

A Critical Assessment of Aid Management and Donor Harmonisation



African Forum and Network
on Debt and Development

The Case of Mozambique

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African Forum and Network on Debt and Development

31 Atkinson Drive, Hillside,
PO Box CY1517, Causeway, Harare, Zimbabwe
Telephone 263 4 778531, 778536 Telefax 263 4 747878
E-Mail afrodad@afrodad.co.zw
Website: www.afrodad.org

About AFRODAD

AFRODAD Vision

AFRODAD aspires for an equitable and sustainable development process leading to a prosperous Africa.

AFRODAD Mission

To secure policies that will redress the African debt crisis based on a human rights value system.

AFRODAD Objectives include the following:

- 1 To enhance efficient and effective management and use of resources by African governments;
- 2 To secure a paradigm shift in the international socio-economic and political world order to a development process that addresses the needs and aspirations of the majority of the people in the world.
- 3 To facilitate dialogue between civil society and governments on issues related to Debt and development in Africa and elsewhere.

From the vision and the mission statements and from our objectives, it is clear that the Debt crisis, apart from being a political, economic and structural issue, has an intrinsic link to human rights. This forms the guiding philosophy for our work on Debt and the need to have African external debts cancelled for poverty eradication and attainment of social and economic justice. Furthermore, the principle of equity must of necessity apply and in this regard, responsibility of creditors and debtors in the debt crisis should be acknowledged and assumed by the parties. When this is not done, it is a reflection of failure of governance mechanisms at the global level that protect the interests of the weaker nations. The Transparent Arbitration mechanism proposed by AFRODAD as one way of dealing with the debt crisis finds a fundamental basis in this respect.

AFRODAD aspires for an African and global society that is just (equal access to and fair distribution of resources), respects human rights and promotes popular participation as a fundamental right of citizens (Arusha Declaration of 1980). In this light, African society should have the space in the global development arena to generate its own solutions, uphold good values that ensure that its development process is owned and driven by its people and not dominated by markets/profits and international financial institutions.

AFRODAD is governed by a Board of seven people from the five regions of Africa, namely East, Central, West, Southern and the North. The Board meets twice a year. The Secretariat, based in Harare, Zimbabwe, has a staff compliment of Seven programme and five support staff.

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Preface

Although donors argue that they have changed their approach and that conditionality has been replaced by 'country ownership', poverty reduction and pro-poor growth strategies, experience on the ground seems to suggest otherwise. Lack of harmonization and alignment of policies, procedures and programs among various donors' agencies continue to mar effective aid delivery to recipient governments who in turn have been eluded by the key concepts of inclusiveness, popular participation and 'good governance'.

Problems of economic governance and ineffective utilization of development assistance have ranged from poor or no consultation with the intended beneficiaries; lack of coordination between various government agencies, the failure to harmonize policies, programs and procedures harmonization and alignment, poor project design within parastatals, public or private enterprises; to poor monitoring of foreign funded projects and consequently in indebtedness and poverty..

This international agenda has evolved over time, and hopefully will continue to evolve. Its principal manifestation at this time is the Paris Declaration of March 2005. The Paris Declaration on Aid Effectiveness represents a landmark achievement for the international community, which brings together a number of key principles and commitments in a coherent way. It includes a framework for mutual accountability, and identifies a number of indicators for tracking progress on the part of donors and partner countries. At the same time, there is a general recognition that the Paris Declaration is a crucial component of a larger aid effectiveness agenda that could engage civil society actors in a more direct manner. The power of the Paris Declaration is its focus on a limited number of general principles for action. As such, the Paris Declaration is not intended to provide operational instructions for how to achieve specific development results. The Paris Declaration is therefore limited in terms of the stated purpose of aid effectiveness in that it does not, and cannot, by itself, tell us how to reduce poverty, improve democratic governance, or promote greater gender equality.

As development actors, CSOs share an interest in the concept of aid effectiveness as an important one for keeping development efforts on-track, for drawing attention to outcome and impact level results, and for drawing lessons of good practice from accumulated experience. The shared pursuit of aid effectiveness provides a legitimate entry point for dialogue among all development cooperation actors, including CSOs. This case study by AFRODAD is but one of the civil society contributions to monitoring and tracking Aid effectiveness in Sub-Saharan Africa, which by and large constitutes the bulk of aid beneficiaries. We do hope that the thoughts and ideas shared by this case study will help enlighten issues and move the continent and its development partners step a head.



Charles Mutasa
Executive Director

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List of Abbreviations

AfDB	African Development Bank
AFRODAD	African Forum and Network on Debt and Development
APRM	African Peer Review Mechanism
BdPES	Economic and Social Plan Report/ <i>Balanço do PES</i>
BoP	Balance of Payments
DAC	Development Assistance Committee (of OECD)
DBS	Direct Budget Support
DFID	United Kingdom Department for International Development
DNT	Treasury National Directorate
DPG	Development Partners Group
EC	European Commission
FAO	United Nations Food and Agriculture Organization
G-20	Group of Civil Society Organizations
GDP	Gross Domestic Product
GNP	Gross National Income
GoM	Government of Mozambique
HDI	Human Development Index
HIPC	Heavily Indebted Poor Country
HLF	High Level Forum
IMF	International Monetary Fund
MDGs	Millennium Development Goals
MEC	Ministry of Education and Culture
MINEC	Ministry of Foreign Affairs and Cooperation
MISAU	Ministry of Health
MoF	Ministry of Finance
MoU	Memorandum of Understanding
MPD	Ministry of Planning and Development
MTEF	Medium-Term Expenditure Framework
NGOs	Non-governmental Organization
ODA	Official Development Assistance
OE	State Budget/ <i>Orçamento do Estado</i>
OECD	Organization for Economic Cooperation and Development
PAF	Performance Assessment Framework
PAP	Programme Aid Partners / the G18
PARPA	Action Plan for the Reduction of Absolute Poverty

SDC	Swiss Development Cooperation
SIDA	Swedish International Development Cooperation Agency
SISTAFE	Integrated State Financial Administration System
SWAp	Sector Wide Approaches
UK	United Kingdom
UN	United Nations
UNDP	United Nations Development Programme
UNESCO	United Nations Education Science and Cultural Organization
UNFPA	United Nations Fund for Population
UNICEF	United Nations Children Fund
US\$	United States Dollar
USA	United States of America
WB	World Bank

1.0 Executive Summary

Mozambique is committed to the fight against poverty. The Government has adopted a number of well-articulated plans for poverty reduction and growth. These include Agenda 2025 (the national long term vision), which is the basis for the Five Year Programme (2005-2009) and the second generation of Action Plan for the Reduction of Absolute Poverty, (PARPA II, Mozambican PRSP II for the period 2006-2009). It has integrated the Millennium Declaration principles and the Development Goals into its national objectives.

