

The discovery of natural resources should be a blessing for a country's national growth and development prospects. Paradoxically, the so-called resource curse is a phenomenon where large natural resource endowments often correlate with lower-than-expected economic growth as well as weaker, more authoritarian institutional development.<sup>1</sup> The best-known explanation for this effect is that resource revenue inflows lead to real exchange rate appreciation, which erodes the competitiveness of other non-export sectors. This is also called the Dutch disease.<sup>2</sup> Additional explanations point to the difficulties that highly fluctuating commodity prices pose for the stable management of macro-economic cycles, and the fact that lucrative resource wealth creates incentives for political contestation of resources and looting. Given that explanations for the resource curse enjoy some consensus, policy recommendations to combat it have also proliferated. However, devising policy solutions that are practically implementable, especially for developing countries with fragile institutions and weak public financial management (PFM), remains a persistent challenge.

Over the last two decades development partners such as the International Monetary Fund (IMF) and World Bank have increasingly advocated for governments in developing countries to establish state-owned investment vehicles, or sovereign wealth funds (SWFs), to manage

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1 Ross ML, 'What have we learned about the resource curse', *Annual Review of Political Science*, May 2015, pp. 239-259; NRG (Natural Resource Governance Institute), *The Resource Curse*, March 2015, [https://resourcegovernance.org/sites/default/files/documents/nrgi\\_primer\\_resource-curse.pdf](https://resourcegovernance.org/sites/default/files/documents/nrgi_primer_resource-curse.pdf), accessed 20 October 2019.

2 NRG, 2015, *op. cit.*

and invest resource revenues.<sup>3</sup> SWFs may have various objectives, which often include macro-economic stabilisation, savings for future generations, and domestic investment/development. Although the first SWF was established in Kuwait in 1953, these funds have proliferated throughout Africa more recently, with 12 SWFs currently operating on the continent. Several more African countries are considering establishing SWFs, including regional economic heavyweights South Africa and Kenya.

Given that many existing African SWFs will soon be reaching their 10-year anniversary, the time is ripe for an assessment of these funds to form policy recommendations for both currently operating funds and yet-to-be-established funds. This paper supports this objective through an in-depth policy and institutional analysis of SWFs in four African countries: Angola, Botswana, Ghana and Nigeria. The analysis examines the effectiveness of institutional structures and rules, investment activity and accountability measures, with reference to stated fund objectives. Ultimately, this paper seeks to understand specific areas where African SWFs are performing more or less effectively, in order to add to the existing body of policy work and give recommendations on making Africa-specific SWFs more fit for purpose.

## Setting the context: Why establish SWFs?

The scope of SWF definitions still varies widely and there is no official definition, complicating their analysis and comparability. However, most standard definitions of SWFs include that they are government-owned, serve as investment vehicles, and invest at least partly in foreign assets.<sup>4</sup> SWFs are also generally not linked to any explicit liabilities. While some SWF definitions include public pension funds, pension funds are not included in the scope of this paper.

Historically, SWFs have been established to manage natural resource-derived revenues. However, they may not be linked explicitly to resource revenues, and in some cases have been established to manage balance of payment (BoP) surpluses in countries with no natural resources. In Africa, most SWFs are either implicitly or explicitly linked to resource revenues, and therefore resource funds will be the focus of analysis. Literature broadly points to two important prerequisites for establishing a resource-based SWF, namely the

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3 Ghura D & C Pattillo, 'Macroeconomic Policy Frameworks for Resource-Rich Developing Countries', IMF (International Monetary Fund), 2012, <https://www.imf.org/external/np/pp/eng/2012/082412.pdf>, accessed 10 September 2019; Davis JM, 'Stabilization and Savings Funds for Non-renewable Resources: Experience and Fiscal Policy Implications', IMF, 205, 2001, <https://www.imf.org/external/pubs/nft/op/205/>, accessed 10 September 2019; Gelb A et al., 'Sovereign Wealth Funds and Long-Term Development Finance: Risks and Opportunities', World Bank, 2014, <https://openknowledge.worldbank.org/handle/10986/17313>, accessed 10 September 2019.

4 Bauer A, Toledano P & M Rietveld, 'Managing the Public Trust: How to Make Resource Funds Work for Citizens', NREGI & CCSI (Columbia Center on Sustainable Investment), 2014a, [https://resourcegovernance.org/sites/default/files/NRF\\_Complete\\_Report\\_EN.pdf](https://resourcegovernance.org/sites/default/files/NRF_Complete_Report_EN.pdf), accessed 15 September 2019.



expectation of large capital inflows and existing low public debt.<sup>5</sup> A country with these conditions will likely experience revenue volatility if fiscal policy adjustments are not made. Dutch disease will also likely occur in countries where foreign currency inflows are large relative to the size of gross domestic product (GDP).<sup>6</sup> Importantly, if public debt is high, it is usually advisable to first pay off existing debt to improve borrowing terms, and only then consider establishing a fund.<sup>7</sup>

SWFs may be designed with one or more explicit policy objectives or mandates, which implies quite distinct institutional set-ups as well as expected macro-economic outcomes, depending on the objective(s). It is therefore worth exploring the various objectives of SWFs in detail. Based on the observed mandates of African SWFs, three potential policy objectives are examined below: stabilisation, savings/sterilisation and domestic investment.

## Stabilisation

Resource revenues often accrue in large amounts and are subject to volatile prices and production, which cannot be forecasted with certainty. Given the autocorrelative nature of commodity prices, while small fluctuations may occur frequently, large variations come more rarely but often persist for extended periods.<sup>8</sup> The discovery of resources can therefore have a destabilising effect on the budget cycle, leading to disproportionate and inefficient spending during resource booms and budget shortfalls during busts.<sup>9</sup>

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Stabilisation should ideally be achieved within fiscal and monetary policy. General countercyclical fiscal policy can be carried out through automatic stabilisers, as well as by paying down debt in boom times and borrowing in bust times.<sup>10</sup> Monetary policy can also

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5 Mulder M *et al.*, 'Setting up a Sovereign Wealth Fund: Some Policy and Operational Considerations', IMF, 9-179, 2009, <https://www.imf.org/external/pubs/ft/wp/2009/wp09179.pdf>, accessed 10 September 2019; Skype interview, anti-corruption expert, 19 September 2019; Skype interview, development economist 1, 17 September 2019; Skype interview, international financial institution (IFI) representative 1, 20 September 2019.

6 *Ibid.*

7 Skype interview, resource governance policy expert, 13 September 2019; Senbet L, Wills S & W Simbanegavi, 'Sovereign wealth funds and natural resource management in Africa', *Journal of African Economies*, 25(suppl\_2), 2016, pp. ii3-ii19.

8 Skype interview, development economist 2, 17 September 2019.

9 Davis JM, *op. cit.*; Ghura D & C Patillo, *op. cit.*; Dixon AD & AH Monk, 'What role for Sovereign Wealth Funds in Africa's Development?', Center for Global Development, Oil-to-Cash Initiative Background Paper, 2011, [http://www.cgdev.org/doc/Initiatives/Oil2Cash/Final\\_Formatted\\_Monk\\_and\\_Dixon\\_SWF\\_10.11.pdf](http://www.cgdev.org/doc/Initiatives/Oil2Cash/Final_Formatted_Monk_and_Dixon_SWF_10.11.pdf), accessed 1 September 2019.

10 Resource governance expert, *op. cit.*

mitigate the effects of real exchange rate fluctuations and demand shocks by loosening in booms and tightening in busts. Therefore, resource revenues are sometimes managed with foreign reserves by central banks.<sup>11</sup>

However, fiscal policy in developing countries is often limited by borrowing constraints, which are exacerbated during commodity busts. Monetary policy is also less effective in developing countries if there is poor monetary policy transmission to interest rates and exchange rates, stemming from underdeveloped domestic capital markets or export sectors. Additionally, monetary policy is ineffective in many countries that maintain pegged exchange rates.<sup>12</sup> Therefore, if a country expects large enough resource windfalls, if central banks are not politically independent, and/or if countries are not able to execute monetary or fiscal policy effectively, a separate stabilisation fund may be advisable.<sup>13</sup>

Although no specific fiscal rule is appropriate in all country contexts, establishing an enforceable fiscal rule with little room for loopholes is essential for stabilisation funds to operate effectively

Fiscal stabilisation funds seek to support countercyclical fiscal policies through ring-fencing resource revenues subject to fiscal rules. For example, a simple fiscal rule can link deposits and withdrawals to an oil reference price, triggering deposits if revenues are above the reference price and withdrawals if they are below it. Alternatively, deposits and withdrawals can be linked to the business cycle; stabilisation funds could accumulate balances when the general government revenue spikes and can be drawn upon when the economy is in recession or during times of emergency. Although no specific fiscal rule is appropriate in all country contexts, establishing an enforceable fiscal rule with little room for loopholes is essential for stabilisation funds to operate effectively.<sup>14</sup> Stabilisation funds otherwise face the risk of succumbing to political pressures to spend when resource revenues are high, counteracting their countercyclical purpose. Designing fiscal rules that allow leniency for exceptional debt crises or development pressures, without allowing this leniency to be manipulated for purposes such as regular debt repayment and additional borrowing, remains a difficult and uniquely contextual challenge for these funds.<sup>15</sup> Additionally,

11 Venables AJ & SE Wills, 'Resource funds: Stabilising, parking, and inter-generational transfer', *Journal of African Economies*, 25(suppl\_2), 2016, pp. ii20-ii40.

12 *Ibid.*

13 IFI representative 1, *op. cit.*; resource governance expert, *op. cit.*

14 NRCI, *Fiscal Rules and Natural Resource Funds Methods to Save and Stabilize Revenues*, March 2015, [https://resourcegovernance.org/sites/default/files/nrci\\_Fiscal-Rules-and-NRFs.pdf](https://resourcegovernance.org/sites/default/files/nrci_Fiscal-Rules-and-NRFs.pdf), accessed 10 October 2019.

15 Bauer A, Toledano P & M Rietveld, *op. cit.*

effective rules crucially depend on independent, accurate and long-horizon commodity revenue projections.<sup>16</sup>

Given that stabilisation requires liquidity, stabilisation funds generally invest in short-term, liquid financial instruments such as high-grade, convertible sovereign debt (eg, US Treasury bills).<sup>17</sup> These funds can therefore serve as a buffer during negative economic shocks, where drawdowns can replace the need for external borrowing.

Stabilisation funds are often recommended as a first step for resource-expectant countries. It is, however, important to ensure that stabilisation funds do not build up excessively large balances, and a cap allows for additional revenues to then be placed in other sub-funds or budget items. This will protect a rapidly accumulating fund from becoming a target for political raiding, given the ease of converting liquid assets.<sup>18</sup> Additionally, a strong, rules-based fiscal stabilisation fund is meaningless if there are not similar discipline and fiscal rules in the general budget, especially if SWF revenue does not comprise a significant percentage of GDP.<sup>19</sup>

## Savings/sterilisation

From an ethical standpoint, the benefits of resource revenues should extend to future generations. However, in resource-rich countries, problems of inter-generational equity often occur when exhaustible resources are over-consumed by the current generation.<sup>20</sup> This can hypothetically be solved by investing resource revenues in capital, which translates into permanent income and continues to grow even after resources have been depleted. Stemming from this logic, savings funds seek to invest resource wealth in long-term assets (often abroad), in order to spread current wealth more evenly over time to benefit future generations. A savings fund is especially advisable for countries with smaller resource discoveries with projected shorter lifespans.<sup>21</sup> The optimal balance between consumption for current generations (especially in countries where basic public needs are not met) and investment for future generations has been subject to much economic modelling and debate. Previously, the IMF-endorsed permanent income hypothesis (PIH) was the gold standard for revenue management in resource-rich countries. The PIH fiscal rule states that

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16 Bawumia M & H Halland, 'Oil Discovery and Macroeconomic Management: The Recent Ghanaian Experience', World Bank Policy Research Working Paper, WPS 8209, 2017, <http://documents.worldbank.org/curated/en/388941507034520272/Oil-discovery-and-macroeconomic-management-the-recent-Ghanaian-experience>, accessed 10 October 2019; development economist 2, *op. cit.*; resource governance expert 2, *op. cit.*

17 Senbet L, Wills S & W Simbanegavi, *op. cit.*; Bauer A, Toledano P & M Rietveld, *op. cit.*

18 Anti-corruption expert, *op. cit.*; Wills S, 'Leave the volatility fund alone: Principles for managing oil wealth', *Journal of Macroeconomics*, 55, 2018, pp. 332-352.

19 *Ibid.*; development economist 2, *op. cit.*

20 Hartwick JM, 'Intergenerational equity and the investing of rents from exhaustible resources', *The American Economic Review*, 67, 5, 1977, pp. 972-974; Solow RM, 'On the intergenerational allocation of natural resources', *The Scandinavian Journal of Economics*, 1986, pp. 141-149.

21 Development economist 1, *op. cit.*; Skype interview, IFI representative 2, 27 September 2019.

present consumption should be limited to interest accrued on saved resource wealth.<sup>22</sup> In recent years, the IMF has adjusted this stance and devised two new policy options for developing countries that are both capital and credit constrained.<sup>23</sup> Given that these countries face high risk premiums, borrowing at high interest rates while earning lower returns on savings makes little economic sense. The 'modified PIH' accommodates present-day constraints by advocating scaled-up investment of resource revenues in the medium-term, followed by scaling down to preserve net financial wealth at PIH-determined levels. The 'fiscal sustainability framework' also advocates for initial scaling up of investments, but accounts for the economic growth impacts and depreciation of investments. Although financial wealth derived from resources stabilises at a lower level than the PIH, fiscal spending stabilises at a higher level owing to the positive impacts of investments on the non-resource budget.<sup>24</sup>

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Given their long-term nature, savings funds can invest in riskier, illiquid assets, and generally seek higher returns in international financial markets.<sup>25</sup> Savings funds also have the dual effect of sterilisation, which may help mitigate Dutch disease effects where this is a problem. When revenues are invested abroad, less capital inflows accrue to the domestic economy, which curbs excessive currency appreciation (or potentially inflation, if the currency is pegged).

Savings funds also have spill-over effects. Requiring a portion of funds to be saved abroad limits potential absorption constraints in the domestic economy such as low investment returns and wage and price pressures, caused by scarce viable domestic investment opportunities and limited domestic capacity to plan and implement projects.<sup>26</sup> Savings abroad also provides portfolio diversification when a portion of resource revenues is insulated from the performance of the domestic economy. Funds locked away in foreign long-term assets are also less easily accessed for political purposes than funds held in more liquid form. Lastly, a savings fund often improves international perception of a country's PFM and ability to pay back loans, leading to better credit ratings and cheaper borrowing

22 Barnett S & R Ossowski, 'Operational aspects of fiscal policy in oil-producing countries', IMF Working Paper, WP/02/177, 2002, <https://www.imf.org/en/Publications/WP/Issues/2016/12/30/Operational-Aspects-of-Fiscal-Policy-in-Oil-Producing-Countries-16121>, accessed 21 September 2019.

23 Chura D & C Pattillo, *op. cit.*; Van der Ploeg F & AJ Venables, 'Harnessing windfall revenues: Optimal policies for resource-rich developing economies', *The Economic Journal*, 121, 551, pp. 1-30; Wills S, *op. cit.*

24 *Ibid.*

25 Senbet L, Wills S & W Simbanegavi, *op. cit.*; Bauer A, Toledano P & M Rietveld, *op. cit.*

26 *Ibid.*

costs.<sup>27</sup> The effects of a savings fund on lowering the risk premium must therefore be carefully weighed against potentially low returns abroad, and the urgency of spending needs at home weighed against inter-generational savings.