International development assistance plays a crucial role in Mozambique's fight against poverty. The country's known reputation in various angles has made it a major destination of Official Development Assistance (ODA). Development partners have engaged in an ongoing and highly participatory dialogue in the context of PARPA. A group of 18 donors, known as 'G-18', currently provide budget support to Mozambique. It is premised on support for poverty eradication by: (a) Building a partnership based on frank and open dialogue on the content and progress of Mozambique's poverty reduction strategy, and (b) Providing financing for poverty reduction, clearly and transparently linked to performance, in a way which improves aid effectiveness and country ownership of the development process, reduces transaction costs, allows allocate efficiency in public spending, predictability of aid flows, increases the effectiveness of the state and public administration, improves monitoring and evaluation and strengthens domestic accountability.

Despite encouraging international resolutions that include the 2005 Paris Declaration on Aid effectiveness and the G8 Gleneagles commitment to increase aid to Africa research evidence continue to point to the fact that a number of obstacles associated with aid modality, management, donor accountability and harmonization still need to be tackled if Africa is to successfully fight poverty. In Mozambique, claims have been made to the fact that aid is often not aligned to national priorities and programmes, most notably the PRSP and recipient African governments have been left with little choice but to accept them. Conditionalities that do not derive from national programmes and not subject to wide consultation risk weak implementation and conflict. Different donor conditionalities also tend to conflict and to be excessively numerous rising from donor prescriptions rather than national consensus. Lastly conditionalities tend to vary widely and the lack of harmonization and lack of harmonization conflicts with national consensus.

The main focus of this research is to study the Mozambican aid architecture, examining how funds are transmitted to Mozambique and its impact on development efforts, how recipients and donors interact in such processes, how aid is coordinated at the country level, and how broad-based are the national planning processes and aid delivery mechanisms.

The main findings were:

- Although short term predictability of aid appear to have improved, mid to long run predictability has not.
- Donors have to harmonise and align more their internal procedures and planning systems with the demands of mutual accountability. From the review and consultations, it was obvious that many donors were not well familiar even with the matrix of their performance indicators.
- Although with many positive aspects, the apparent partnership between donors and government has been focused on procedures - how to do things - but little attention has been placed on actual directions, strategies and policies, and all requisites of the Paris Declaration.
- There is a need to improve government-donor data base and information system.
- There is a need to develop a wider and more accurate framework to identify and significantly reduce unnecessary administrative and transaction costs. Controlling the number of missions is effective in reducing them, sometimes quite dramatically, and this is also extended to donors' internal administrative burdens and transaction costs.

2.0 Introduction

From the beginning of the liberation war in 1964, Mozambique experienced nearly 30 years of violent strife, social and political disruption, and economic crisis. Under pressure of civil war, the infrastructure of governance disintegrated. In large parts of rural Mozambique, schools and health posts were destroyed and teachers and nurses evacuated.

The signature of the 1992 General Peace Accord, brought along a period of almost uninterrupted growth of around 8 percent per annum, making Mozambique one of Africa's most successful stories of post war reconstruction and economic reform. The country experienced its third peaceful and democratic general elections in December 2004, proving political stability and national reconciliation. These elections were accepted by the opposition, making it possible to anticipate political stability. These however, strengthened further the main political party, which brought alterations in governmental management. In the first mandate year, tight measures were undertaken to improve government's service delivery as well as efficiency aiming to put an end to illegal practices.

The proportion of people living below the national poverty line in Mozambique has significantly declined from 69.4 percent in 1997 to 54.1 percent in 2003 ; and there have been significant advances in relation to key indicators of human and social development, with a substantial decrease in the areas of child and maternal mortality and an increase in net enrolment rates.

Despite these achievements, the country is still one of the poorest countries in the world; with a Human Development Index (HDI) rank of 168 out of 177 countries . More than half of the population relies on the informal rural economy and income inequality is high . Gross Domestic Product (GDP) per capita is US\$ 313 (2004). Life expectancy at 41.6 years is among the lowest in Africa, partly due to the impact of HIV and AIDS - about 16.2 per cent in 2004 (Mozambique MDG Report 2005). The country's geographical location makes it prone to natural disasters such as severe droughts and floods. As with other South African countries, Mozambique is affected by global climate change altering rainfall patterns. In the first quarter of 2000 floods hit the southern and central Mozambique as heavy rains caused rivers banks to burst. Apart from an estimated 700 deaths, over 1m people were displaced and economic and social activities were seriously disrupted. Homes, factories and critical infrastructure were damaged or destroyed, constituting a major setback for the country and underlining it's vulnerable to climatic shocks.

The major obstacles to private sector development are source of financing (financing institutions almost inexistent in rural areas), red tape and infrastructure. Governance issues like, corruption, anti competitive practices, regulatory uncertainty and crime. On the financial side, the commercial banking sector dominates the financial system, accounting for more than 90 percent of the systems total assets; and almost all commercial banks in Mozambique are majority foreign-owned.

Mozambicans, however, are fully committed to the fight against poverty. The Government has adopted a number of well-articulated plans for poverty reduction and growth. These include Agenda 2025 (the national long term vision), which is the basis for the Five Year Programme (2005-2009) and the second generation of Action Plan for the Reduction of Absolute Poverty, (PARPA II, Mozambican PRSP II for the period 2006-2009). The PARPA II is based on the 2005-2009 government five-year programme and it has integrated the Millennium Declaration principles and the MDGs into its objectives. It clearly defines its strategy of economic growth and poverty reduction through three pillars: governance, human capital, and economic development.

International development assistance also plays a crucial role in Mozambique's fight against poverty. The country's known reputation in various angles has made it a major destination of Official Development Assistance (ODA). Development partners have engaged in an ongoing and highly participatory dialogue in the context of PARPA. A group of 18 donors, known as 'G-18', currently provide budget support to Mozambique. Government and the G18 have signed a Memorandum of Understanding (MoU) at the end of 2004, which sets out the principles, terms and operations for the Programme Aid Partnership (PAP).

This is one of the largest joint programmes in Africa, both in terms of volume and donor agencies involved. It is premised on support for poverty eradication by:

(a) Building a partnership based on frank and open dialogue on the content and progress of Mozambique's poverty reduction strategy, and (b) Providing financing for poverty reduction, clearly and transparently linked to performance, in a way which improves aid effectiveness and country ownership of the development process, reduces transaction costs, allows allocate efficiency in public spending, predictability of aid flows, increases the effectiveness of the state and public administration, improves monitoring and evaluation and strengthens domestic accountability.

The country's development plans in the immediate post independence year involved running up substantial foreign debt. When war and draught led to serious growth deterioration in the mid-1980s the debt load became unsustainable. The war also led to a high military debt to the Soviet Union. By 1998, Mozambique's total foreign debt, even after repeated rescheduling and write-offs by various bilateral creditors stood at 5.5 billion in normal terms. Complex negotiations resulted in the WB and the IMF declaring in April 1998 that Mozambique was eligible for debt relief under the Highly Indebted Poor Country, (HIPC) initiative. Since 1996, Mozambique has gone through two rounds of debt relief under the HIPC initiative, bringing its debt-to-exports ration down from 70 percent in 1997 to 131 percent in 2001. In June 1999, some US\$ 1.7 billion of Mozambique's debt was waived. After the floods, several creditors - including the US, UK, Finland, Spain and Portugal - agreed to suspend all or part of the debt payments to the country.

2.1 Background of the Study

As highlighted in the introductory section, Mozambique is a country with substantial leading factors, both from substantial progress and from the amount of challenges ahead. Aid appears to be a necessary factor to the country's development challenges. Aid is important and likely to become so, mainly because the incremental requirements to meet poverty reduction targets are unlikely to come from elsewhere. The G8 Summit in Gleneagles promised a quantum leap in levels of aid to Africa; and it appears to have been the culmination of a process initiated at the Millennium Summit in September 1999, which endorsed the Millennium Development Goals (MDGs). The landmark event in this process was the financing for Development Summit at Monterrey, Mexico in 2002, at which donor nations pledged to increase aid to 0.7 per cent of their Gross National Product (GNP).

The 1990s saw the emergence of new aid approaches as general budget support (GBS), sectoral budget support (SBS) and pool fund arrangements under the Sector-Wide approach (SWAp) - along with the Poverty Reduction Strategy Papers (PRSP) and the related institutional frameworks such as the Mid-term Expenditure Framework (MTEF). Their emergence is an attempt to overcome the weaknesses of existing aid modalities, typically "stand alone" projects and structural adjustment operations, especially in the sub-Saharan Africa context.

It is against this background that a research was conducted in Mozambique with the objectives of identifying stumbling blocks to effective aid delivery, donor practices that place the highest burdens on partner governments in terms of ownership, transaction costs, institutional capacity as well as identify possible benefits and opportunities to cost effective development assistance delivery. Mozambique has benefited substantially from development partners' support and has undergone macroeconomic reforms yet still had outstanding high levels of debt service and poverty.

2.2 The Various Conferences

In the past decades, there have been various world gatherings on development issues. We resume concisely the different international conferences shaping the new aid and funding environment. Further information can be found on the websites indicated herein.

2.2.1 The Millennium Development Summit (2000)

The Millennium Development Summit was held in September 2000, with a presence of 147 heads of State and Government, and 189 nations in total: all committed themselves to making the right to development a reality for everyone. To help track progress, the United Nations, as well as representatives of IMF, the World Bank and OECD defined a set of time-bound and measurable goals and targets. The MDG Goal number 8 is to develop a global partnership for development.

2.2.2 Conference on Financing for Development (2002)

The Monterrey Consensus was adopted on 22 March 2002. This was the first United Nations-hosted conference to address key financial and development issues with 50 Heads of State or Government, over 200 ministers as well as leaders from the private sector and civil society, and senior officials of all the major intergovernmental financial, trade, economic, and monetary organizations. The Conference succeeded in placing financing for development on the forefront of the global agenda. The conference highlights the need for a substantial increase in Official development assistance policies and practices and states that greater efforts are necessary in both donor and recipient countries to improve the effectiveness of official development assistance.

2.2.3 Rome High-Level Forum (2003) - Rome Declaration on Harmonisation

In February 2003, leaders of the major multilateral development banks and international and bilateral organizations, and donor and recipient country representatives gathered in Rome for the HLF. The HLF concluding statement, The Rome Declaration on Harmonization, sets out an ambitious program of activities: (i) ensure that harmonization efforts are adapted to the country context, and that donor assistance is aligned with the development recipient's priorities; (ii) expand country-led efforts to streamline donor procedures and practices; (iii) review and identify ways to adapt institutions' and countries' policies, procedures, and practices to facilitate harmonization; and (iv) implement the good practices principles and standards formulated by the development community as the foundation for harmonization.

2.2.4 The Paris High-Level Forum (2005) - Paris Declaration

The Paris HLF, in March, 2005 was attended by development officials and ministers from 91 countries, 26 donor organizations and partner countries, representatives of civil society organizations and the private sector. The participants took stock of progress that have taken place since the Rome HLF and identified the areas in which further work is needed. The participants at the Paris High-Level Forum issued the "Paris Declaration on Aid Effectiveness, " in which they committed their institutions and countries to continuing and increasing efforts in harmonization, alignment, and managing for results, and listed a set of monitorable actions and indicators to accelerate progress in these areas.

2.3 Problem Statement

The quality of aid is a function of both donor and recipient country policies and practices. While a lot of studies have focused on how recipient African countries have misused or misappropriated aid, little focus has been put on how donor behaviour has impacted on the quality and effectiveness of aid.

Despite encouraging international resolutions that include the 2005 Paris Declaration on Aid effectiveness and the G8 Gleneagles commitment to increase aid to Africa research evidence continue to point to the fact that a number of obstacles associated with aid modality, management, donor accountability and harmonization still need to be tackled if Africa is to successfully fight poverty.

Claims have been made to the fact that aid is often not aligned to national priorities and programmes, most notably the PRSP and recipient African governments have been left with little choice but to accept them. Conditionalities that do not derive from national programmes and not subject to wide consultation risk weak implementation and conflict. Different donor conditionalities also tend to conflict and to be excessively numerous rising from donor prescriptions rather than national consensus. Lastly conditionalities tend to vary widely and lack of harmonization and lack of harmonization conflicts with national consensus. As with the Mozambican case we will deepen our analysis towards understanding the underlying characteristics of development assistance in its various forms.

2.4 The Purpose of the Study

2.4.1 Overall Objective

The main focus of the project is to study and promote public dialogue within Africa concerning donor aid management and its impact on African countries' development efforts by examining how funds and knowledge are transmitted to recipient African countries, and how recipients and donors interact in such processes. In so doing there is need to unpack issues of how aid is been delivered and coordinated at country level (aid modalities) with particular focus on aid modalities (general budget support, sectoral budget support, and pool fund arrangements) and mutual accountability.

2.4.2 Specific Objectives to the Mozambique Case

- To assess the current salient aid facts (requirements and availabilities) and policies about the quality of aid and its effectiveness in the context of a possible large increase of aid to Mozambique.
- To recommend ways of making aid management and delivery effective to poverty reduction and development.
- To influence public policy makers and donor agencies to put in place national mechanisms of translating international donor commitments on Aid to the national levels.