## Domestic investment

SWFs branded with domestic investment mandates have been established more recently. However, in essence this can be viewed as a new label for extra-budgetary funds that derive financing from resource revenue. The popularity of these funds aligns with the changing global consensus towards investing a portion of resource wealth immediately to alleviate capital constraints.<sup>28</sup> Analysis of development SWFs is muddled, as there are different types of domestic investment activities. Firstly, a development fund can invest in capital projects that form part of the normal budget; generally projects with low financial returns and high social returns. Policy literature has largely opposed this type of development fund, as it unnecessarily fragments budget spending and increases opportunities to bypass project appraisal and procurement processes within the budget.<sup>29</sup> This increases opportunities for corruption and to fund politicised or excessively risky projects. If the normal budget process suffers from mismanagement, it is highly unlikely that a parallel fund will effectively self-insulate from such pressures. Resource revenues intended for social investments should rather be channelled directly through the budget (along with necessary budget reforms), which is indeed an important objective in capital-scarce countries facing high risk premiums.<sup>30</sup>

Secondly, development funds can be set up as special purpose funds to invest in projects with high financial return (as well as some level of social return, given that they are still public-owned investment funds).<sup>31</sup> These funds essentially function as development banks. Special purpose funds may be established as catalytic funds, primarily to crowd in international private or institutional finance by providing first-loss capital. They can also seek to attract co-partnership on an equal basis, or even attract capital at fund level rather than project level if there is significant fund credibility, although this has not as often been the case in developing countries.<sup>32</sup> It is possible that the existence of an investment fund in and of itself may increase the chances of attracting external capital, through signalling that the project has political will behind it as well as the contextual knowledge of a local partner.<sup>33</sup> If such funds are invested in trusted, illiquid, high-return assets, in essence the investment can also serve a dual savings purpose.<sup>34</sup>

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27 Yousefi M, 'Public Sector Balance Sheet Strength and the Macro Economy', IMF, WP/19/70, August 2019, <https://www.imf.org/en/Publications/WP/Issues/2019/08/06/Public-Sector-Balance-Sheet-Strength-and-the-Macro-Economy-48529>, accessed 25 October 2019.

28 Gelb A *et al.*, 'Sovereign Wealth Funds and Long-Term Development Finance: Risks and Opportunities', World Bank, <https://openknowledge.worldbank.org/handle/10986/17313>, accessed 10 September 2019.

29 *Ibid.*; resource governance expert, *op. cit.*; development economist, 1 *op. cit.*; IFI representative 1, *op. cit.*

30 *Ibid.*

31 Gelb A *et al.*, 2014, *op. cit.*; IFI representative 1, *op. cit.*

32 IFI representative 1, *op. cit.*

33 Anti-corruption expert, *op. cit.*

34 Development economist 2, *op. cit.*



Domestic investment funds are often ring-fenced to invest in a specific sector. More recently, many African infrastructure SWFs have been established, promoted by global partners such as the Organisation for Economic Co-operation and Development, the African Development Bank and AU as an important tool to help fill the African infrastructure financing gap.<sup>35</sup> Given that infrastructure is a long-term, illiquid, higher risk investment, this matches the long-term liability-free nature of SWFs. Less liquidity can have the added spinoff of increasing the difficulty of raiding the fund.<sup>36</sup> Infrastructure also shows less correlation with traditional assets because its primary growth comes from income growth rather than asset appreciation, providing diversification for an SWF investment portfolio.

A number of cautions are levelled against all types of development funds, with some experts maintaining that there is rarely sufficient motivation for their establishment.<sup>37</sup> Firstly, the risk of political interference is high for any domestically intended investments in countries with weak PFM, regardless of strict specifications and regulations on paper. Secondly, such investments are liable to counteract sterilisation objectives and/or fiscal rules and lead to capacity constraints if capital is flooding into the economy when resource revenues are high and viable investment opportunities are few.<sup>38</sup> In this case, projections may show that resource revenues will continue to drive demand, but this is ultimately predicated on continued favourable economic conditions, which repeated commodity price crashes have shown is never a certainty.<sup>39</sup> Therefore, gradual and incremental investment strategies are important considerations for any development fund, and overall these funds should be pursued with greater caution.

## Management of SWFs: Institutional considerations

In developing countries especially, the success or failure of SWFs often comes down to the strength of their institutional structure and management. It follows that a large portion of SWF literature is devoted to best practice guidelines for institutional structures, governance, investment/risk management strategies, and transparency and accountability in management and reporting.

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35 Della Croce R & J Yermo, 'Institutional Investors and Infrastructure Financing', OECD (Organisation for Economic Co-operation and Development) Working Paper on Finance, Insurance and Private Pensions, 36, 2013, [http://www.oecd.org/daf/fin/private-pensions/WP\\_36\\_InstitutionalInvestorsAndInfrastructureFinancing.pdf](http://www.oecd.org/daf/fin/private-pensions/WP_36_InstitutionalInvestorsAndInfrastructureFinancing.pdf), accessed 10 September 2019; AU-NEPAD, 'Continental Business Network (CBN) - 5% Agenda Report', 2017, <http://www.au-pida.org/download/au-nepad-continental-business-network-cbn-5-agenda-report/>, accessed 25 October 2018; AfDB (African Development Bank), *African Economic Outlook*, 'Chapter 4: Financing Africa's Infrastructure: New strategies, mechanisms, and instruments', 2018, [https://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/2018AEO/African\\_Economic\\_Outlook\\_2018\\_-\\_EN\\_Chapter4.pdf](https://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/2018AEO/African_Economic_Outlook_2018_-_EN_Chapter4.pdf), accessed 10 October 2019.

36 Development economist 2, *op. cit.*

37 Resource governance expert, *op. cit.*; development economist 1, *op. cit.*; IFI representative 1, *op. cit.*

38 Gelb A *et al.*, 2014, *op. cit.*

39 IFI representative 2, *op. cit.*

A number of assessment tools have been developed for this purpose. In particular, the International Forum for SWFs has gained prominence as a voluntary grouping of SWFs that in 2008 agreed to develop and adhere to SWF governance principles (the Santiago Principles).<sup>40</sup> Although the Santiago Principles have been criticised as providing a low standard for governance and transparency (given their initiation by SWFs themselves), in the same vein this has increased the willingness of funds to sign up to and begin to implement reforms.<sup>41</sup> However, the Truman Scoreboard,<sup>42</sup> developed in 2008 by Edwin Truman of the Peterson Institute of International Economics, is a more stringent assessment framework for SWF management. The Truman Scorecard is divided into four categories: structure, governance, transparency and accountability, and behaviour, with a final score reflecting the percentage of possible points achieved (out of 100). Table 1 shows the metrics used to assess each category.

<b>Structure</b>	<b>Governance</b>	<b>Transparency and accountability</b>	<b>Behaviour</b>
Objective stated	Role of government	Categories	Risk management
Legal framework	Role of governing body	Benchmarks	Policy on leverage
Changing the structure	Role of managers	Credit ratings	Policy on derivatives
Investment strategy	Decisions made by managers	Mandates	Portfolio adjustment
Source of funding	Internal ethical standards	Size	
Use of fund earnings	Guidelines for corporate responsibility	Returns	
Integrated with policies	Ethical investment guidelines	Locations	
Separate from international reserves		Specific investments	
		Currency composition	
		Annual reports	
		Quarterly reports	
		Regular audits	
		Published audits	
		Independent audits	

Source: Peterson Institute, 'A Blueprint for Sovereign Wealth Fund Best Practices', Policy Brief, Pb07-4B08-3, April 2008, <https://www.piie.com/sites/default/files/publications/pb/pb08-3.pdf>, accessed 11 October 2019

Below, this paper briefly describes specific management issues that have proven to be particularly relevant and challenging for African SWFs, under the categories of investment and operational management.

40 IFSWF (International Forum for Sovereign Wealth Funds), 'Santiago Principles', <https://www.ifswf.org/santiago-principles-landing/santiago-principles>, accessed 11 October 2019.

41 Resource governance expert 1, *op. cit.*; Monk A, 'Santiago Principles Vs. Truman Scoreboard', Oxford Sovereign Wealth Fund Project, <https://oxfordswf.wordpress.com/2010/07/19/santiago-principles-vs-truman-scoreboard/>, accessed 11 October 2019.

42 Peterson Institute, 'A Blueprint for Sovereign Wealth Fund Best Practices', Policy Brief, Pb07-4B08-3, April 2008, <https://www.piie.com/sites/default/files/publications/pb/pb08-3.pdf>, accessed 11 October 2019.

## Operational management

Establishing governance and management structures that limit the ability of politicians to arbitrarily break or change rules is crucial in evading short-term political pressures to misuse funds. Governance of SWFs largely falls to the central bank, government entities such as the presidency or finance ministry, or a completely separate legal entity (and often some mix of the three).<sup>43</sup> The optimal governance structures for SWFs differ based on a country's institutional landscape. For example, if a country's central bank has functioned effectively and independently, and the country is only establishing a stabilisation fund, it may be sensible to place the fund in the bank to use this existing capacity.<sup>44</sup> However, if reserves have been managed ineffectively in past, or if the fund also seeks to augment fiscal policy, establishing separate structures becomes a more attractive option. Funds that designate governance decisions to government departments may be effective in a country with strong political checks and balances, but often face problems in developing countries.<sup>45</sup>

Establishing governance and management structures that limit the ability of politicians to arbitrarily break or change rules is crucial in evading short-term political pressures to misuse funds

It is also important to ensure separation between the fund's execution and its oversight. Accountability checks such as the board of directors should be appointed based on skills and merit, and should be apolitical, with terms lasting longer than election cycles where possible.<sup>46</sup> Importantly, resource revenue forecasting (especially when this factors into withdrawal and deposit rules) should be conducted independently, otherwise these projections can be inflated to increase allowances for political spending.<sup>47</sup>

In order to ensure transparency, internal and external audits, and transparent investment reports with reference to benchmarks should be required, and available publicly. Establishing functioning formal accountability mechanisms that are independent and have influence in society increases the pressures on politicians to address any fund discrepancies. Aside from internal and external auditors, these might include parliamentary budget oversight committees or independent accountability committees established

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43 Bauer A, Toledano P & M Rietveld, *op. cit.*

44 Resource governance expert, *op. cit.*; anti-corruption expert, *op. cit.*

45 NRG1 & CCS1, *Natural Resource Fund Governance: The Essentials*, 2014b, [https://resourcegovernance.org/sites/default/files/NRF\\_Overview\\_EN.pdf](https://resourcegovernance.org/sites/default/files/NRF_Overview_EN.pdf), accessed 11 October 2019.

46 *Ibid.*; anti-corruption expert, *op. cit.*; resource governance expert, *op. cit.*

47 Development economist 2, *op. cit.*

by government to monitor resource revenues. Additionally, informal accountability mechanisms may include civil society groups and media.<sup>48</sup>

## Investment management

At the most basic level, funds should have clearly stated objective(s) and an investment mandate that aligns with these objectives. Funds that have not clearly defined their objectives, or have crowded multiple objectives into a single fund, face the high risk of having a fund management strategy that is not targeted appropriately and/or managers with capacities misaligned to objectives. This decreases potential returns, as well as the ability to evaluate returns appropriately when the original objectives are not clear.<sup>49</sup> The pursuit of multiple fund objectives must therefore be weighed against the administrative costs of additional institutional structures and capacity to ensure fund effectiveness, while guarding against disproportionately high management fees.

Due diligence procedures should be established to limit excessive investment risk-taking and conflicts of interest/politicised projects. These processes should be especially stringent for funds with domestic investment mandates. Examples of these checks include explicit investment screening processes, investment limits in riskier asset classes, liability limits, and minimum credit grade requirements for investments.<sup>50</sup> Domestic investments should seek clear returns at least commensurate with international asset returns, or alternatively, allocation for and measurement of below-return social investments should be stipulated as clearly as possible in investment mandates and revenue projections.<sup>51</sup> The ability to attract additional capital on an equal co-funding basis can serve as an informal gauge of the quality of investment projects.<sup>52</sup>

## Taking stock of African SWFs

According to the Sovereign Wealth Center, there are 83 SWFs and pension funds globally with assets greater than \$1 million.<sup>53</sup> A total of 12 SWFs are on the African continent, with most financed by oil revenues (see Table 2).<sup>54</sup> Half of the continent's SWFs were established within the last decade. The objectives and structure of funds on the continent vary widely. Some countries have established one fund with one objective, some countries have established one SWF tasked with multiple objectives, and others have established separate

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48 NRCI & CCSI, 2014b, *op. cit.*, resource governance expert, *op. cit.*

49 IFI representative 1, *op. cit.*

50 Bauer A, 'Funds and Mechanisms for the Management of Oil and Gas Revenues to Support Sustainable Development: Insights from Country Experiences and Lessons for Senegal', PAGE (Partnership for Action on Green Economy), 2018, [https://www.un-page.org/files/public/page\\_fiscal\\_study\\_senegal\\_-\\_en.pdf](https://www.un-page.org/files/public/page_fiscal_study_senegal_-_en.pdf), accessed 25 October 2019.

51 Gelb A *et al.*, 2014, *op. cit.*

52 *Ibid.*; IFI representative 1, *op. cit.*

53 Sovereign Wealth Center, 'Fund profiles', <https://www.sovereignwealthcenter.com/fund-profiles.html>, accessed 2 October 2019.

54 Table 2 excludes African pension funds. It also lists Nigeria and Ghana's two SWFs separately in order to provide more detail, while most global lists only include the NSIA in Nigeria and list Ghana's two funds as the combined Petroleum Funds.



funds or sub-funds to achieve different objectives. In practice, however, many SWFs have been used to finance recurrent expenditures, in contravention of their objectives. In recent years many more extra-budgetary funds have also been created and considered as SWFs. Most African SWFs are opaque in terms of public information provision, as is often the case globally. This complicates the ability to make assessments on such funds. However, some funds, notably the four case study countries, have made a point to emphasise transparency, at least on paper.

Country	Name	Year of establishment	Assets under management (AUM)	Principal non-renewable resource
Libya	Libyan Investment Authority*	2006	\$67 billion	Oil
Botswana	Pula Fund	1994	\$4.33 billion	Diamonds
Angola	Fundo Soberano de Angola (FSDEA)*	2012	\$2 billion	Oil
Nigeria	Nigeria Sovereign Investment Authority (NSIA)	2011	\$1.69 billion	Oil
Gabon	Sovereign Fund of the Gabonese Republic	1998	\$1 billion	Oil
Ghana	Ghana Heritage Fund	2011	\$485.17 million	Oil
Ghana	Ghana Stabilisation Fund	2011	\$381.2 million	Oil
Nigeria	Excess Crude Account	2004	\$323.7 million	Oil
Mauritania	National Fund for Hydrocarbon Reserves*	2006	\$150 million	Oil
Uganda	Petroleum Revenue Investment Reserve	2015	\$125.87 million	Oil
Equatorial Guinea	Equatorial Guinea Fund for Future Generations*	2002	\$80 million	Oil
São Tomé and Príncipe	National Oil Account	2004	Unknown	Oil

a Given the ambiguities around SWF definitions, for the purposes of this paper only funds that are explicitly or implicitly linked to resource revenues are included in the above list. National investment funds such as Rwanda's Agaciro Development Fund and Senegal's FONSIS are not included.