2.5 Main Messages from the Country Case

There have been significant improvements in donor performance and aid management in Mozambique. In general, donors are committed to the Paris agenda: for example, the PAPs with their performance assessment framework (PAF), one of the major donor groupings in Africa, (now 18 donors), and accounts for more than 80 percent (both off and on-budget aid) of all aid inflows to Mozambique. Aid flows continue to increase steadily, and the total share of Aid to the country is very large and robust. Indeed this is at the core of the main policy for a, given the need for scaling up of aid to meet the MDGs on one hand, and the ownership and government leadership concerns implied with high donor dependence (with serious interference on domestic agenda) in the name of partnership, on the other. According to the respondents, the messages below arise from the country case:

- There is a need to strengthen and significantly increase the share of DBS and Program Aid to government. This will require: (i) an open discussion amongst donors to consolidate and develop the common understanding of the issues at stake; (ii) a clearer government position through its aid policy and strategy, about the portfolio composition and dynamics that better fit to the national context: Mozambique is yet to develop its Aid Strategy.
- Donor grouping and donor behaviour in Mozambique seems to have come a long way since the signature of the MoU between Government and donors, but it still lagging behind in some fundamental areas, such as the composition of the portfolio.
- Although short term predictability appear to have improved, mid to long run predictability has not. A combination of better, longer and rolling (or adjustable) multi-year programs, with a good and realistic MTEF and a systematic macroeconomic analysis of predictability of aid inflows.
- Donors have to harmonise and align more their internal procedures and planning systems with the demands of mutual accountability. From the review and consultations, it was obvious that many donors were not well familiar even with the matrix of their performance indicators.
- Although with many positive aspects, the apparent partnership between donors and government has been focused on procedures - how to do things - but little attention has been placed on actual directions, strategies and policies, and all requisites of the Paris Declaration.
- The government needs to have political space to reflect and decide on the best allocation of resources to create economic and social dynamics that are, gradually, more integrated and less dependent on donors charity.
- There is a need to improve government-donor data base and information system.
- There is a need to develop a wider and more accurate framework to identify and significantly reduce unnecessary administrative and transaction costs. Controlling the number of missions is effective in reducing them, sometimes quite dramatically, and this is also extended to donors' internal administrative burdens and transaction costs.

2.6 Aid Harmonization - Working Definitions

We start by defining "aid", which is the shorthand term for official development assistance (ODA). The term originates from the Development Assistance Committee (DAC) of the OECD, which is a grouping of mostly industrialised nations, thus, donors.

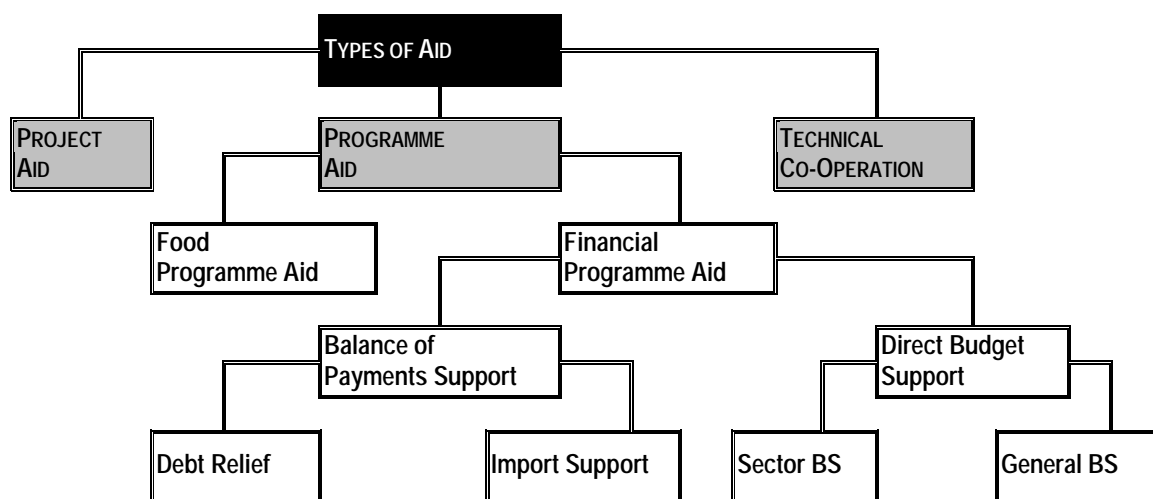
According to the DAC guidelines, a given foreign inflow will qualify as ODA if it fulfils the following three criteria:

- Aid has to be official. ODA are transfers from official sources (e.g. state/local governments and their executive agencies) to developing countries included in the DAC list of aid recipients. Therefore, money raised by non-governmental organisations (NGOs) is not included.
- It has to be used for development purposes. Hence it excludes military aid expenditure.
- It should represent assistance. Flows have to take either the form of grants or concessional loans.

However, the concept is not static. There have been recent pressures to include some types of military expenditure as ODA following the events of 9/11 and the increasing emphasis on security and terrorism. We now discuss the different types of "aid" (see table below). The first major classification results in the subdivision into projects, programme aid and technical co-operation.

- Project aid relates to the influx of external funding that is targeted to a specific project, for example, building a school/road or improving access to water. Thus it comprises activities primarily designed to augment the physical capital (infrastructure) of recipient countries. One of its common features is that it is normally off-budget.
- Programme aid - in contrast with previous form- is not earmarked to a particular activity, although donors make disbursements conditional upon policy reform by the recipient government. It includes, amongst others, budget and balance-of-payments (BoP) support, financing of capital goods and commodities, and sector programme assistance.
- Technical co-operation, also known as technical assistance (TA), is a broad term covering contributions to development mainly through the provision of advice and/or skills, in the form of specialist personnel, training and scholarship, grants for research and associated costs while the focus is the development of human capital.

Figure 1.6.1 The Different Types of Foreign Aid



Whereas project aid and technical assistance are rather straightforward, programme aid tends to be slightly more complex. The first distinction is between food programme aid and financial programme aid. The former, food programme aid, is associated with food commodities to support development projects; and it is different from emergency food assistance. On the other hand, financial programme aid is mainly composed of cash flows (foreign exchange) originating abroad with the aim of providing extra liquidity in a developing country, normally to correct Balance of Payment (BoP) imbalances. We further subdivide financial programme aid into two major blocks: Balance of payments support, and direct budget support.

- In Balance of Payments (BoP) support, aid is not used to finance specific projects or activities. It is normally associated with IMF loans to tackle BoP problems/deficits - for macroeconomic stabilisation purposes - where the money is deposited in Central Bank to supplement international reserves. Two distinct forms of BoP support are debt relief and import support. Aid financed Debt Relief, in the context of the Paris Club negotiations or HIPC initiative, is not tied to specific goods or services. It entails debt forgiveness or restructuring of either the principal or the servicing obligations (amortization and interest payments). It is considered BoP support since it saves foreign exchange - that would otherwise be used to service the debt - which can be used for other purposes (e.g. build a school). On the other hand, Import Support (or commodity aid) is a form of BoP support aimed at reducing the shortages of imported goods and increasing production capacity in the economy. Import support is still considered a currency instrument for BoP support, because it reduces the need of the recipient country to use foreign exchange for commercial imports.
- Direct Budget Support (DBS) is a modality of aid in which funds are provided directly to a government's budget, normally the Ministry of Finance (MoF). This cash envisages the support of a broad government programme that may include fostering economic growth, poverty reduction, fiscal adjustment, and strengthening institutions (e.g. budgetary processes). The government will spend these funds using its own financial management, procurement and accountability systems.