Source: AUM derived from annual reports or official government reports. For countries marked with (\*), figures were retrieved from the Sovereign Wealth Fund Center, 'Fund profiles', <https://www.sovereignwealthcenter.com/fund-profiles.html>, accessed 2 October 2019

The remainder of this section will examine SWFs operating in the four African case study countries – Angola, Botswana, Ghana and Nigeria<sup>55</sup> – in greater depth. Each case study will begin with a snapshot table that details the fund objectives, activity, and macro-economic

55 The four countries were chosen based on the availability of information.

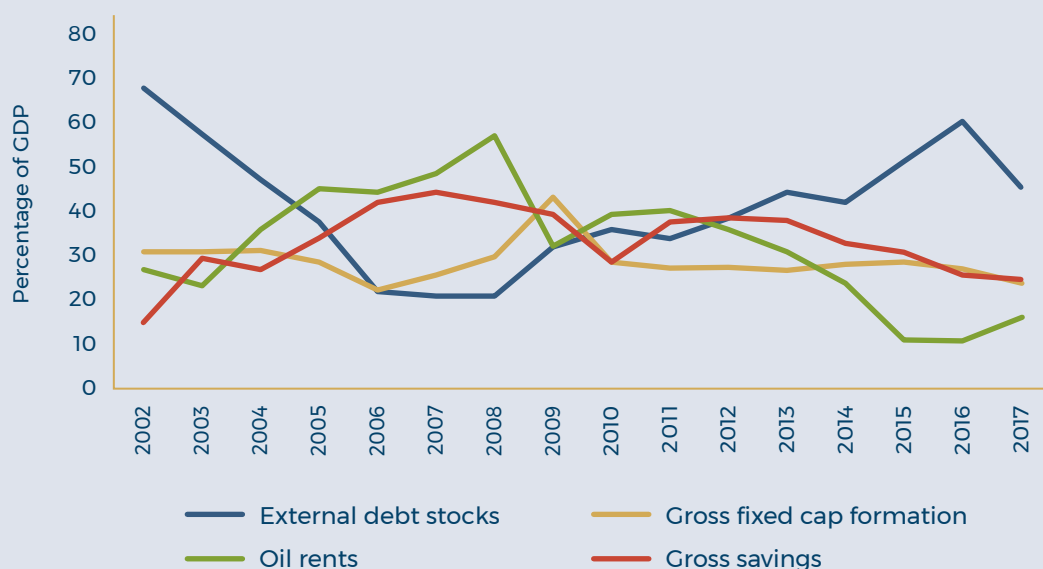
context of the country. A figure also depicts key indicators from 10 years before SWF establishment until the present (where data is available).<sup>56</sup> The figures show external debt, gross savings, gross fixed capital formation and resource rents (as a percentage of GDP), in order to visualise the productiveness of resource revenue investments in countries with SWFs. The case studies will then examine the SWFs' structure, mandate and objectives, as well as their performance against these objectives, with reference to the overarching question of whether the SWFs are achieving improved macro-economic/public financial management and economic growth. This will help to ascertain whether the structure and performance of African SWFs supports existing theory and evidence, and draw conclusions unique to African SWFs.

## Angola

TABLE 3 ANGOLA SNAPSHOT	
Name of fund	Fundo Soberano de Angola (FSDEA)
Year established	2012
Type of fund	Single fund; savings, development and partial stabilisation objectives
Seed capital	\$5 billion
AUM growth (% , 2016)	5.05% (only from returns)
Current AUM	Exact AUM unknown after 2019 withdrawal; approximately \$2 billion
AUM as % of GDP	1.6%
Investment strategy	Mix of capital preservation (short-term, safe assets), and private equity/domestic developmental objectives in sub-Saharan Africa
Additional deposits	None
Drawdowns	\$2 billion withdrawal in 2019
<b>Angola economic indicators</b>	
GDP growth (% , 2018)	-2.31
External debt stocks (% of GNI, 2018)	54
Gross fixed capital formation (% of GDP, 2017)	23.24
Current account (% of GDP, 2018)	7.0
Interest payment (% of revenue, % of expense, 2017)	16.54, 16.23
Interest spread (% , 2018)	13.8
Inflation (% , 2018)	20.19
Oil rents (% of GDP)	15.75
Human Development Index	0.581

<sup>56</sup> In Nigeria's figure, the 10-year pre-SWF period refers to the NSIA rather than the ECA. In Botswana's figure, the time period does not reflect 10 years before and after SWF establishment due to limited data availability.

Figure 1 Select macro-economic indicators for Angola



Source: World Bank, 'World Development Indicators', <https://datacatalog.worldbank.org/dataset/world-development-indicators>, accessed 2 October 2019

The Fundo Soberano de Angola (FSDEA) was established in 2011 by presidential decree<sup>57</sup> and initially capitalised with \$5 billion. Although it is a single fund, the investment objectives allude to the fact that the fund has savings, development and stabilisation purposes. The fund's investment objectives, as defined in Presidential Decree No. 107/13,<sup>58</sup> include supporting the development of infrastructure and industry, supporting efficient fiscal policy, increasing the country's wealth (for current and future generations), and preventing negative economic shocks. These objectives are distilled to three governing principles: 'protection of capital, maximization of long-term returns, development of infrastructure for the benefit of Angolan citizens'.<sup>59</sup>

It is managed independently of the Banco Nacional de Angola (BNA) and the Treasury, but with governance oversight from the presidency. Angola also has separate stabilisation funds outside of the FSDEA, managed by the BNA on behalf of the Treasury. These are the Strategic Financial Oil Reserve Account for Infrastructure (Reserva Estratégica Financeira Petrolífera para Infraestruturas, or RFEP) and the Oil Price Differential Account (Fundo do Diferencial do Preço do Petróleo, or OPDP).<sup>60</sup>

57 Government of Angola, Presidential Decree No. 48/11, 9 March 2011.

58 Government of Angola, Presidential Decree No. 107/13, 28 June 2013.

59 *Ibid.*

60 UN Committee for Development Policy, *Graduating and Graduated Countries: Lessons Learned in Developing Productive Capacity*, 2016, <https://www.un.org/development/desa/dpad/wp-content/uploads/sites/45/2016-EGM-Geneva-Lessons-bgPaper.pdf>, accessed 1 October 2019.

Fiscal rules for Angola's three funds are relatively vague. The RFEP receives deposits based on selling 100 000 barrels of oil per day, and the OPDP receives the balance of oil revenue above expected projections based on an oil reference price.<sup>61</sup> The FSDEA should receive surpluses from the stabilisation funds when they are not needed to stabilise the budget; however, it has not received additional funds since inception. The funds do not have specific withdrawal guidelines, and withdrawals are made at the discretion of the finance minister.<sup>62</sup> Overall, Angola's fiscal management has been volatile, stemming from the constant reshuffle and restructure of government departments, high public debt, lack of adherence to fiscal rules, weak oversight of budget from the National Assembly and the Audit Court, and little transparency in PFM.<sup>63</sup>

The FSDEA has a much greater investment focus on regional development in sub-Saharan Africa than other funds, particularly in high-risk, high-potential private equity in emerging markets. It has seven private equity sub-funds: agriculture, infrastructure, real estate, hotels, timber, healthcare and mining. A total of 7.5% of the investment allocation is in social development, including healthcare, education, electricity and water. It aims for one-third of its funds to go towards restructuring distressed assets – a much riskier investment for an SWF.<sup>64</sup> Another third of its investments are geared towards capital preservation, through safe instruments and hedging, and 20% of its assets must be liquid. Given the country's dependence on oil, 95% of assets must be uncoordinated with the oil price.<sup>65</sup>

The investment strategy sets out the following maximum asset allocations:

- investments in liquid assets and debt (100%)
- private equity (10%)
- agriculture and mining (10%)
- real estate (10%)
- investment in infrastructure (30%)
- investments in distressed asset opportunities (5%)
- BRICS and border markets (2.5%)
- commodities (5%)
- social development projects and socially responsible investments (7.5%)

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61 *Ibid.*

62 Government of Angola, Presidential Decree No. 48/11, 9 March 2011.

63 Jensen S & F Paulo, 'Reforms of the Angolan Budget Process and Public Financial Management: Was the Crisis a Wakeup Call?', Chr. Michelsen Institute Report, 7, 2011, <https://www.cmi.no/publications/file/4259-reforms-of-the-angolan-budget-process-and-publ>, accessed 12 October 2019; IMF, *Angola: Selected Issues*, Country Report, 18/157, June 2018, <https://www.tralac.org/images/docs/13155/angola-selected-issues-paper-imf-country-report-no-18-157-june-2018.pdf>, accessed 12 October 2019.

64 Wright C, 'Inside Angola's Sovereign Wealth Fund', *Forbes*, 5 October 2014, <https://www.forbes.com/sites/chriswright/2014/09/05/inside-angolas-sovereign-wealth-fund/#5a1c28978b98>, accessed 12 October 2019; FSDEA (Fundo Soberano de Angola), *Annual Report 2013*, <https://s3.amazonaws.com/rqi-documents/46d163b72eb5e965c09b8ebc85e33b213e87bb4b.pdf>, accessed 9 September 2019.

65 FSDEA, 2013, *op. cit.*



According to the FSDEA website, the current net investment portfolio is comprised of 43% fixed income assets, 45% variable income assets, 8% hedge funds and 3% global funds.<sup>66</sup> FSDEA first recorded a net profit from its investments in 2016, and 48% of these investments were channelled into sub-Saharan Africa.<sup>67</sup>

In terms of specific investments, the FSDEA has supported the international programme 'One Laptop per Child' in Angola, through the provision of laptops and capacity building for teachers. Another programme supports small farmers in developing micro-businesses and accessing markets.<sup>68</sup> An amount of \$18.2 million has been devoted to seven agricultural programmes across the country to target food security, while \$32.5 million has been devoted to the development of fibre plantations, including a training/skills development component. In terms of infrastructure, \$180 million was invested in a strategic deep-sea port (Porto de Caiao).<sup>69</sup> The fund also supported two national training programmes, one in banking and finance and the other in hotel management.<sup>70</sup> These investments have been supported by a \$1.1 billion infrastructure sub-fund and \$500 million hotel fund.<sup>71</sup> The biggest financial gains for the seven private equity funds have been in agriculture and infrastructure.<sup>72</sup>

After its establishment, the FSDEA made it a point to advertise its commitment to good governance. This was in part to address past criticisms that the stabilisation funds were established without proper legal backing. The FSDEA signed up to the Santiago Principles and hired an established international consulting firm to conduct its external audits. It also migrated its accounting system to adopt the International Financial Reporting Standards, unique among the four profiled SWFs.<sup>73</sup>

However, the FSDEA's investment mandate is vague without a clear separation of objectives. As an example, its mandate includes stabilisation even though stabilisation is not an official investment objective and Angola already has separate stabilisation funds. The FSDEA Board of Directors is appointed by the president and the investment advisory board consists of government officials, and thus structural independence is limited. The FSDEA also does not have a code of conduct preventing conflict of interest. These factors all create a scenario ripe for loopholes and political manipulation.

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66 FSDEA, 'Investment strategy', <https://fundosoberano.ao/en/investments>, accessed 25 October 2019.

67 *How We Made It in Africa*, 'Fundo Soberano de Angola announces investment updates for Q2 2017', 12 October 2017, <https://www.howwemadeitinafrica.com/fundo-soberano-de-angola-announces-investment-updates-q2-2017/60007/>, accessed 7 October 2019.

68 FSDEA, 2013, *op. cit.*

69 *BizCommunity*, 'FSDEA commits to \$180 million investment in port infrastructure', 6 January 2017, <https://www.bizcommunity.com/Article/196/586/156676.html>, accessed 7 October 2019.

70 *Business Chief*, 'FSDEA leads development in Angola through 'Future Leaders' Initiative', 19 August 2014, <https://africa.businesschief.com/leadership/1630/FSDEA-Leads-Development-in-Angola-through-Future-Leaders-Initiative>, accessed 7 October 2019.

71 Jablonski A, 'Will Angola's sovereign wealth fund allow it to adapt to falling oil prices?', *Global Risk Insights*, 4 January 2015, <https://globalriskinsights.com/2015/01/will-angolas-sovereign-wealth-fund-allow-adapt-falling-oil-prices/>, accessed 7 October 2019.

72 *How We Made It in Africa*, 12 October 2017, *op. cit.*

73 *How We Made It in Africa*, 'Fundo Soberano de Angola retains high ranking on the Sovereign Wealth Fund Institute Transparency Index', 25 July 2017, <https://www.howwemadeitinafrica.com/fundo-soberano-de-angola-fsdea-retains-high-ranking-sovereign-wealth-fund-institute-swfi-transparency-index/59280/>, accessed 6 October 2019

It is thus unsurprising that the FSDEA's activities since inception have not been independent. Most notably, the chairperson of the fund (former president Eduardo dos Santos's son) appointed an asset management company owned by a friend to be the sole fund manager, without competitive tender. While the chairperson initially said this appointment was purely based on available domestic competencies and that they intended to hire additional managers, this never occurred.<sup>74</sup> The 2017 Paradise Papers revealed that the fund has invested hundreds of millions of dollars in projects where this asset manager has personal interests, including many of the projects listed above.<sup>75</sup> Although the Paradise Papers did not uncover anything technically illegal, considering the lenient FSDEA rules, it shows how SWFs (and especially development funds) can be set up to legally allow crony capitalism without oversight, rather than to encourage prudent, rules-based investments. Aside from the FSDEA, the two stabilisation funds have also been criticised for opaque use of funds and ultimately their inability to stabilise, given that they hold miniscule revenues compared to the share of oil revenue in the budget (the REFP held 4% of the national budget and the OPDA 1% of the national budget in 2014).<sup>76</sup>

Angola's new president as of 2017, Joan Lourenco, has voiced his intention to root out all institutionalised patronage, and has fired the FSDEA's chairperson. This has led to a protracted legal battle between the SWF and its asset manager that reached the supreme court, as well as a \$3 million FSDEA asset freeze. The asset manager eventually won the case and the freeze was lifted; however, the recovery of these assets reportedly cost the state \$10 million in attorney fees, in direct contrast to the financial prudence that SWFs should stand for.<sup>77</sup> This political battle has decreased the credibility and inhibited the day-to-day functioning of the fund and its investments.<sup>78</sup>

In 2019 Lourenco withdrew \$2 billion from the FSDEA to finance the budget's Integrated Municipal Intervention Plan, focused on developing energy, water, education, health, basic sanitation and road infrastructure.<sup>79</sup> Social infrastructure is needed in Angola and it is important to finance these investments through the existing budget where possible, rather than borrowing. However, the future sustainability of the fund becomes questionable when

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74 Pegg D, 'Head of Angola's wealth fund fired after Paradise Papers revelations', *The Guardian*, 11 January 2018, <https://www.theguardian.com/news/2018/jan/11/head-angola-wealth-fund-fired-paradise-papers-revelations>, accessed 5 October 2019.

75 Pegg D, 'Angola sovereign wealth fund's manager used its cash for his own projects', *The Guardian*, 7 November 2017, <https://www.theguardian.com/news/2018/jan/11/head-angola-wealth-fund-fired-paradise-papers-revelations>, accessed 5 October 2019.

76 Jensen S, 'Angola's Infrastructure Ambitions through Booms and Busts: Policy, Governance and Reform', Chatham House, September 2018, <https://www.chathamhouse.org/sites/default/files/publications/research/2018-09-14-angola-infrastructure-ambitions-kirk-jensen.pdf>, accessed 10 October 2019; UN Committee for Development Policy, 2016, *op. cit.*

77 *Platforma*, 'Angola spends 10 million USD on lawyers to recover assets', 26 March 2019, <https://www.platformamedia.com/en-uk/news/society/interior/angola-spends-10-million-usd-on-lawyers-to-recover-assets-10727390.html>, accessed 15 October 2019; Milhench C, 'UK judge lifts asset freeze order against Quantum Global in Angolan SWF case', *Reuters*, 31 July 2018, <https://www.reuters.com/article/us-global-swf-assets/global-sovereign-fund-assets-jump-to-7-45-trillion-preqin-idUSKBNHJ2DG>, accessed 20 October 2019; *Sharenet*, 'Asset manager Quantum says Swiss prosecutors close Angola-related case', 2019, <https://www.sharenet.co.za/views/views-article.php?views-article=45184>, accessed 20 October 2019.

78 *Angola FOREX*, 'Gesterra takes over management of projects withdrawn from FSDEA', 16 March 2019, <https://angolaforex.com/en/2019/03/16/gesterra-assumes-management-of-projects-withdrawn-from-fsdea/>, accessed 20 October 2019.

79 *EIN Newsdesk*, 'PIIM to get USD 2 billion funding', 27 June 2019, [https://www.einnews.com/pr\\_news/489196504/piim-to-get-usd-2-billion-funding](https://www.einnews.com/pr_news/489196504/piim-to-get-usd-2-billion-funding), accessed 20 October 2019.

half of its balance can be withdrawn arbitrarily. More importantly, this is an example of how a heavily politicised fund can easily be delegitimised after regime changes, and raises questions over whether the fund should have been established in the first place.<sup>80</sup>

Angola’s case demonstrates that when a fund is instituted by a politicised entity, the fund objectives, rules and accountability mechanisms will likely be crafted loosely to allow existing patronage networks to be maintained, even if some protocols are put in place in a bid for international credibility

Figure 1 shows that the FSDEA has not achieved its intended purposes since establishment, considering public debt has spiked and savings have decreased as oil revenues declined. Overall, Angola’s case demonstrates that when a fund is instituted by a politicised entity, the fund objectives, rules and accountability mechanisms will likely be crafted loosely to allow existing patronage networks to be maintained, even if some protocols are put in place in a bid for international credibility.

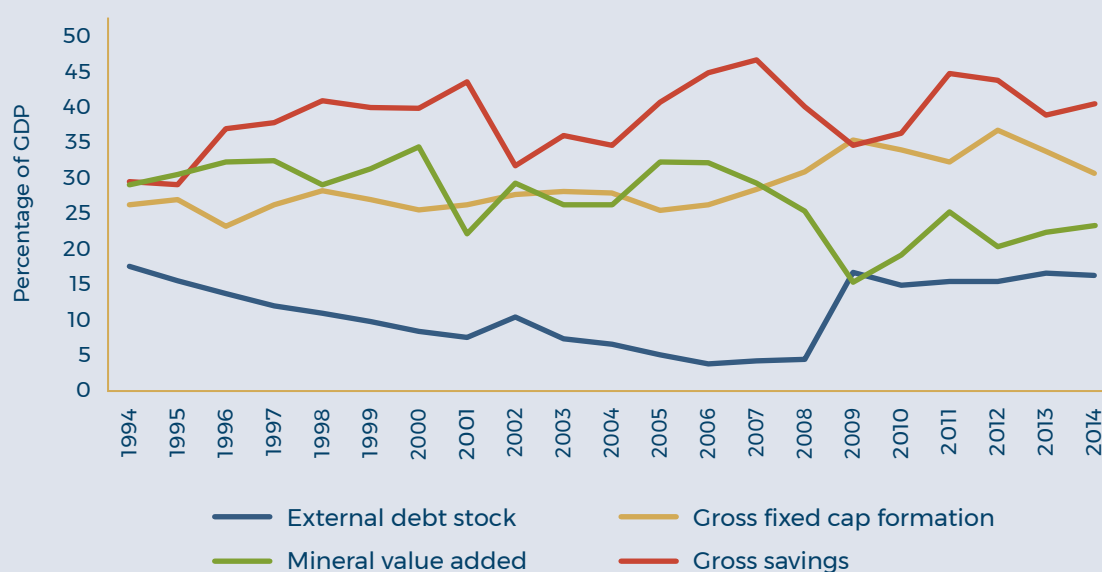
## Botswana

TABLE 4 BOTSWANA SNAPSHOT	
Name of fund	Pula Fund
Year established	1994
Type of fund	Single fund; savings fund (although in practice has also served stabilisation purposes)
Seed capital	Unknown (approximately \$5.2 billion in 1999)
AUM growth (% , 2016)	-.14% (from withdrawals as well as returns)
Current AUM	\$5.5 billion
AUM as % of GDP	31.5%
Investment strategy	Foreign fixed income and equity investments only (conservative investment strategy)
Additional deposits	Unknown
Drawdowns	Drawdowns on the fund in 2002, 2003, 2005, 2008, 2012, 2015 and 2018 of various amounts not exceeding \$200,000
<b>BOTSWANA ECONOMIC INDICATORS</b>	
GDP growth (% , 2017)	4.45

80 Sovereign Wealth Fund Institute, ‘Angolan SWF shrinks after \$2 billion withdrawal for infrastructure’, 1 July 2019, <https://www.swfinstitute.org/news/73701/angolan-swf-shrinks-after-2-billion-withdrawal-for-infrastructure>, accessed 20 October 2019.

External debt stocks (% of GNI, 2018)	9.72
Current account (% of GDP, 2018)	1.85
Interest payment (% of revenue, % of expense, 2017)	1.75, 2.1
Interest spread (% , 2018)	4.98
Inflation (% , 2018)	3.24
Gross fixed capital formation (% of GDP, 2018)	30.18
Oil rents (% of GDP)	N/A
Human Development Index	0.717

Figure 2 Select macro-economic indicators for Botswana



Source: World Bank, World Development Indicators, <https://datacatalog.worldbank.org/dataset/world-development-indicators>, accessed 25 October 2019; WAVES (Wealth Accounting and the Valuation of Ecosystem Services), *Economic Accounting of Mineral Resources in Botswana: Technical Report*, <https://www.wavespartnership.org/sites/waves/files/kc/Technical%20Rept%20WAVES%20Botswana%20Minerals%20pub%205-28-16%281%29.pdf>, accessed 20 October 2019

The Bank of Botswana Act (1975)<sup>81</sup> made provision for the establishment of a long-term government investment entity comprised of excess international reserves. The Pula Fund was subsequently established in 1993. The Pula Fund is not legally linked to diamond revenues or to savings for future generations, although official documents often reference it as a savings fund. Unlike the other three selected countries, Botswana’s SWF is not a separate legal entity but is housed and managed within the Bank of Botswana (BoB), the central bank. Botswana previously also maintained a Stabilization Fund, established in 1970

81 Government of Botswana, Bank of Botswana Act, 1975. Gaborone: Government Printer, 1975.



to smooth government revenues. However, according to the 2012 BoB Annual Report,<sup>82</sup> given Botswana's consistent national budget surplus the fund was permanently drawn down for lending to local authorities and corporates. The report does imply that the Pula Fund can serve a dual stabilisation purpose, stating that, 'on occasion, there is a drawdown of foreign exchange reserves for stabilisation purposes and to afford counter-cyclical policy response'.<sup>83</sup>

The Pula Fund is opaque in terms of its rules. For deposits, the fund receives foreign exchange reserves in excess of six months' import cover, which must be held by Botswana's primary reserve, the liquidity portfolio.<sup>84</sup> However, the import cover is subject to adjustment. There are no withdrawal restrictions explicit to the Pula Fund.

In order to manage the overall budget, the Ministry of Finance and Development Planning (MFDP) has followed a Sustainable Budget Index since 1994, which sets a maximum ratio of recurrent (non-investment) spending from non-resource revenues, which can be adjusted but should be no greater than 1:1. An expenditure rule developed in 2006 also sets maximum government expenditure at 40% of GDP.<sup>85</sup> The remaining non-resource fiscal revenues, as well as all resource revenues, must be allocated between public investments, limited recurrent expenditure, including health and education, and the Pula Fund. Fiscal investments have closely followed national development plans (NDPs), which are integrated into the national budget. NDPs have also required parliamentary approval for any changes to be made, and take into account capacity constraints by limiting projects where costs cannot cover expenditures.<sup>86</sup> Additionally, a 2005 fiscal rule limits maximum external debt to 20% of GDP.

The Pula Fund's investments are separated into a government investment account managed by the MFDP and a reserve account managed by the BoB. Fund management is split between the BoB's financial markets department and foreign fund managers. There are no formal, publicly available investment restrictions. Despite the lack of rules, the fund's investment strategy has been conservative, traditionally investing only in long-term foreign fixed income (60%) and equities (40%), and in highly rated sovereign debt.<sup>87</sup> It has used the IMF Special Drawing Rights for fixed income currency investments. This distinguishes it from the Nigerian and Angolan funds, which invest domestically. In 2019

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82 Bank of Botswana, *Annual Report 2012*, <http://www.bankofbotswana.bw/index.php/content/2009110614010-annual-report>, accessed 5 September 2019.

83 *Ibid.*

84 *Ibid.*

85 NREGI & CCSI, Botswana: Pula Fund, 2013, [https://resourcegovernance.org/sites/default/files/NRF\\_Botswana\\_July2013.pdf](https://resourcegovernance.org/sites/default/files/NRF_Botswana_July2013.pdf), accessed 5 September 2019; Republic of Botswana & World Bank, *Public Finance and Mineral Revenues in Botswana: Technical Report*, April 2016, [https://www.wavespartnership.org/sites/waves/files/kc/Mineral%20revenues%20and%20public%20finance\\_final\\_compressed.pdf](https://www.wavespartnership.org/sites/waves/files/kc/Mineral%20revenues%20and%20public%20finance_final_compressed.pdf), accessed 5 September 2019.

86 Lewin M, 'Botswana's success: Good governance, good policies, and good luck', in Chuhan-Pole P & M Angwafo (eds), *Yes, Africa Can: Success Stories from a Dynamic Continent*, World Bank, 2011, <http://siteresources.worldbank.org/AFRICAEXT/Resources/258643-1271798012256/Botswana-success.pdf>, accessed 7 September 2019.

87 Alswilem KA et al., 'A Comparative Study of Sovereign Investor Models: Sovereign Fund Profiles', Harvard Kennedy School, Belfer Center for Science and International Affairs & Center for International Development, Harvard University, 2015, <https://www.ifswf.org/publications/comparative-study-sovereign-investor-models-sovereign-fund-profiles>, accessed 2 September 2019.

the fund revised its investment approach to be slightly less conservative and more growth-orientated, expanding eligible currencies from four to 17, expanding the equities focus to emerging markets, and loosening its sovereign debt rating requirements from AA to BBB. It has also shifted its balance to 50% fixed income, 45% equities, and 5% high-yielding opportunities.<sup>88</sup> The fund is subject to regular internal and external audits, but management and oversight of day-to-day activities is not as transparent.<sup>89</sup> Information on specific investments, their performance and asset managers is not publicly available.<sup>90</sup>

In practice, the Pula Fund has essentially functioned as a stabilisation fund, cushioning against external shocks, more so than as a savings fund.<sup>91</sup> This is confirmed by Figure 2, which shows that overall AUM from 1999–2018 has not grown significantly since the Pula Fund's establishment, and has therefore not fulfilled a true savings purpose. Notably, the Pula Fund was drawn down to stabilise fiscal expenditures during the global financial crisis after diamond revenues dropped sharply. It has also been drawn down on occasion for domestic expenses such as funding budget deficits (in order to avoid raising taxes) and establishing and funding the national public pension fund.<sup>92</sup> Drawdowns on the fund have been made in 2002, 2003, 2005, 2008, 2012, 2015 and 2018 for such purposes.<sup>93</sup> These drawdowns have essentially replaced the need to borrow internationally, but are not in line with the purposes of an SWF, or correlated with diamond prices. Accordingly the IMF has advised that the withdrawal rules be clarified.<sup>94</sup>

In spite of this, in the 25 years since its establishment, the Pula Fund has not run into any major scandals and on aggregate has invested responsibly and conservatively. The management of the fund has positively impacted the cost of borrowing; Botswana is currently rated A2 by Moody's, the highest rating for an African country, and Moody's cites the Pula Fund as one of the key reasons for Botswana's fiscal prudence.<sup>95</sup> The logic and adherence to the Sustainable Budget Index despite its non-binding nature, as well as the conservative management of the Pula Fund despite loose regulations, stems from a culture of fiscal conservatism and a belief that recurrent expenditure should not rely on resource revenues.<sup>96</sup> This is demonstrated in Figure 2 by Botswana's consistently high savings and capital investment rates, coupled with low public debt.

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88 Mguni M, 'Botswana to invest diamond wealth more widely', *Bloomberg*, 21 May 2019, <https://www.bloomberg.com/news/articles/2019-05-21/conservative-botswana-wealth-fund-broadens-its-horizons-a-little>, accessed 5 September 2019.

89 NRCI & CCSI, 2013, *op. cit.*

90 Jefferis K, 'Public Finance and Mineral Revenues in Botswana', World Bank, April 2016, [https://www.wavespartnership.org/sites/waves/files/kc/Mineral%20revenues%20and%20public%20finance\\_final.compressed.pdf](https://www.wavespartnership.org/sites/waves/files/kc/Mineral%20revenues%20and%20public%20finance_final.compressed.pdf), accessed 10 September 2019.

91 Kojo NC, 'Small Countries with Volatile Revenue: Botswana and Bhutan', World Bank, Economic Policy and Debt Department, 2015, <http://documents.worldbank.org/curated/en/413221467997599192/pdf/98089-WP-Small-states-with-volatile-revenue-flows-Box391504B-PUBLIC.pdf>, accessed 5 September 2019.

92 Alswellem KA *et al.*, *op. cit.*

93 Konopo J *et al.*, 'Botswana repeatedly raids preservation fund', *Mail & Guardian*, 5 February 2016, <https://mg.co.za/article/2016-02-04-botswana-repeatedly-raids-preservation-fund>, accessed 5 September 2019.

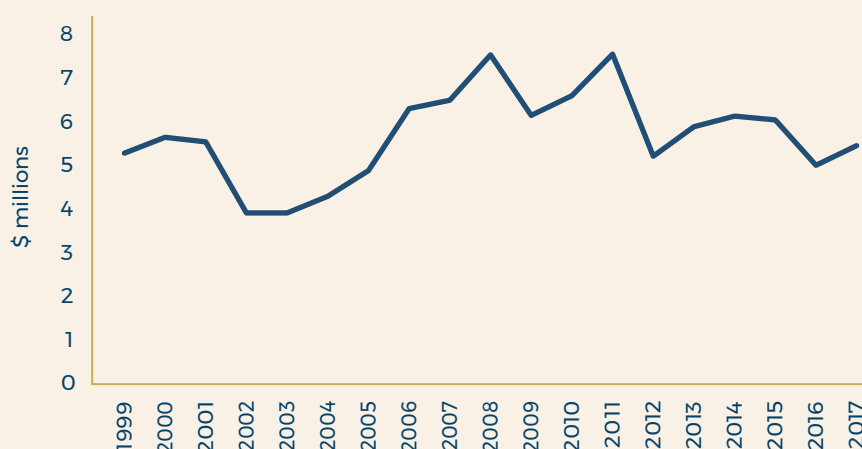
94 Central Banking, 'IMF issues advice on Botswana's sovereign fund', 9 August 2017, <https://www.centralbanking.com/central-banks/reserves/foreign-exchange/3280986/imf-issues-advice-on-botswanas-sovereign-fund>, accessed 10 September 2019.

95 Moody's Investors Service, 'Moody's affirms Botswana's A2 rating: Outlook stable', 27 April 2018, [https://www.moody.com/research/Moodys-affirms-Botswanas-A2-rating-Outlook-stable--PR\\_382811](https://www.moody.com/research/Moodys-affirms-Botswanas-A2-rating-Outlook-stable--PR_382811), accessed 10 September 2019.

96 Alswellem KA *et al.*, *op. cit.*

In the 25 years since its establishment, the Pula Fund has not run into any major scandals and on aggregate has invested responsibly and conservatively. Botswana is currently rated A2 by Moody's, the highest rating for an African country, and Moody's cites the Pula Fund as one of the key reasons for Botswana's fiscal prudence

Figure 3 Pula Fund AUM



Source: Bank of Botswana, 'Annual Report 2018', <http://www.bankofbotswana.bw/assets/uploaded/BoB%202018%20Annual%20Report%20Main%20document.pdf>, accessed 30 October 2019

Much research has probed the reasoning for Botswana's stable institutions. Some of the explanations proffered include: the country's homogenous population, single-party democracy with little contestation, favourable pre-colonial (Tswana) and colonial institutional arrangements, the alignment of a political and economic elite that promotes property rights, and strong agreements with diamond extraction companies. The president also managed expectations when the Pula Fund was established by stating that the fund would serve as a tool for future development, and that revenues should be managed by the government (rather than having regional or ethnic-based allocations).<sup>97</sup> A deeper look at the roots of Botswana's conservative fiscal culture is beyond the scope of this paper; however, it positions the country as somewhat of an anomaly in the region. An important takeaway is that Botswana's overarching constrained fiscal policy regime has facilitated the integration of a successful SWF, rather than the reverse.