DBS can take the form of General Budget Support (GBS), which is a general contribution to the overall budget, or Sector Budget Support (SBS), when financial aid is to support development plans in specific sectors, i.e. earmarked to a discrete sector, with any conditionality relating to these sectors.

SBS is often provided in the context of a Sector Wide Approach (SWAp) - which is not an aid modality, but a process or method of working.

- Pooled Funding (or basket funding) is an example of sector earmarked support, whereby donors jointly fund an activity or institution through the establishment of a separate and designated financial arrangement (thus off-budget). There are a number of examples of pooled funding arrangements in Mozambique (e.g. for the importation of essential medicines).

Before turning to the advantages and disadvantages of each type of foreign aid, we ought to expand a bit more on stand-alone projects (project aid). In project aid, all planning, financing, accounting, delivery and monitoring is responsibility of the donor. However, this is a simplification. Decomposing the main category we have (i) project aid using government systems (bilateral agreements), (ii) project aid using parallel systems, and (iii) project aid through NGO/private providers. These forms have different impact on ownership and capacity building. Countries, however, will necessarily have a different portfolio/mix of aid modalities depending on both the features of the recipient country and donor preferences. In order to understand the allocation of resources to a developing country, we need to understand the intrinsic characteristics of each aid modality as outlined in the table below.

Table 2.6.1 Main Features of Different Types of Aid

Type of Aid	Accountability	Earmarking	Fungibility	Conditionality
Project Aid	Donor	Total / project	Limited	Limited
Tec. Co-operation	Donor/Govt	Total	Limited	None
BoP Support	None	None	Varies	Macro
Debt Relief	Govt systems	Usually none	Varies	Macro & budget
Budget Support	Govt systems	Varies	Very high	Varies
General BS	Govt systems	None or nominal	Completely	Macro & budget
Sectoral BS	Govt systems	On-budget to sector	Yes, unless in conditionality	Sectoral

Table 2.6.1 shows the main characteristics of each type of foreign aid. Given that the focus of the discussions on aid modalities is centred in the project aid versus programme aid dichotomy, the following assessment will mainly concentrate on those two broad categories.

In terms of the accountability (disbursement) criteria, the outcomes vary between donor and recipient governments. In the case of project aid, the accountability is often leaning to the donor (procurement and reporting requirements are normally those of the donor). This type of aid is often agreed on an ad-hoc basis (off-budget) and is highly donor-driven (the government/sector is often not consulted). However, the case of budget support favours government accountability systems in the sense that these flows are included in the state budget and are channelled through government mechanisms. Earmarking refers to the allocation of resources to a specific and previously agreed purpose.

When aid assumes the form of projects, the cash has a very specific target, which is the project itself. However, there are cases where earmarking is sectoral or even inexistent. For DBS no earmarking is considered. On the other hand, fungibility refers to possibility that donor resources are used to release funds for other activities that were not initially agreed - In most cases the money is disbursed using donor mechanisms (totally bypassing the government). In other forms of aid, namely budget support, the possibility of deviating funds from its original purposes increase.

Table 2.6.2 Advantages and Disadvantages of Each Aid Modality

Type of Aid	Accountability	Earmarking	Fungibility	Conditionality
Project Aid	Donor	Total / project	Limited	Limited
Tec. Co-operation	Donor/Govt	Total	Limited	None
BoP Support	None	None	Varies	Macro
Debt Relief	Govt systems	Usually none	Varies	Macro & budget
Budget Support	Govt systems	Varies	Very high	Varies
General BS	Govt systems	None or nominal	Completely	Macro & budget
Sectoral BS	Govt systems	On-budget to sector	Yes, unless in conditionality	Sectoral

The table above summarises the strengths and weaknesses of each aid modality. Both government and its partners seem to agree with what studies indicate, the increasing preference of budget support over project aid, given a certain set of circumstances pertaining Mozambique, a country not in war, corruption is reasonably low, with good macroeconomic performance.

3.0 The Case Of Mozambique

There are several aid modalities co-existing in Mozambique. The contributions (grants) to the national budget (as GBS) currently stand at \$188 million for 2004, plus \$60 million in concessional loans for BoP support by the World Bank. In general, aid to the country has been increasing; Net ODA to the country has doubled from 1990 to 2002, with substantial increases from bilateral ODA. Policy wise, it's clearly stated in the PARPA that although aid is important to assist in overcoming the country's challenges, aid dependency should be reduced, and other sources of financing the budget (including widening the revenue base) should be explored.

Table 3.1 illustrates the main harmonised arrangements and typology in Mozambique. As discussed in the previous sections, overall budget support seems to be increasingly dominant (more donors adhering to) and most preferred system by the government.

Table 3.1 Harmonised Arrangements in Mozambique

Sector	Type	Participants	Annual Amount
National Budget	Budget Support (GBS)	PAP and Observers	\$188 m
Central Bank	BoP Support	World Bank	\$60 m
Programa Nacional para Agricultura 2001-2005	Earmarked Programme Aid (SBS)	Denmark, EC, Ireland, Netherlands, Sweden, UK, USA, World Bank, Italy	\$23 m vs. \$40 m (budgeted)
Fundo de Apoio ao Sector da Educao	Earmarked Programme Aid (SBS)	AfDB, Austria, Canada, Denmark, EC, FAO, Finland, France, Germany, Ireland, Italy, Japan, Netherlands, Portugal, Spain, Sweden, UNESCO, UNFPA, UNICEF, UK, USA, World Bank	\$13 m
PROSAUDE (Fundo Comum Geral) – Programa Nacional de Sade	Earmarked Programme Aid (SBS)	Denmark, EC, Finland, Germany, Ireland, Netherlands, Switzerland, UK, UNICEF, UNDP, UNFPA, USA, World Bank	\$24 m
Global Fund for Aids Tuberculosis and Malaria	Global Fund		\$7 m
Common Fund for Medicines	Basket-funding		\$14 m
Provincial Common Fund	Basket-funding	Denmark, Ireland, Norway, Switzerland, EC	\$5 m
Total Aid 2003			\$1 billion

Source: Evaluation of General Budget Support: the case of Mozambique (2004)

3.1 Methodology

The study comprises two different, but related components. The first component consists of the review of the overall national and world literature on aid agenda and donor practices. The second component of the study consists on an evidence and perceptions assessment made through individual interviews with the selected persons from donor agencies, government bodies, and civil society organizations. The questions and issues raised are based on the AFRODAD's project terms of reference (a list of persons interviewed are attached to this report). The consultant would like to thank, with appreciation, the collaboration and support provided by all involved parties, without which this study could not have been conducted successfully.