97 IFI representative 1, *op. cit.*; IFI representative 2, *op. cit.*; Acemoglu D, Johnson S & JA Robinson, 'An African Success Story: Botswana', MIT (Massachusetts Institute of Technology), Department of Economics Working Paper, 01-37, July 2001, <https://dspace.mit.edu/bitstream/handle/1721.1/63256/africansuccessst00acem.pdf>, accessed 7 September 2019.

## Ghana

TABLE 5 GHANA SNAPSHOT	
Name of fund	Ghana Petroleum Funds
Year established	2011
Type of fund	Two funds; Ghana Stabilisation Fund and Ghana Heritage Fund (the latter is a savings fund)
Seed capital (first year of oil revenue)	Approximately \$69 million
AUM growth (% , 2017)	18.4% (from deposits/withdrawals as well as returns)
Current AUM	\$0.5 billion
AUM as % of GDP	1%
Investment strategy	Stabilisation Fund aims to achieve capital preservation, Heritage Fund invests conservatively in long-term, safe international assets
Additional deposits	Contributions every year since inception, approximately \$1.537 billion in aggregate
Drawdowns	Drawdowns in 2014, 2015 and 2018, totalling \$375.81 million from the Stabilisation Fund
<b>GHANA ECONOMIC INDICATORS</b>	
GDP growth (% , 2018)	6.26
External debt stocks (% of GNI, 2018)	36.27
Current account (% of GDP, 2017)	-,3.39
Interest payment (% of revenue, % of expense, 2017)	-
Interest spread (% , 2018)	-
Inflation (% , 2018)	9.84
Gross fixed capital formation (% of GDP, 2018)	20.58
Oil rents (% of GDP)	2.96
Human Development Index	0.592

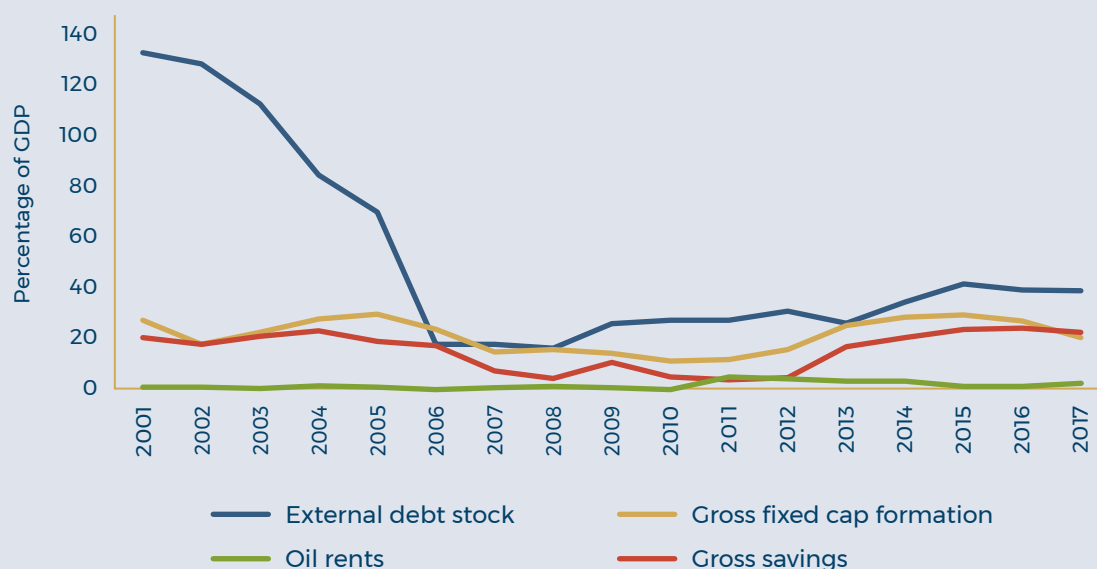
In Ghana, the Petroleum Revenues Management Act 815 (PRMA Act) was enacted in 2011 in order to ‘regulate the collection, allocation and management by government of petroleum revenue derived from upstream and midstream petroleum operation’.<sup>98</sup> Ghana is unique in that legislation governing oil revenues was enacted pre-emptively after the discovery of oil in 2007, before extraction began. The act established the Petroleum Holdings Funds, which houses a savings and stabilisation fund – the Ghana Heritage Fund and the Ghana Stabilisation Fund, respectively – as well as a Consolidated Fund, which supports the annual budget. The Petroleum Holding Funds are under the oversight of the Ministry of Finance, with disbursements managed by the Bank of Ghana, the central bank.<sup>99</sup> In 2014 the Ghana

98 Government of Ghana, Petroleum Revenue Management Act 815, 2011, <http://www.eisourcebook.org/cms/February%202016/Ghana%20Petroleum%20Revenue%20Management%20Act%202011.PDF>, accessed 26 August 2019.

99 *Ibid.*

Infrastructure Investment Fund (GIIF) Act (as well as a 2015 amendment to the PRMA) established a separate and independent domestic investment fund, also accountable to the Minister of Finance.<sup>100</sup>

**Figure 4** Select macro-economic indicators for Ghana



Source: World Bank, 'World Development Indicators', <https://datacatalog.worldbank.org/dataset/world-development-indicators>, accessed 25 October 2019

Unlike Angola and Botswana, deposit and withdrawal rules for Ghana's SWFs are very specific. Public oil revenues are first allocated to the Petroleum Holding Funds. A maximum of 70% of funds based on the calculated benchmark revenue are allocated to the Consolidated Fund for budget purposes; this is the Annual Budget Funding Amount (ABFA).<sup>101</sup> Of this allocation, not less than 70% is meant for public investment and 30% for recurrent expenditure, including an amount not exceeding 25% that should go to the GIIF. Part of this 70% can also be used as collateral for debt or to fund liabilities for 10 years after the establishment of the fund. The remaining percentage of the benchmark revenue amount is then allocated to the Ghana Petroleum Funds, and of this allocation not more than 70% goes to the Stabilisation Fund and not less than 30% to the Heritage Fund.<sup>102</sup> In terms of withdrawal rules, the Heritage Fund cannot be drawn from, although a resolution by Parliament can change this provision 15 years after the fund's establishment.<sup>103</sup> The Stabilisation Fund's mandate (as of the 2015 amendment) allows for withdrawals of

100 Government of Ghana, Petroleum Revenue Management (Amendment) Act 893, 2015, <https://www.mofep.gov.gh/sites/default/files/reports/petroleum/PRMA-Amendment-2015.pdf>, accessed 26 August 2019.

101 Government of Ghana, 2011, *op. cit.*

102 *Ibid.*

103 *Ibid.*

excesses above a cap for debt repayment and contingency, and to support shortfalls in the budget.<sup>104</sup>

In 2018 petroleum receipts came to \$723.55 million, of which \$305,273,896 was transferred to the Ghana National Petroleum Company, \$235,103,316 to the ABFA, \$305,723,402 to the Ghana Stabilisation Fund and \$131,024,315 to the Ghana Heritage Fund.<sup>105</sup> According to the 2018 annual report,<sup>106</sup> \$375.81 million has been withdrawn from the Stabilisation Fund since its inception. In 2014, \$305,684,689 was withdrawn over three quarters, as these amounts were over the cap amount. In 2015, \$53.69 million was withdrawn to meet ABFA shortfalls, and \$71,265,213 was withdrawn as over the cap. In the second and third quarter of 2018, \$206,343,762 was withdrawn in total as over the cap.

According to the PRMA,<sup>107</sup> the funds will invest in 'qualifying instruments', including fixed interest investment-grade debt, currency deposits and hedging derivatives. These instruments are subject to the discretion of the Ministry of Finance and the Investment Advisory Committee, which the act creates. While the Stabilisation Fund's investment mandate is standard (to provide a buffer against negative macro-economic shocks or resource shortfalls), the Heritage Fund is particularly conservative in its mandate as a long-term investment fund. It seeks to invest in 'safe but low yielding investments' and is invested in AAA bonds. According to the 2018 annual report,<sup>108</sup> the Ghana Petroleum Funds are invested in the following:

- overnight and call deposits;
- discount notes;
- Treasury bills;
- short-term deposits;
- investment grade bonds;
- certificates of deposit;
- commercial papers; and
- medium-term notes

In 2018, returns for the Heritage Fund were 2.75%, and 0.85% in 2017. In 2018 returns for the Stabilisation Fund were 1.08% and 0.78% in 2017.<sup>109</sup> While the Stabilisation Fund has

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104 Government of Ghana, 2015, *op. cit.*

105 PIAC (Public Interest and Accountability Committee), *Annual Report on the Management and Use of Petroleum Revenues for the Period 2018*, [http://www.piacghana.org/portal/files/downloads/piac\\_reports/piac\\_2018\\_annual\\_report.pdf](http://www.piacghana.org/portal/files/downloads/piac_reports/piac_2018_annual_report.pdf), accessed 27 August 2019.

106 Republic of Ghana, Ministry of Finance, *2018 Annual Report on the Petroleum Funds*, 15 November 2018, <https://www.mofep.gov.gh/sites/default/files/reports/petroleum/2018-Petroleum-Annual-Report.pdf>, accessed 25 August 2019.

107 Government of Ghana, 2011, *op. cit.*

108 Republic of Ghana, 2018, *op. cit.*

109 *Ibid.*



performed well when compared to three-month treasuries, the Heritage Fund has performed well below both the S&P 500 and a 60/40 profile.<sup>110</sup>

The GIIF mandate is exceptionally broad, stipulating that investments can be made in projects with either financial or social returns.<sup>111</sup> The range of potential infrastructure sectors is also all-encompassing, including economic infrastructure, such as energy, transport, agribusiness, telecommunications, heavy industry, mining, and oil and gas; and social infrastructure, such as water, housing, health, education, security, sports and local government facilities. It seeks to catalyse additional private finance, engage in co-sponsoring arrangements and use a variety of innovative financial products. While the GIIF is still new, this mandate is concerning in terms of the possibility for investments in political projects when the specifications are so broad (as has been the experience in many countries). Investments thus far by the GIIF include co-funding in the development of a domestic airport terminal, a reported co-investment in a domestic port terminal, and an MoU with South Africa to build a 'Skytrain' public transport system.<sup>112</sup>

The Public Interest and Accountability Committee (PIAC) was created as an independent mechanism of oversight for the Petroleum Funds, ensuring that regulations are complied with.<sup>113</sup> This is in addition to the Petroleum Funds' standard accountability mechanisms of internal and external audits. The PIAC is comprised of a wide range of stakeholders, including professional organisations, religious groups, traditional leaders and other civil society organisations. The committee has a duty to provide semi-annual and annual reports on the fund management, as well as a platform for public information and participation.

Despite Ghana's efforts to pre-emptively create a robust resource management regime with its SWF, the Petroleum Funds did not achieve their intended purpose. After the discovery of oil the government embarked on unsustainable borrowing sprees against future revenues while depositing oil revenues into the funds. These two activities counteract each other and the objectives of an SWF.<sup>114</sup> For example, the government borrowed against future oil revenue to finance recurrent expenditure items such as a bloated public sector wage bill, interest payments and fuel subsidies.<sup>115</sup> In the years after oil discovery, Ghana has experienced high inflation and current account deficits that persist to the present (see Table 5), as well as lower-than-expected growth. Debt has risen steadily since oil was anticipated in 2007, subsequent to Ghana's receiving Heavily Indebted Poor Countries debt

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110 Kuseh J, 'How well are Ghana's Petroleum Funds performing?', *Ceditalk*, 9 February 2017, <https://www.ceditalk.com/2017/02/how-well-are-ghanas-petroleum-funds-performing/>, accessed 28 August 2019.

111 Government of Ghana, 'Ghana Infrastructure Investment Fund Investment Policy Statement', 6 April 2017, [https://www.mofep.gov.gh/sites/default/files/reports/economic/GIIF%20Investment%20Policy%20Statement\\_April62017.pdf](https://www.mofep.gov.gh/sites/default/files/reports/economic/GIIF%20Investment%20Policy%20Statement_April62017.pdf), accessed 25 August 2019.

112 GhanaWeb, 'Ghana infrastructure investment fund approves US\$30 million corporate loan to Ghana Airports Company Limited', <http://www.ghwebs.com/giif/mediaroom/press-releases/item/11-ghana-infrastructure-investment-fund-approves-us-30-million-corporateloan-to-ghana-airports-company-limited.html>, accessed 19 July 2018; Tshwane T, 'SA-Ghana deal the largest at Africa Investment Forum', *Mail & Guardian*, 8 November 2018, <https://mg.co.za/article/2018-11-08-sa-ghana-deal-the-largest-at-africa-investment-forum>, accessed 28 August 2019.

113 Government of Ghana, 2011, *op. cit.*

114 Bawumia M & H Halland, *op. cit.*; IFI representative 1, *op. cit.*; IFI representative 2, *op. cit.*; resource governance expert, *op. cit.*

115 IFI representative 1, *op. cit.*; Van der Ploeg R & S Wills, 'Harnessing Africa's oil wealth: Lessons from Ghana', International Growth Centre, <https://www.theigc.org/blog/harnessing-africas-oil-wealth-lessons-from-ghana/>, accessed 27 August 2019.

relief from the IMF and World Bank in the early 2000s (see Figure 4). Ghana's poor fiscal position ultimately led the country to seek IMF assistance in 2015, only four years after the extraction of oil began.<sup>116</sup>

Given that oil revenues are relatively small compared to the size of the economy, most these adverse impacts were not directly attributable to oil rents or the oil management regime. They were rather driven by raised expectations of future revenue, which has been called the 'pre-source curse'.<sup>117</sup> Specifically, the closely contested campaign for national elections in 2007–2008 meant that rival parties faced pressure to make promises regarding expected future oil revenues, which resulted in heavy borrowing and spending.<sup>118</sup> The global financial crisis provided a rationale for countercyclical expansionary fiscal policy even as fiscal conditions worsened in Ghana, with the projected oil revenues serving as a buffer to support this policy.<sup>119</sup> The government released overly optimistic oil projections that supported this fiscal policy. The Bank of Ghana also financed the country's debt in the first years of oil production, which then compounded these effects.<sup>120</sup>

With respect to the Petroleum Funds specifically, they have largely been managed within rules. However, the Finance Ministry has taken advantage of a buffer that allows the Stabilisation Fund cap to be legally revised. The cap was revised downward multiple times to finance debt/recurrent expenditures during the aforementioned overspending period.<sup>121</sup> This points to the difficulty of designing a fiscal buffer that allows flexibility for crises but is not used haphazardly. With regard to the Heritage Fund, yields have been low, at around 1% annual return on average. While this is in line with the fund's investment mandate, concerns have been raised over the logic of borrowing at high interest rates and investing abroad at low interest rates. Alternatives, such as using funds to pay off debt and decrease borrowing, or investing at least a portion of the revenues in higher risk, high-yield investments, have been suggested. However, higher risk investments also depend on the capacity of the Investment Advisory Committee, which has not met regularly – in contravention of the PRMA.<sup>122</sup> Outside of the Petroleum Funds, ABFA allocations have been spent in unfocused ways, allocated in a highly fragmented manner to projects that could

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116 Bawumia M & H Halland, *op. cit.*; Extractives Hub, *Managing Commodity Lifecycles: Petroleum*, 2016, <https://extractiveshub.org/servefile/getFile/id/4211>, accessed 28 August 2019.

117 Cust J & J Mihalyi, 'The Presource Curse', IMF Finance and Development, December 2017, <https://www.imf.org/external/pubs/ft/fandd/2017/12/pdf/cust.pdf>, accessed 28 August 2019.