3.2 The National Development Framework

The Governments poverty reduction objectives, targets and strategies are articulated in a series of policy instruments.

Above all, there is a country long-term vision, known as the Agenda 2025 to which, a Government's Five-year Programme is anchored. This framework provides the set of guidelines and mid-term development objectives that constitute a broad, platform for other policy statements. This Five Year Programme is operationalised by the Action Plan for the Reduction of Absolute Poverty (PARPA, a Portuguese acronym for PRSP). The first PARPA run from 2001 to 2005, and in 2006, PARPA II was approved for the period 2006-2009. The PARPA specifies and prioritises the pillar and sectoral actions to be undertaken at different levels with the aim of reducing the incidence of absolute poverty. PARPA incorporates various components of national policies and strategies, and where sectoral programmes exist, it also provides clear links between these policies and programmes in the context of a comprehensive poverty reduction strategy.

PARPA Short term operational instruments, the Economic and Social Plans (PES), and their reports called the Balanço do PES, (BdPES). The State Budget(OE) is based to a large extent on the PES and provides a more detailed view of how the Government intends to collect, allocate and redistribute its resources in pursuit of the objectives set out in the above document. The State Budget is complemented by the rolling Triennial Public Investment Programme (setting out the Government's investment programme) and the recently introduced a MTEF setting a 4-year scenario of revenues as well as current and investment expenditures.

3.3 Country Ownership - Systemic Procedural Issues

The Government of Mozambique (GoM) has been taking action to strengthen its leadership role in coordinating development assistance. Currently there is an on-going process of developing an Aid and Cooperation Policy along with its strategy. While the Ministry of Foreign Affairs and Cooperation (MINEC) is formally in charge of coordinating development assistance, the Ministry of Planning and Development (MPD) is responsible for day-to-day coordination within the PARPA. An ODA database has been adopted by most external partners in 2006 is being handed over to the Government.

External partners' move towards budget support has also contributed to establishing a formal structure for regular government-development partner dialogue. The MPD National Director and the chair of the PAP co-chair a joint steering committee which meets monthly to discuss budget support issues. This committee includes the Troika plus group, consisting of the previous, present and future chairs of the PAP, plus the EC and the World Bank. An economist working group, a PAF coordination group and sector working groups (about 22), chaired by development partners, meet regularly and ensure regular dialogue with central and line ministries. The World Bank and UNDP have been co-chairing the Development Partners Group (DPG), a wider external partners group, beyond the PAP. MPD co-chairs Joint and Mid-Year Government-Donor Reviews to assess PARPA implementation; and GoM has chosen the Joint and Mid-Year Reviews as the main instrument to garner external partner support, replacing the traditional pledging approach of Consultative Group (CG) meetings. The last CG meeting was held in Paris in October 2003 and was chaired by the World Bank.

Both Government and donor representatives share the idea that positive steps have been taken to strengthen fiduciary. For example, the Government prepares an annual report on fiduciary risk for the group of external partners providing budget support, the PAP. The rollout of the Integrated Financial Management System (SISTAFE), which was introduced in 2004, is contributing to improving reliability of budget transactions. However, not all transactions are being processed through SISTAFE, and there are still some shortfalls and overruns in the execution of the budget. SISTAFE is currently used by the ministries of Finance, Education and Planning.

There is also some action to strengthen internal and external audit capacity; the country's Supreme Audit institution, known as Tribunal Administrativo enjoys a reputation of being largely independent. It is also responsible for reviewing the application of external funds provided to the Government. However, similar to the rest of the justice system, the Tribunal Administrativo struggles to fulfill its mandate under severe capacity constraints. Performance audits are relatively new in Mozambique. In 2006, the Inspeccao Geral das Financas under the Ministry of Finance initiated performance audits of external funds in selected sectors, including justice. There is a procurement complaint mechanism which, however, has made limited progress in promoting transparency, confidence and timely resolution of complaints. Procurement practices are expected to improve following the approval of a new Procurement Code in 2005. Mozambique ranks 99th of 163 in Transparency International's 2006 Corruption Perceptions Index; in a range from 0 (highly corrupt) to 10 (highly clean), it receives a score of 2.8. An Anti-Corruption Law was approved in 2004, and a Central Anti-Corruption Agency was also established.

3.4 Financial Management and Accountability

The first Public Financial Management Assessment (PFM) using a Standardized Assessment approach was conducted in Mozambique in 2004, mainly led by donors. In early 2006, an assessment of PFM based on the PEFA methodology was concluded and its findings and recommendations were discussed between government and the PAPs, and a workshop was carried out within government for discussion of the recommendations and prioritization of future actions. According with the PEFA methodology, such PFM assessments should be carried out within a 3-5 years interval. On the other hand, as defined in the MoU between GoM and PAPs, an annual report on fiduciary risk assessment within PFM should be done by or with GoM.

At the Joint Review in April 2006, GoM and PAPs agreed to give a flexible interpretation to the MoU stipulation for the annual Fiduciary Risk Assessment, and that is more appropriate to perform a full and comprehensive PFM Assessment every two or three years. The next full exercises are foreseen for end 2007 and for 2010. Additionally, it was agreed that for the Joint Review 2007, the assessment of PFM will be based on the regular follow-up of the related PAF/strategic matrix indicators and on other relevant available analytical inputs. This agreed process is also compatible with the 2006 PEFA-based assessment recommendation that in order to feed into the yearly joint review processes, a reduced assessment should be carried out on an annual basis in years between full assessments.

The Joint Review is the annual culmination of a continuous dialogue between GoM and donors on the progress of government performance against its main objectives for sustainable development and poverty reduction. The dialogue is structured around working groups, where five sub-groups represent the PFM area: budget analysis, SISTAFE, tax reform, procurement and internal and external audit. By covering the broad area of integrated financial management information systems, the SISTAFE group is particular amongst those 5, for covering the broad area of critical reforms and therefore a particular role in the overall view and integration of reforms. Additionally, the link with Public Sector Reform (including decentralisation) groups, as well as links with sectoral services groups is important for a wide transversal view of main challenges of financial management.

3.5 Monitoring and Evaluation

A country-level monitoring and evaluation system is emerging. PARPA II M&E systems have been integrated into existing Government mechanisms to avoid multiple reports. Significant improvements have been achieved in 2005 in terms of strengthening the semi-annual and annual BdPES, which is the main monitoring tool for all Government activities. The BdPES tracks progress in PARPA II and PARPA implementation and reports on progress toward achieving the MDGs. The financial execution of PARPA II and PARPA priority programs is tracked through quarterly budget execution reports prepared by the Government.

However, sector ministries' M&E systems need to be better linked to PES indicators; they also need strengthening to provide timely and relevant information to inform the PES Report. In an attempt to address this issue, the PARPA II Strategic Matrix incorporates indicators and targets included in the M&E matrices accompanying sectoral papers prepared by the Working Groups which prepared the PARPA II. Baselines for PARPA targets have been updated to reflect new information collected during the implementation of the PARPA. There have been some improvements in the harmonization of sector and provincial monitoring systems with BdPES preparation.

3.6 Mutual Accountability

The Government and its partners have established an effective development partnership based on mutual commitment and open dialogue on the content and progress of the PARPA, the MDGs, the MTFF, the PES and the budget. The PAF provides the basis for assessing Government and external partner performance. For example, each year, PAP partners agree on an updated PAF. All performance assessments are undertaken jointly by the Government and PAP partners. Annual Joint Reviews are undertaken following the production of the BdPES and focus on reaching a joint view on performance as a basis for aid commitments. Mid-Year Reviews are undertaken prior to submission of the PES and the budget to the Assembly of the Republic.

Annual PAP Performance Assessment Scoring rates PAP partners in relation to the Paris Declaration Targets. Since 2004, PAP partners have supported annual independent aid assessments, based on the PAF indicators, conducted by national and international consultants. The country has signed the Paris Declaration on Aid Effectiveness, and it also participates in the African Peer Review Mechanism (APRM) to help ensure that policies and practices conform to the principles of the Declaration on Democracy, Political, Economic and Corporate Governance.

4.0 Towards Budget Support Mechanism

4.1 Joint Missions and Analytical Partnership

Mozambique external partners increasingly conduct analytic work jointly. The PAP Economists Working Group is responsible for coordinating joint analytical work underpinning dialogue with the Government in the areas of public financial management, economic and financial governance, and the link between growth and poverty reduction. In 2004, several external partners, engaged in joint analysis with the Government and among each other. Also, the Government, in partnership with other donors, conducted a Public Expenditure Review, which was undertaken in two phases in 2001 and in 2003. In 2004, the Government, in partnership with the World Bank, Denmark and SIDA, also finalized a Legal and Judicial Assessment. External partners have posted 36 documents on the Country Analytic Work website as of October 2006. External partners are increasingly undertaking missions jointly, building on joint budget support and SWAps. In addition to the mandatory Joint Review and Mid-Year Review, the Programme Aid Partners (PAP) group undertook other missions in 2005, some of them were undertaken jointly while others.

4.2 Partners' Assistance Strategy Alignment

External partners have aligned their assistance strategies with national priorities as outlined in the PARPA and the PES, building strongly on joint budget support. The five major external partners are the World Bank, the EC, the USA, Denmark and the UK, accounting for approximately 67 percent of gross ODA in 2003-04. Net ODA accounted for 23.6 percent of GNI in 2004. Assistance provided by the PAP group, is aligned with the PARPA through a Performance Assessment Framework (PAF), a multi-year matrix of actions associated with budget support. The 2006 PAF is aligned with the PARPA II Strategic Matrix and the PES and was jointly agreed by the Government, external partners and national stakeholders through the work of the Quality Control Group. External partners are discussing the development of a joint assistance strategy. Its terms, composition and timeline are still under discussion.

4.3 External vs. Domestic Accountability Mechanisms

As discussed in previous sections, Mozambique still suffers from some distortions in domestic accountability due to partly heavy reliance on external assistance, to the fragmentation of instruments used by donors, and to the extent of donor involvement in central policy processes, including the poverty reduction strategy and the budget. Donors are among the main 'consumers' of budget and poverty reduction reporting information, and donor-government Joint Reviews have become a major arena for performance reviews and (more limitedly) policy debates. Despite the side-effects that these processes are having on domestic accountability, there is a question of sustainability of the stronger central mechanisms that are being put in place. Their 'institutionalization' will still take a few years, and during such period much of the burden for making sure that they continue to be strengthened will fall onto a small circle of government and donor officials, with a risk that a political crisis, such as a major instance of corruption, or a shift in donor priorities decided at headquarters level might undermine the whole process.

On another dimension, actors were until recently largely absent from these debates, The increasing transparency and availability of information also bodes well for an enhanced role of media scrutiny over budget formulation and implementation, further strengthening domestic accountability mechanisms.

In order to ensure effective implementation of PARPA, the GoM has developed and introduced a national System of Monitoring and Evaluation. Along with this system, comprehensive mechanisms of participatory poverty assessments were also introduced both at national and provincial levels. Of particular importance in this perspective is the poverty observatory (PO), in some cases referred to as development observatory. The PO is a participatory forum that includes government, civil society, and cooperation partners. There is a central PO and provincial POs. Within the framework of the POs, monitoring and evaluation of the performance of public and private entities in respect to poverty reduction takes place, and main recommendations from this forum are taken on board, in some cases even reflected in the future plans and implementation processes. Civil society therefore has an increasingly recognized venue to participate in the policy dialogue. Worries however, are that with the already known limited capacities of the civil society organizations (CSOs), coupled with strong donor presence and dependence, one does face situations of accountability bias.

Also at the central level, the GoM-G18 DBS donor group operational framework, the PAF along with its joint reviews, seems to be more visible than the PO, thus sending perceptions that GoM is more accountable to its donors, especially the PAP, than to its people: the Governance Dilemma!

4.4 Predictability of Donor Assistance

As noted in previous sections, budget support mechanism in Mozambique is aligned with the country's annual budgetary framework. The PARPA and PES review precede the annual Joint Reviews on the updated PAF matrix. This allows all parties to review past progress and make indicative commitments on the basis of actual outcomes in the previous fiscal year. PAPs make their commitments within four weeks from the end of the annual Joint Review, confirming them by the end of August, in time for the preparation of the budget. In 2005, two-thirds of disbursements occurred in the first two quarters of the fiscal year.

At the sector level, SWApS are also helping the Government and external partners align commitments with the annual budgetary framework. In 2005, for example, commitments to an Education Sector Support Fund supporting the education SWAp were made before June 2005, so that they could be reflected in the budget presented to the Assembly of the Republic. The sequence and timing of existing SWAp review processes has been aligned with the annual PARPA and PES review process, about two months after the end of the fiscal year, namely in late February or early March, thus allowing results from the previous fiscal year to inform these reviews. Efforts have also been made to include project financing in the budget. The Government and external partners have established an off-budget task force to bring off-budget funds, including external financing, on budget. Table 6.1 below illustrates an analysis of the disbursement schedule along with a predictability indication.