118 Resource governance expert, *op. cit.*; IFI representative 1, *op. cit.*; Lwabukoma O, 'Governing African Extractives for Development: Lessons from Ghana's Petroleum Revenue Management Law', Africa Institute of South Africa Briefing, 122, July 2016, <http://www.hsrc.ac.za/uploads/pageContent/7260/Policy%20Brief%20122.Governing%20african%20extractives%20for%20development.pdf>, accessed 25 August 2019.

119 Bawumia M & H Halland, *op. cit.*

120 *Ibid.*

121 Republic of Ghana, 2018, *op. cit.*; Adam A & D Mihalyi, 'Optimizing Ghana's Fiscal Rule', Natural Resource Governance Institute Briefing, October 2017, <https://resourcegovernance.org/sites/default/files/documents/optimize-ghana-fisal-rule.pdf>, accessed 28 August 2019; Ghana Web, 'Ghana Petroleum Funds yielding low returns', 5 May 2018, <https://www.ghanaweb.com/GhanaHomePage/business/Ghana-Petroleum-funds-yielding-low-returns-648970#>, accessed 25 August 2019; Lwabukoma O, 2016, *op. cit.*; Anaman P & J Darko, 'Is Ghana's Petroleum Revenue Management Act (PRMA), 2011 (Act 815) an Effective Public Financial Management Tool for Public Investment and Consumption Smoothing?', University of Oxford, 2018, [https://www.bsg.ox.ac.uk/sites/default/files/2018-12/Anaman\\_Petroleum%20Revenue%20Management.pdf](https://www.bsg.ox.ac.uk/sites/default/files/2018-12/Anaman_Petroleum%20Revenue%20Management.pdf), accessed 20 September 2018.

122 PIAC, 2018, *op. cit.*

not be seen to completion (this was partly enabled by vague stipulations in the PRMA on the allocation of the ABFA amount, as well as political pressure). The PIAC also recently raised the issue of large amounts of ABFA money that have not been spent, with no allocations from the ABFA to the GIIF in recent years.<sup>123</sup>

While the Petroleum Funds still hold revenues and the result might have been worse if no oil management regime had been put in place, the relatively small size of oil revenues has meant that the Petroleum Funds rules have not had a broad impact.<sup>124</sup> More importantly, Ghana's difficulties in managing public and political expectations regarding oil have negatively affected fiscal discipline and monetary independence outside the Petroleum Funds.<sup>125</sup> Overall, Ghana's PFM has historically been weak, lacking formal debt and expenditure rules or monetary policy independence, other than when operating under past IMF programmes.<sup>126</sup>

One positive outcome of Ghana's experience has been the activism of the PIAC in bringing these issues to the attention of the public and opposition parties, putting pressure on politicians. Although the PIAC was initially financially constrained, which limited its ability to perform its duties, in 2015 the PRMA was amended to finance the PIAC from the ABFA.<sup>127</sup> As of 2019, the state will reportedly begin to prosecute cases of misuse of funds, which would be a triumph for the effectiveness of independent accountability mechanisms.<sup>128</sup>

## Nigeria

TABLE 6 NIGERIA SNAPSHOT	
Name of fund	Nigeria Sovereign Investment Authority
Year established	2012
Type of fund	Three funds: Future Generations Fund, Stabilisation Fund and National Infrastructure Investment Fund (NIF)
Seed capital	\$1 billion
AUM growth (% , 2018)	16; 7.73 from the three core funds (only from returns)
Current AUM	\$1.4 billion
AUM as % of GDP	0.37%
Investment strategy	Stabilisation Fund aims to achieve capital preservation, Future Generations Fund invests in long-term assets with higher returns (hedge funds and private equity), NIF invests in local infrastructure and development

123 Anaman P & J Darko, *op. cit.*

124 Resource governance expert, *op. cit.*

125 *Ibid.*; IFI representative 1, *op. cit.*; Bawumia M & H Halland, *op. cit.*

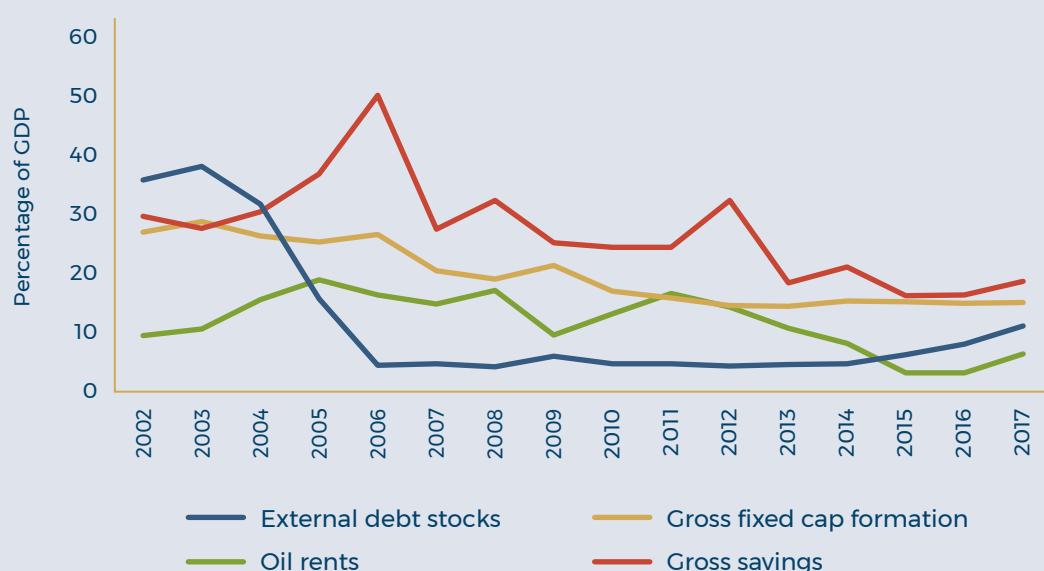
126 *Ibid.*

127 Government of Ghana, 2015, *op. cit.*

128 Ibrahim A, 'PIAC, EOCO partner to prosecute officials who divert, misuse petroleum funds', *Joy Online*, 25 February 2019, <https://www.myjoyonline.com/business/2019/February-25th/piac-eoco-partner-to-prosecute-officials-who-divert-misuse-petroleum-funds.php>, accessed 28 August 2019.

Additional deposits	Contributions in 2013, 2016 and 2017, approximately \$1.43 million in aggregate
Drawdowns	None
GDP growth (% , 2018)	1.94
<b>NIGERIA ECONOMIC INDICATORS</b>	
External debt stocks (% of GNI, 2018)	12.20
Gross fixed capital formation (% of GDP, 2017)	14.72
Current account (% of GDP, 2017)	2.76
Interest payment (% of revenue, % of expense)	-
Interest spread (% , 2018)	7.2
Inflation (annual % , 2018)	12.09
Oil rents (% of GDP, 2017)	6.12
Human Development Index	0.532

Figure 5 Select macro-economic indicators for Nigeria



Source: World Bank, 'World Development Indicators', <https://datacatalog.worldbank.org/dataset/world-development-indicators>, accessed 25 October 2019

A brief history of Nigeria's resource revenue regime is helpful in understanding the context of the country's current SWF. After discovering oil in the 1970s Nigeria established a number of resource revenue management mechanisms, but still struggled to avoid volatile spending patterns and unsustainable borrowing.<sup>129</sup> The primary resource fund since 2004

129 Ugwuibe C, 'Strengthening the Nigerian Sovereign Investment Authority: A Policy Analysis of the Nigerian Excess Crude Account and the Nigerian Sovereign Investment Authority Act', MA thesis, University of California Los Angeles, 2012, <https://escholarship.org/uc/item/5zn1h1d6>, accessed 20 September 2019.

has been the Excess Crude Account (ECA), informally a stabilisation fund domiciled at the Nigerian Central Bank. While the ECA accumulated a large amount of resource revenues at different points in time, it was established without legal backing and has been subject to arbitrary withdrawals at the discretion of the president.<sup>130</sup>

The 2007 Fiscal Responsibility Act attempted to provide some legal backing for the ECA by setting an oil reference price (based on a long-term oil price average) for deposits and withdrawals.<sup>131</sup> Although the ECA did provide a stabilising effect during the global financial crisis, it has continued to spend on items outside its rules such as subsidies and loans, and has not been able to stabilise effectively. For example, from 2005–2015, \$201 billion accrued in the account but \$204 billion was withdrawn, indicating negative net transfers.<sup>132</sup> The distribution of resource revenues from the ECA has consistently been hampered by legal and political disputes with states, given Nigeria's constitutional revenue-sharing agreement between federal, state and local governments.<sup>133</sup> While the ECA reached \$20 billion in 2008, the account depleted significantly after the financial crisis and falls in oil prices, dropping to \$4 billion in 2010. The ECA still held \$2.45 billion at the end of 2018, but held just \$249 million as of February 2019.<sup>134</sup>

In 2011 the Nigeria Sovereign Investment Authority Act established the Nigeria Sovereign Investment Authority (NSIA),<sup>135</sup> a new, legally mandated SWF. The NSIA manages three funds: the Future Generations Fund (a savings fund), the Stabilisation Fund and the National Infrastructure Investment Fund (NIF, a domestic investment fund). The NSIA was initiated with \$1.5 billion in seed capital. The NSIA is a separate legal entity and ministers and the central bank do not exercise direct control over the fund. The fund is managed by a three-person executive committee that reports to the Board of Directors. Unlike many other funds, the board members are independent private sector experts rather than government officials.<sup>136</sup> The 35-member governing council is led by Nigeria's president and supervises the board. As is standard, the NSIA publishes internally and externally audited reports and detailed annual reports.<sup>137</sup>

According to the NSIA Act, additional deposits to the NSIA come from the Federation Account, which allocates public revenue to national, state and local governments.

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130 NEITI (Nigeria Extractive Industries Transparency Initiative), 'The Case for a Robust Oil Savings Fund for Nigeria', Occasional Paper, 2, July 2017, <https://eiti.org/sites/default/files/documents/neiti-ops2-180717.pdf>, accessed 24 September 2019.

131 Natural Resource Governance Institute, 'Nigeria', Country Strategy Note, <https://resourcegovernance.org/sites/default/files/documents/country-strategy-note-nigeria.pdf>, accessed 21 September 2019.

132 NEITI, 2017, *op. cit.*; anti-corruption expert, *op. cit.*

133 Amusan L, Saka L & AJ Omede, 'Sovereign Wealth Fund and fiscal federalism in Nigeria (2011-14): An assessment of contending issues', *Regional & Federal Studies*, 27, 4, 2017, pp. 441-463.

134 Anthony-Uko N, 'Election spending: Nigeria govt further depletes excess crude account to \$249m', *business a.m.*, 1 March 2019, <https://www.businessamlive.com/election-spending-nigeria-govt-further-depletes-excess-crude-account-to-249m/>, accessed 24 September 2019; Chen J, 'Excess crude account', *Investopedia*, <https://www.investopedia.com/terms/e/excess-crude-account.asp>, accessed 25 September 2019.

135 Government of Nigeria, 'Nigeria Sovereign Investment Authority (Establishment etc.) Act 2011, No. 15', 3 June 2011, <https://nsia.com.ng/-/nsia/sites/default/files/downloads/NSIA%20Act.pdf>, accessed 10 September 2019.

136 IFI representative 1, *op. cit.*; NSIA (Nigeria Sovereign Investment Authority), 'Board of Directors', <https://nsia.com.ng/governance/board-of-directors>, accessed 24 September 2019.

137 *Ibid.*

Revenues above the budgetary smoothing amount, 'an amount equal to ten percent of monthly Residual funding up to a cumulative maximum amount at any one time of 2.5 percent of the Projected Federation Hydrocarbon Revenue for the year of such funding', are transferred to the authority.<sup>138</sup> However, the ECA is still the initial recipient of resource windfalls before they are allocated to the NSIA. Up until 2017 the NSIA's division of incoming revenues was 40% to the NIF, 40% to the Future Generations Fund and 20% to the Stabilisation Fund. Since 2017 the NSIA has increased the allocation to the infrastructure portion of the fund, which now holds 50% of the fund allocations, with 30% in the Future Generations Fund.<sup>139</sup> Since its establishment, the NSIA has received three additional contributions: \$250 million in dividends in 2016 from Nigeria LNG Limited (NLNG), the national oil company, \$250 million in 2017 from the ECA, and \$650 million in dividends in 2018 from NLNG again.<sup>140</sup> The government has not drawn down on the NSIA since its establishment.

The NSIA established the Externally Managed Investments Committee to manage the investments and risks of the Future Generations Fund and Stabilisation Fund. The three funds have publicly available investment strategies, with separate investment committees for the NIF and the Future Generations Fund/Stabilisation Fund.<sup>141</sup> However, unlike the strict investment mandates in Ghana and (in practice) Botswana, the investment mandate is broad, with some discretion given to the fund managers. The NSIA's annual reports provide extensive detail on the investment strategies of the various funds, the structure of fund management, the returns on a selection of the asset classes, and project-level detail on certain investments.<sup>142</sup>

The Stabilisation Fund's investment strategy balances the need for capital preservation and modest returns. It invests in Treasury bills, Treasury bonds, term deposits and Eurobonds. Every quarter the finance minister can ask to draw down on the Stabilisation Fund an amount equal to the difference between the projected and actual oil revenues, if negative, after the Budgetary Smoothing Amount has been depleted.<sup>143</sup> In 2018 Return on Capital Employed (ROCE) was 7.2% for the Stabilisation Fund. The Future Generations Fund looks for higher risk adjusted returns, investing in private equity and hedge funds in addition to developed and emerging market equities. It can invest in less liquid assets given its 20-year time horizon. It is also diversified in inflation and deflation hedges. The 2018 ROCE was 8.3% for the Future Generations Fund. The NIF uses a range of innovative financial tools to invest in domestic developmentally significant projects across different sectors.<sup>144</sup> While 10% of the NIF's investments can be invested in social projects, there is no clear indication of any

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138 Government of Nigeria, 2011, *op. cit.*

139 NSIA, *NSIA Annual Report 2017*, <https://www.nsia.com.ng/~nsia/sites/default/files/annual-reports/NSIA%20Annual%20Report-2017%20%281%29.pdf>, accessed 20 September 2019.

140 NSIA, 'Investor relations', <https://nsia.com.ng/investor-relations>, accessed 20 September 2019.

141 NSIA, 'Annual reports', <https://www.nsia.com.ng/investor-relations/financials-statement/annual-reports>, accessed 20 September 2019.

142 *Ibid.*

143 Government of Nigeria, 2011, *op. cit.*

144 NSIA, 'Key facts', <https://nsia.com.ng/investor-relations/key-facts>, accessed 20 September 2019.



mechanism for alignment with budget priorities in these cases, with discretion given to fund managers. This can potentially provide a loophole for wasteful spending and also put inflationary pressures on the economy.<sup>145</sup> The ROCE was 7.7% for the NIF.

Innovative co-investments of the NSIA's NIF include medical technology for cancer screening,<sup>146</sup> the second Niger Bridge and the Abuja-Kano Highway,<sup>147</sup> oil capture development,<sup>148</sup> state land restoration,<sup>149</sup> a fund for agricultural finance<sup>150</sup> and an expected \$1.5 billion ammonium plant for fertiliser through co-investment with Moroccan company OCP,<sup>151</sup> and a \$200 million partnership with South African insurer Old Mutual in agriculture and real estate.<sup>152</sup> The NSIA has partnered with AfriEXIM Bank and the Bank of Industry to develop special economic zones that support export-orientated manufacturing industries.<sup>153</sup> It has also supported domestic private equity and venture capital.

In 2017, the NSIA partnered with GaurantCo, a subsidiary of the Private Infrastructure Development Group, to establish InfraCredit, a \$200 million infrastructure credit facility that will enhance local corporate and infrastructure bonds.<sup>154</sup> The objective of the facility is to unlock new sources of finance for infrastructure development, such as pension and insurance funds. It has attracted support from the African Development Bank, the KfW and the Africa Finance Corporation, which has increased its reputational legitimacy.<sup>155</sup> The NSIA also signed an MoU with the Infrastructure Concession Regulatory Commission for cooperation on infrastructure development, including the development of a publicly listed infrastructure public-private partnership fund to help mobilise private capital for projects in progress.<sup>156</sup> The NSIA also manages investments for third parties, including the Debt Management Office and the federal government's stabilisation account.<sup>157</sup>

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145 Oshionebo E, 'Mismanagement of Nigeria's oil revenues: Is the Nigeria Sovereign Investment Authority the panacea?', *The Journal of World Energy Law & Business* 10, 4, August 2017, pp. 329-347.

146 *Africa News*, 'Fight against cancer: GE Healthcare collaborates with Nigeria Sovereign Investment Authority (NSIA) to advance early cancer detection in Nigeria', 28 February 2019, <https://www.africanews.com/2019/02/28/fight-against-cancer-ge-healthcare-collaborates-with-nigeria-sovereign-investment-authority-nsia-to-advance-early-cancer-detection-in-nigeria/>, accessed 21 September 2019.

147 NIPC (Nigeria Investment Promotion Commission), 'ICRC, NSIA sign agreement to improve infrastructure delivery', 29 March 2019, <https://nipc.gov.ng/2019/03/29/icrc-nsia-sign-agreement-to-improve-infrastructure-delivery/>, accessed 21 September 2019.

148 Bungane B, 'Will Nigeria's fresh look into gas flaring, finally end it?', *ESI Africa*, 18 June 2019, <https://www.esi-africa.com/industry-sectors/generation/will-nigerias-fresh-look-into-gas-flaring-finally-end-it/>, accessed 21 September 2019.

149 UK AID, 'Improving communications of the Nigerian Sovereign Investment Authority (NSIA)', August 2018, <https://www.pdfnigeria.org/wp-content/uploads/2018/08/Improving-Communications-of-the-Nigeria-Sovereign-Investment-Authority-NSIA.pdf>, accessed 20 September 2019.

150 *Ibid.*

151 Egbejule E, 'OCP fertiliser deals take Nigeria closer to self-sufficiency', *The Africa Report*, 18 March 2019, <https://www.theafricareport.com/10431/ocp-fertiliser-deals-take-nigeria-closer-to-self-sufficiency/>, accessed 20 September 2019.

152 Radley D, 'Old Mutual partners with Nigeria's Sovereign Wealth Fund', Old Mutual, <http://ww2.oldmutual.co.za/old-mutual-partners-with-nigeria-s-sovereign-wealth-fund>, accessed 20 September 2019.

153 *Business Times Africa*, 'Nigeria signs agreements with Afreximbank, Bol, NSIA to develop special economic zones', 9 February 2019, <http://www.businesstimesafrica.net/index.php/banking/item/3995-nigeria-signs-agreements-with-afreximbank-boi-nsia-to-develop-special-economic-zones>, accessed 21 September 2019.

154 Guarantco, 'NSIA & Guarantco establish the Infrastructure Credit Enhancement Facility (InfraCredit)', 17 January 2017, [https://www.guarantco.com/storage/pdf/Press-Release\\_NSIA-and-Guarantco-Announce-Establishment-of-InfraCredit.pdf](https://www.guarantco.com/storage/pdf/Press-Release_NSIA-and-Guarantco-Announce-Establishment-of-InfraCredit.pdf), accessed 21 September 2019.

155 *Financial Nigeria*, 'AfDB invests \$15 million in NSIA-backed InfraCredit', 12 April 2019, <http://www.financialnigeria.com/afdb-invests-15-million-in-nsia-backed-infracredit-news-1805.html>, accessed 21 September 2019.

156 NIPC, 2019, *op. cit.*

157 NSIA, Annual Report 2017, *op. cit.*

## Overall, the NSIA is a major improvement on other resource funds in Nigeria's past and the current ECA, in terms of rules, transparency and investment management

Overall, the NSIA is a major improvement on other resource funds in Nigeria's past and the current ECA, in terms of rules, transparency and investment management. This is an accomplishment, given the lack of true separation of powers in the federal government, federal versus state disputes and a culture of political patronage in Nigeria that does not favour fiscal discipline.<sup>158</sup> The NSIA's initial success comes in part from merit-based appointments, including the president, board members and members of investment committees, who are private sector finance professionals with international experience. These personnel appointments, in addition to the knowledge that the NIF (as a government-backed fund) and its projects enjoy political backing, have assisted the fund in gaining international trust and credibility and allowing the NIF to crowd in significant amounts of external finance.<sup>159</sup> Although the fund was initially politically contentious given the failures of the ECA and persistent federal-state disputes, as a result of significant public engagement efforts many states now support the fund.<sup>160</sup> The governing council reflects different levels of government in the country, which has assisted in achieving broad-based buy-in.<sup>161</sup> The NSIA has also not been drawn down on since establishment and has survived a change in presidency without losing relevance.

However, it is important to flag the comparatively tiny size of the NSIA – it is currently a mere 0.37% of GDP. Although oil revenue has slumped in the last couple of years owing to the decline in commodity prices, statistics in recent years show oil sitting consistently above (and sometimes well above) 10% of GDP. Thus the NSIA's small fiscal impact in part explains why the fund has not been tampered with in the same way as the ECA.<sup>162</sup> In terms of political incentives, the international legitimacy dividend gained from the NSIA (especially if Nigeria seeks external budget support in future) likely outweighs the political incentive to tamper with a small amount. However, the NSIA's small size also questions the effectiveness of the savings and stabilisation sub-funds and its overall ability to have a significant impact on PFM in the country, at least at this point in time.<sup>163</sup> According to Figure 5, since the establishment of the NSIA, investment has trended downward and debt has increased slightly as oil revenues have decreased. However, given its small size any trends cannot realistically be attributed to the NSIA.

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158 Development economist 2, *op. cit.*; anti-corruption expert, *op. cit.*

159 Anti-corruption expert, *op. cit.*; IFI representative 1, *op. cit.*

160 UK AID, *op. cit.*

161 Oshionebo E, *op. cit.*

162 Anti-corruption expert, *op. cit.*

163 Resource governance expert, *op. cit.*; *ibid.*

The initial accomplishments of the NSIA should not be diminished, especially in terms of the example it provides for a legislatively robust set-up, transparent practices and a successful domestic investment sub-component

At this point, the ECA is still Nigeria's most important resource revenue fund, and it still does not have clear rules on setting the oil reference price, which is subject to the annual discretion of the president.<sup>164</sup> The finance minister has recently recognised the need for more revenues from the ECA to accrue to the NSIA, while many have called for the ECA to be abolished altogether and replaced by the NSIA.<sup>165</sup> However, major changes will always be difficult politically. The ECA has traditionally been used both to support Nigeria's currency and to satisfy a range of political spending pressures, and has also allowed Nigeria to maintain relatively low debt levels. Without broader changes in fiscal discipline and culture, these fiscal challenges and pressures will remain, and are currently intensified given the ECA's exceptionally low balance.<sup>166</sup> In spite of these challenges, the NSIA's strong groundwork could cement the building blocks for it to become a more relevant SWF if there are serious political or bureaucratic changes in Nigeria. The initial accomplishments of the NSIA should not be diminished, especially in terms of the example it provides for a legislatively robust set-up, transparent practices and a successful domestic investment sub-component.

## Political economy analysis: Are African SWFs fulfilling their mandates?

The four case study SWFs all have some form of basic legal, institutional and accountability foundations on paper; however, their operational success has varied. The following section therefore seeks to distil policy takeaways from the political economy issues underlying these funds. The first subsection analyses the interplay between a fund's institutional structure and the country's overarching fiscal culture, highlighting the difficulties in overcoming the latter. The second subsection examines how the alignment of incentives in the domiciled countries can sometimes shift the prevailing norms and allow SWFs to operate effectively. The final section highlights the importance of national PFM reform to align with an SWF's mandate.

164 Yar' Adua Foundation, 'A savings and stabilization mechanism for Nigeria', Roundtable Report, 24 May 2019, [http://yaraduafoundation.org/files/Stakeholder\\_Roundtable\\_Report.pdf](http://yaraduafoundation.org/files/Stakeholder_Roundtable_Report.pdf), accessed 20 September 2019; anti-corruption expert, *op. cit.*

165 NEITI, 2017, *op. cit.*; Vanguard, 'FG commits to improved funding of NSIA', 13 April 2019, <https://www.vanguardngr.com/2019/04/fg-commits-to-improved-funding-of-nsia/>, accessed 21 September 2019; Odude F, 'The sovereign wealth fund should subsume the Excess Crude Account', *Financial Nigeria*, 17 May 2018, <http://www.financialnigeria.com/the-sovereign-wealth-fund-should-subsume-the-excess-crude-account-blog-350.html>, accessed 19 September 2019; Yar' Adua Foundation, *op. cit.*

166 Anti-corruption expert, *op. cit.*

## The interplay between fiscal culture and fiscal rules

Literature and policy papers highlight the importance of well-defined and focused SWF rules, investment strategies and accountability mechanisms to ensure that SWFs work explicitly towards their macro-economic and/or development mandates. However, this has proven difficult in practice in the case study countries. SWFs are often used to fund recurrent expenditures, invest in questionable projects, or even implicitly as justification to borrow. This study has indicated that fiscal culture plays an important role in determining the ability of a fund to serve its stated purpose in the economy. The case studies have shown that if there is a lack of high-level commitment to fiscal discipline, funds will often either be intentionally designed with weak fiscal rules or intentionally limited in their influence by a mandate that comprises a very small pot of money.

Fiscal culture plays an important role in determining the ability of a fund to serve its stated purpose in the economy

In Ghana the government borrowed unsustainably at high interest rates while its well-regulated Petroleum Funds invested in low-yielding assets. An undisciplined fiscal and monetary culture stemming from the pre-source curse has overshadowed the existence of a comparatively small pot of rules-based funds (the Petroleum Funds) in relation to overall GDP.<sup>167</sup>

In Angola the lack of rules governing prescribed FSDEA investments meant that using the FSDEA to invest in political projects was within the fund's mandate. In this case, the fund was more likely created to validate these investments than to achieve macro-economic or development objectives, with a minimal base of rules put in place to gain international credibility rather than promote fiscal discipline.<sup>168</sup> Similar issues have arisen from Angola's stabilisation funds, which are not rules based, have not achieved stabilisation and have been subject to political inquiry over missing funds.<sup>169</sup>

In Nigeria the ECA was initially not underpinned by law, and intentionally designed without rules. As a result, Nigeria has consistently performed poorly in managing oil volatility and has not used revenues for sustainable expenditure.<sup>170</sup> While oil revenues were used to prevent borrowing during the financial crisis, the effectiveness of this manoeuvre was contingent on the fact that oil revenues had been so high previously that funds were still

167 Resource governance expert, *op. cit.*; Bawumia M & H Halland, *op. cit.*; Lwabukoma O, 2016, *op. cit.*

168 Resource governance expert, *op. cit.*

169 UN Committee for Development Policy, 2016, *op. cit.*

170 NEITI, 2017, *op. cit.*

available in the ECA despite undisciplined spending, rather than as a result of prudent or rules-based stabilisation procedures.<sup>171</sup> The dramatic decrease in ECA reserves since the oil price crash is evidence of this. Although the newer NSIA is, laudably, much more stringent than the ECA, the fact that so few funds have been transferred from the ECA to the NSIA is not a coincidence when considering existing political pressures for undisciplined spending.

Botswana's Pula Fund, which holds almost 40% of GDP, does not have any explicit withdrawal regulations. The government has been free to withdraw funds when facing budget shortfalls for expenses such as education, government pensions and salaries.<sup>172</sup> However, the flexibility of the Pula Fund's fiscal rules has not spiralled into unsustainable spending sprees as in the other countries, and the fund has stabilised the budget in limited instances. The Pula Fund is noted as contributing to Botswana's low risk premium, a key positive spillover of SWFs according to literature.<sup>173</sup> Yet, considering the Pula Fund has few rules and regulations, it is questionable whether this is explicitly attributable to the design of the fund. Technically, the structure of the fund does not contain safeguards against the possibility of misuse by a different political regime in future, although the establishment of the fund within the reserves of the credible central bank does provide some de facto protection. Outside of the fund, Botswana has also adhered to its broader budget management and expenditure rules, and a conservative fiscal culture has prevented blatant corruption or macro-economic mismanagement.<sup>174</sup> Therefore, more realistically, the fund has served as a symbol that augments domestic and international buy-in within an existing national culture of fiscal discipline.

However, the Pula Fund has also only marginally increased its AUM over its lifespan, as the remaining horizon for diamond production becomes shorter. Little transparency on prescribed fund uses and withdrawals has made it impossible to fully know what some funds have been used for.<sup>175</sup> Therefore, even though the Pula Fund has been managed prudently, the development of explicit fiscal rules supporting savings would more effectively have targeted the fund's paramount purpose of saving for future generations.<sup>176</sup>

Overall, it is worth noting that the fiscal discipline challenges highlighted in this section are often expected and difficult to avoid. This is because SWFs are state-owned entities, and political incentives are inherently short term. Election cycles have an enormous impact on political decisions and on the structure of budget management.<sup>177</sup> Additionally, budgets are based on yearly projections of revenue inflows and outflows, whereas SWFs are based on long-term assets and liabilities. This is compounded by the fact that commodity price swings are also often long term, materialising as sustained drifts rather than short cycles.<sup>178</sup>

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171 Anti-corruption expert, *op. cit.*

172 Konopo J *et al.*, *op. cit.*

173 Moody's Investors Service, *op. cit.*

174 Jefferis K, *op. cit.*

175 Konopo J *et al.*, *op. cit.*

176 Resource governance expert, *op. cit.*

177 Development economist 2, *op. cit.*

178 *Ibid.*

The structure of commodity cycles and SWF mandates therefore requires long-term projections and conflicts with short horizon fiscal procedures. Designing fiscal rules to reconcile this incongruence is difficult in any country, especially in developing countries with weaker capacity and political incentives that often dominate institutional rules. In Nigeria misaligned incentives are further compounded by the attempt to implement a centralised resource revenue management system in a country that operates within a broader decentralised fiscal management system with federal and local governments.<sup>179</sup> Overall, while many countries have tried to achieve disciplined structures when in commodity price crunches or before revenues accrue, the case studies have shown that SWFs are only truly tested when revenues are high – at these times it becomes clear whether fiscal discipline prevails and short-sighted incentives can be mitigated.<sup>180</sup>

While a strict rules-based fund on paper may certainly make corruption more difficult, funds will often either deliberately be created with loose rules or politicians will find ways to work around existing rules

This section underlines that while a strict rules-based fund on paper may certainly make corruption more difficult,<sup>181</sup> funds will often either deliberately be created with loose rules or politicians will find ways to work around existing rules. In the case study countries, this has often resulted in high debt and inflation, as well as budget volatility, despite the existence of an SWF. In contrast, a disciplined fiscal culture can sometimes partly overcome weak SWF rules, as in Botswana. Globally, there are developing countries that have established SWFs with strong fiscal rules, counteracting weak existing institutional contexts and misaligned incentives. Examples include Chile, Kazakhstan, Timor-Leste and Indonesia. Peru provides an example of a fund that has instituted an ‘escape clause’, which allows for the revision of rules in emergencies without allowing this to become a loophole, as has been the case with the stabilisation fund cap revisions in Ghana.<sup>182</sup> In Nigeria and

In Nigeria and Ghana the legal foundations of the NSIA and Petroleum Funds show potential, although the small size of funds under their ambit relative to overall GDP currently limits their influence

179 Saka L & AJ Omede, *op. cit.*

180 Anti-corruption expert, *op. cit.*

181 IFI representative 2, *op. cit.*; natural resource governance policy expert 2, *op. cit.*

182 Mihalyi D & L Fernandez, ‘How Did Fiscal Rules Hold Up in the Commodity Price Crash?’, NRG, June 2018, <https://resourcegovernance.org/sites/default/files/documents/fiscal-rules-commodity-crash.pdf>, accessed 20 October 2019.



Ghana the legal foundations of the NSIA and Petroleum Funds show potential, although the small size of funds under their ambit relative to overall GDP currently limits their influence. Acknowledging these challenges, the remaining two sections go into more detail on strategies to overcome them and achieve rules-based SWFs and fiscal management in difficult contexts.

## Aligning incentives to achieve buy-in

The above analysis highlights that establishing an SWF in a country with weak and politicised institutions is an uphill battle in terms of enforcing rules-based governance. However, positive examples from the case study countries also show how short-sighted or self-serving political objectives can be altered, even in difficult contexts. This can be done by changing or increasing the costs of political incentives to overspend.<sup>183</sup>

Positive examples from the case study countries also show how short-sighted or self-serving political objectives can be altered, even in difficult contexts

The management of expectations, creation of public and political awareness, and generation of buy-in are all often overlooked in the process of designing the technical components of an SWF. Misinformed public and political expectations, in particular those that are raised too high, can contribute to the lack of commitment to rules.<sup>184</sup> In Botswana the narrative around the endowment of diamonds and the Pula Fund was never centred on spending commitments and promises of immediate developmental results. The narrative of a long-term sustainable future was cemented into the public conscious, to the extent that current public and media criticisms of the Pula Fund do not concern a lack of immediate tangible results but rather the lack of sufficient growth to ensure savings for the future.<sup>185</sup> Granted, Botswana's small size, higher development status and lack of political pressures cannot be ignored in terms of improving the ability to effectively manage expectations.

With the NSIA in Nigeria, emphasis was also put on managing expectations and driving buy-in in a more difficult context. The NSIA faced strong opposition from state governments, which were dissatisfied with both the lack of discipline of the ECA and the

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183 Ugwuibe C, *op. cit.*; Resource governance expert *op. cit.*; anti-corruption expert, *op. cit.*

184 Resource governance expert, *op. cit.*; UNU WIDER, *Oil In Ghana: How Inflated Expectations of Oil Revenues Led to a Deterioration in Macroeconomic Management*, WIDER Research Brief, 2017/3, 2017, <https://www.wider.unu.edu/publication/oil-ghana>, accessed 28 August 2019.

185 IFI representative 1, *op. cit.*

disadvantage at which it put state governments.<sup>186</sup> However, through continuous public engagement with all levels of government, the federal government was able to properly explain the NSIA and provide reassurance, eventually achieving buy-in and reducing negative expectations.<sup>187</sup> Efforts to build a coalition of support for a proposed fund by addressing concerns and giving opposing political parties or societal groups a role in fund governance are important in ensuring a fund's longevity beyond political cycles.<sup>188</sup> Choosing a respected and independent president for the fund who is better equipped to stand up to political pressure can also assist in this process.

Efforts to build a coalition of support for a proposed fund by addressing concerns and giving opposing political parties or societal groups a role in fund governance are important in ensuring a fund's longevity beyond political cycles

The story of the FSDEA in Angola shows that establishing a fund linked closely to the incumbent political party and president creates an inherent political risk. Given the hostility between the administration that established the fund and the subsequent administration, the FSDEA has shifted from an internationally respected fund to a greatly handicapped fund, where almost half of its AUM has been withdrawn arbitrarily. Thus achieving buy-in and commitment within the state beyond political parties is critical.<sup>189</sup> While the political party in Angola did not anticipate a change in power, such certainties are never guaranteed.

In Ghana the pre-emptive establishment of a strong legal backing for resource governance with detailed disclosures on spending and investments is laudable; however, management of political expectations was not given the same weight. Oil forecasts were not properly estimated and communicated, resulting in pressure to spend resource revenues in order to gain votes at the expense of long-term sustainability.<sup>190</sup> While there is no way to fully alleviate the pressure on politicians to make spending and investment promises in order to win elections, in Ghana little effort was made to temper this wave of anticipation by promoting a long-term vision. Instead, both parties chose to ride and even heighten the wave of anticipation.<sup>191</sup> In some cases, a country operating in a challenging political context may only be able to learn from experience. The painful after-effects on the Ghanaian

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186 Amusan L, Saka L & AJ Omede, *op. cit.*; UK AID, *op. cit.*

187 UK AID, *op. cit.*

188 Resource governance expert, *op. cit.*

189 *Ibid.*

190 UNU WIDER, *op. cit.*

191 Resource governance expert, *op. cit.*; Lwabukoma O, *op. cit.*; Bawumia M & H Halland, *op. cit.*

economy of receiving IMF assistance do seem to be driving motivation to chart a different course forward.<sup>192</sup>

The benefits of international reputational credibility can also align political incentives to support strong institutional structures. If funds are only created to appear robust at surface level, they will often eventually break down with no real winners, as in the case of Angola. However, the NSIA in Nigeria demonstrates the spill-over effects of creating a robust fund. The appointment of a credible president, board and investment managers, and establishment of a legally independent fund (which is important in Nigeria given the history of resource mismanagement by the government and central bank) created a strong legitimacy dividend domestically and internationally.<sup>193</sup> This has allowed the infrastructure fund, in particular, to mobilise large amounts of capital from a relatively small base, for mostly credible projects. In Nigeria, establishing the infrastructure fund within an SWF rather than separately also had important implications in terms of credibility and image. Nigeria has a history of corrupt and mismanaged special funds, so establishing the NIF within the NSIA helped to separate the NIF from the image of past extra-budgetary funds.<sup>194</sup> The credibility of the NSIA can also work to Nigeria's advantage in terms of the cost of future potential capital. For any political structure, barring a complete kleptocracy, these tangible results are a win that can boost the reputation of political parties. It is therefore important for fund architects to relay to politicians the link between credible institutional underpinnings and the political legitimacy dividend from an effectively functioning fund.

Finally, devising an inclusive process for fund accountability can provide a strong defence against political use of a fund. In the case of Ghana, the architects of the Petroleum Funds managed to institute an effective informal check on the funds' abuse of rules. Before establishing the funds, the government's massive public awareness creation campaign explained the purpose of the fund and sought inputs into its setup.<sup>195</sup> This created both an informed public and a sense of public ownership of the Petroleum Funds. Establishing a credible and independent accountability mechanism, the PIAC, comprised of reputable and diverse members of civil society and the private sector, then created the vehicle for public grievances to be aired and an independent check on the government's power. When politicians tried to draw down on the stabilisation fund in contravention of the Petroleum Revenue Management Act, public and PIAC outcry led to pressure on government to rectify the situation.<sup>196</sup> In the other case study countries, efforts to create serious formal and informal checks removed from politics have not been as strong. The motivation to establish strong accountability is obviously weaker in countries with weaker democracies, and unique to the power of different interest groups in any specific country.<sup>197</sup> Overall, ensuring that information is provided as deeply and widely as possible, as well as

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192 IFI representative 2, *op. cit.*

193 Anti-corruption expert, *op. cit.*

194 *Ibid.*

195 Resource governance expert, *op. cit.*; Lwabukoma O, *op. cit.*

196 Resource governance expert, *op. cit.*; Bawumia M & H Halland, *op. cit.*

197 Development economist 1, *op. cit.*

placing requirements on a fund that force transparency, is key to improving the chances of effective accountability.<sup>198</sup>

Ensuring that information is provided as deeply and widely as possible, as well as placing requirements on a fund that force transparency, is key to improving the chances of effective accountability

## Advocating for broader public financial management reform

Lastly, it is critical that SWFs are conceptualised within a country's broader fiscal framework, and that governments make serious efforts to encourage simultaneous enabling fiscal reforms. As the unsustainable spending in Ghana, Angola and Nigeria has shown, a lack of broader fiscal alignment can quickly neutralise any benefits of an SWF.<sup>199</sup> Even in the case of Botswana, limited industrial diversification from diamonds, as well as limited growth in the Pula Fund, speaks to a fiscal regime that has not been fully effective.<sup>200</sup> Driving broader reforms can be difficult when systems of loose discipline and patronage are entrenched in fiscal culture. The way in which an SWF is presented both within government and to the public can affect this dynamic. For example, countries should present a resource discovery as an urgent impetus for PFM reform that is necessary to capitalise on revenues, and as part of a strategy that only includes an SWF as one of many tools to do this. In contrast, the above three case study countries predominantly conceptualised resource wealth as an isolated occurrence to be managed through an isolated mechanism. Broader reforms in debt management and expenditure and budget legislation should be required alongside the establishment of an SWF (if strong frameworks are not already in place), in order to avoid the familiar case of borrowing unsustainably while saving in an SWF.<sup>201</sup> Examples include debt ceilings, deficit-to-GDP ratios, balanced budget rules, limits on resource revenues entering the budget, and nominal spending growth ceilings, as well as the

It is critical that SWFs are conceptualised within a country's broader fiscal framework, and that governments make serious efforts to encourage simultaneous enabling fiscal reforms

198 IFI representative 2, *op. cit.*; resource governance expert, *op. cit.*; Bauer A, Toledano P & M Rietveld, *op. cit.*

199 Lwabukoma O, *op. cit.*; Bawumia M & H Halland, *op. cit.*; NIPC, 2019, *op. cit.*; Jensen S & F Paulo *op. cit.*

200 Resource governance expert, *op. cit.*

201 Development economist 2, *op. cit.*; Resource governance expert, *op. cit.*

establishment of independent fiscal councils to increase transparency by assessing current fiscal activity and compliance with fiscal rules.<sup>202</sup> In the case of Ghana, after experiencing the economic fallout of the oil discovery and having to borrow from the IMF, the country has now committed to establishing a new set of fiscal rules that apply to all government spending, along with a fiscal council.<sup>203</sup>

The above three case study countries predominantly conceptualised resource wealth as an isolated occurrence to be managed through an isolated mechanism. Broader reforms in debt management and expenditure and budget legislation should be required alongside the establishment of an SWF (if strong frameworks are not already in place), in order to avoid the familiar case of borrowing unsustainably while saving in an SWF

A fund must also be considered in relation to monetary policy. For example, Nigeria uses a substantial portion of its resource reserves to support its currency, which has not been realistically considered in relation to the revenues desired to accrue to the NSIA.<sup>204</sup> Botswana's Pula Fund is part of the BoB reserves, which means that it is highly integrated with monetary policy.

With regard to resource revenues invested domestically (either through a development fund or through the normal budget), governments should ensure a specific and publicised national public investment programme is already in place when an SWF is established.<sup>205</sup> The programme should include projects that have been independently assessed for financial viability, and take into account absorptive capacity constraints within the investment timeline.<sup>206</sup> When the public and political opposition/interest groups are aware of the country's investment programme, this can increase pressure on politicians to spend on credible investments rather than political projects and recurrent expenditures. Botswana's policy emphasis on investing rather than spending resource revenues and adherence to its NDPs is a testament to this strategy.<sup>207</sup> In contrast, ABFA regulations in Ghana (while important) are both vague and fragmented across too many possible sectors and objectives, allowing for unproductive spending.<sup>208</sup>

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202 IFI representative 2, *op. cit.* See Mihalyi D & L Fernandez, *op. cit.* for detailed analysis of fiscal rules in resource-dependent countries.

203 *Ibid.*

204 Anti-corruption expert, *op. cit.*

205 IFI representative 1, *op. cit.*

206 *Ibid.*; Jefferis K, *op. cit.*

207 Jefferis K, *op. cit.*

208 Anaman P & J Darko, *op. cit.*

This paper proposes a focus on the third pillar of the SADC 4IR Declaration: skills and awareness, considering both SADC's strength as a regional convening power and its limitations in terms of resources and enforcement mechanisms

Overall, resisting a plethora of fiscal pressures in order to institute PFM reform within a national culture of low fiscal discipline is difficult. Success may depend on a resolute national leader willing to sacrifice short-term interests during his/her own presidency (and face much political difficulty in manoeuvring), for the long-term growth of the country.

## Policy takeaways

While the second and third sections of this paper provided a high-level overview of issues in SWF development and management, the subsequent two sections narrowed the scope to challenges facing four African countries. The following policy suggestions are broadly based on the latter challenges, observed specifically in the four case studies. These takeaways seek to target policymakers in African countries intending to establish SWFs, as well as to suggest policy adjustments for countries with existing funds.

- Before establishing an SWF, conduct a sober assessment of whether the fund's objectives are both necessary and feasible within the domestic context:
  - » isolate a specific problem that the SWF seeks to solve, and determine if an SWF is the most appropriate tool to solve it;
  - » weigh the costs and benefits of saving versus development to determine optimal amounts of net savings and spending. Further determine the most appropriate investment vehicle for savings (considering the country's risk-return preference), as well as the most appropriate mechanism for spending (these should not be limited to an SWF); and
  - » conduct a SWOT analysis of country-specific political and economic forces that may work against both optimal savings and spending mechanisms, and how they can or cannot be mitigated.
- When designing an SWF, prioritise the creation of strong institutional structures that increase the difficulty of misusing funds and/or political raiding:
  - » design a rules-based fund that minimises potential loopholes, limits the discretion of fund managers, and promotes transparency and accountability. Examples of



important rules include: clear deposit and withdrawal rules, a clear investment mandate, a strong investment risk management framework with internal and external oversight mechanisms, a code of conduct, procurement procedures, and public disclosure requirements;

- » keep stabilisation assets at low enough levels to avoid political incentives to siphon funds, given the liquidity of these assets; and
- » build flexibility into withdrawal rules for exceptional circumstances/emergencies (specifics are unique to the context of each country) to decrease incentives to bypass rules.

*\*If the above objective does not seem to be practically implementable owing to political pressures, this may be a sign that an SWF is not yet advisable, and funds should first be focused on debt repayment and/or immediate development needs*

- Build broad-based political support for a proposed SWF before its operationalisation:
  - » seek to establish coalitions of different interest groups in support of a fund, especially when operating in an environment with strong adverse political incentives. Examples might be opposition parties, private sector elites, labour unions, extraction companies, local branches of government, international watchdogs, etc.;
  - » ensure such interest groups have a role in official accountability mechanisms or fund governance structures; and
  - » emphasise the legitimacy dividends of an institutionally sound fund to politicians, ie, the benefits of lower risk premiums and crowding in external capital for visible projects, which can be credited to political parties.
- Develop a comprehensive plan for public sensitisation and expectation management before the concept is introduced to the public:
  - » provide extensive information on the fund, which will ensure informed public advocacy;
  - » as a part of this information provision, explain in detail what an SWF can feasibly achieve and why, the limitations and risks, as well as the long-term impact of appealing but ill-advised policy options that may be circulating among political parties or the public; and
  - » seek public/interest group inputs on fund objectives and structure in order to drive a sense of public ownership.

- Position an SWF as a component of a broader PFM plan from inception:
  - » garner buy-in for broader PFM reform by demonstrating the consequences and neutralising effects of spending, savings and monetary policies that are not coordinated;
  - » ensure that fiscal rules on borrowing and expenditure within the budget align with SWF rules;
  - » anticipate potential roadblocks to an effective SWF within the broader PFM reform plan, such as the implications of a currency peg, a non-independent central bank, etc.; and
  - » ensure independent resource reference price forecasts free from political involvement. Integrate buffers for unexpected commodity price crashes into projections.
  
- Ensure a strong national domestic investment policy alongside the establishment of any SWF (and potentially in place of a domestic fund):
  - » focus this policy on a manageable number (rather than a comprehensive list) of well-planned projects designed for the budget, and aligned with national development plans;
  - » assess national capacity to implement each project, and consider temporarily hiring international expertise or putting projects on hold if there are significant absorption constraints;
  - » focus on tightening processes within the project pipeline if there are loopholes, and attempt to institutionalise legal consequences for arbitrary and politically motivated changes to chosen projects; and
  - » approach special development funds with caution, prioritising the above reforms within the budget.

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## Cover image

An oil platform in Lagos Port Complex (port of Lagos), 2016, Lagos, Nigeria  
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