Table 4.4.1 Analysis of group disbursement schedule and predictability (2005)

	2005 Quarters				Total (US\$ m)
	I	II	III	IV	
Number of PAPs disbursing in the quarter	8	4	2	3	-
Cumulative number	8	12	14	17	-
% of DBS+BoPS disbursed in the quarter	39	24	29	8	-
Cumulative %	39	63	92	100	-
Total committed and confirmed (US\$ million)	82.4	77.8	80.3	38.3	240.5
Total disbursed (US\$ million)	111	67.9	29.2	78.9	287.0
Balance (Disbursed – Committed) (US\$ million)	28.6	-9.9	-51.1	40.51	8.11

The tables above confirm that predictability is improving. In the 2004, two thirds of the disbursements took place in the last two quarters (and many donors waited until the World Bank disbursed in September/October 2004 to disburse their own funds). By contrast, in 2005 two thirds of the disbursements occurred in the first two quarters and almost 40 percent actually occurred in the first quarter. It is also significant that 12 of the then 17 PAPs disbursed in the first two quarters, and half of the PAPs did so in the first quarter of 2005. Although only 13 of the PAPs had clearly defined disbursement schedules, 12 of those 13 disbursed as agreed. Furthermore, in 2004 there was a disbursement deficit (disbursement - commitment) of -13.8 million US\$, whereas in 2005 disbursements exceeded commitments by US\$ 8.1 million.

Despite these significant improvements, there are still many challenges ahead for the PAPs to consider. First, there were four donors that did not meet the commitment about the period to inform the GoM and confirm disbursement schedules for the following. Second, almost 30 percent of the donors did not disburse according to schedule, and one of them disbursed six month later. Third, mid to long term predictability is seriously affected by the fact that almost all donors are still working on a 2-3 year, fixed (not rolling) program, and half of those with such programs do not have confirmed commitments for Year n+1 until the Joint Review or Year n takes place - which means that predictability is, at most, of one year only. Mid to long term predictability decreases fast over the duration of the fixed, multi-year program.

These problems are exacerbated by the fact that two thirds of the PAPs end their programs around the same year, meaning that at some point there is near zero mid term predictability for more than two thirds of the aid portfolio.

4.5 Predictability in Budget Implementation

The Public Expenditure Review carried out by the World Bank in collaboration with the Government in 2002-2003 notes that 'overall, the existing system in Mozambique provides for good aggregate control of expenditures within years. There have not been significant over-runs of expenditures, and there is no apparent problem of expenditure arrears. The system suffers, however, from major weaknesses that hinder efficiency and transparency in the use of public funds' (World Bank 2003:53). A broader analysis carried out by Hodges and Tibana (2005) compares projected and executed expenditure in the PARPA priority sectors, finding great discrepancies. In general, three main factors shape the lack of predictability in budget implementation:

- Parliament grants the Minister of Finance of discretion in re-allocating budget resources along the course of the year, both between lines and between different government institutions. While this is seen as a necessary measure of flexibility to respond to changing circumstances, it also undermines the credibility of the budget, for two reasons. Firstly, it provides an incentive for sector ministries and other budget entities not to take the budget formulation process too seriously, knowing that there is a high degree of flexibility during implementation. Secondly, it provides the Ministry of Finance with the opportunity of significantly modifying budget composition during the course of the year without having to seek further parliamentary approval.
- The current system for budget disbursements is based on an advance payment mechanism, which requires budget entities to report on expenditure and ask for replenishment on a monthly basis. This out-dated system, bound to be replaced within the broader SISTAFE reforms, has always caused inflexibility and delays in funds transfers, preventing budget entities from managing their budget allocations more effectively. Liquidity constraints and delays in the submission and processing of accounts have compounded this problem, affecting rates of budget implementation.
- Further limitations are imposed by the existence of large 'off-budget' expenditure, in the form of donor-financed projects or of own revenues directly retained by spending agencies. A substantial part of investment expenditure is externally financed, as can be expected in an aid-dependent country like Mozambique. Much of this expenditure is either (i) off-budget in programming, meaning it never gets included in the OE, (ii) off budget in execution, meaning funds are not channeled through the public Treasury, or (iii) off-budget in accounting, meaning expenditure is not recorded in budget reports .
- These three factors highlight the difficulties that exist in ensuring a better integration of planning and budgeting, and a budget implementation process that has concrete linkages with the policies and objectives stated in medium-term and annual plans. As can be drawn from the above 6 Article 9 of the annual Budget Law has been determining the powers of the Minister of Finance on budget reallocations. While reallocations within broad economic categories are usually interpreted as a signal of managerial flexibility, large reallocations between administrative units are considered as poor budgeting practice, unless duly sanctioned by parliamentary approval.

4.6 Sector Assistance

An issue of particular interest in aid management in Mozambique relates to donor preferences and appetites. Although this is often linked to the principles of the Paris Declaration, one notes some sectors being 'more assisted than others'. As per PARPA priority focus, the education and health sectors, appear to be donor sectors... For example, in 2006, 69% of the health sector funding came from donors. In addition, the sector has three donor financed common funds: (i) PROSAUDE (the largest with about 47% of the total amount of common funds), (ii) Common Fund for Medicines (FCM), and (iii) Provincial Common Fund (FCP). The first one is financed by 10 donors, and 97% of the fund is financed by 6 donors alone: the Global Fund (HIV/AIDS, TBC and Malaria), which provide 50% of the finance; DFID, Flemish Cooperation, CIDA, The Netherlands and the EU (approximately 47%). The remaining four (AFD, DANIDA, SDC and UNFPA) provide 3% of the funds.

The Common Fund for Medicines (approximately US\$ 31.8 million in 2006) is not recorded on budget and the funds are not managed by the Treasury. Its finances are allocated to finance imports of basic medicines and other small, basic equipment. In 2006, non-earmarked funds finance approximately 80% of the fund, the EU provides 14% of the funds, and AFD provides 4%. Together, DANIDA and SDC provide 2% of the funds. Two donors have moved out of this fund: DFID, which has increased its contribution to PROSAUDE, and Finland, which has joined the non-earmarked funds.

The Provincial Common Fund (FCP) (approximately US\$ 20 million) is not recorded on budget, although its funds are managed through the Provincial Directorates for Planning and Finance only as management agencies. The major contributors to the FCP are non-earmarked funds (approximately US\$ 10.7 million in 2006, the equivalent to 1/3 of the non-earmarked funds and 54% of the FCP) and six donors (SDC, AECI, EU, DANIDA, Catalunya and AFD), which contribute to about 40% of the fund. Together, DANIDA and Catalunya contribute with less than 5% of the funds.

The non-earmarked funds (approximately US\$ 35 million in 2006) resulted from a decision of three donors (Norway and Ireland from 2005, and Finland from 2006) to provide finance not-earmarked to any of the three common funds that the GoM could use to cover any gaps across the other funds, according to GoM own allocative priorities.

Relative to 2005, in 2006 the amounts available directly to each of the common funds (PROSAUDE, FCM and FCP) were significantly reduced: FCM funds fell by 37%, PROSAUDE fell by 26% and FCP fell by 22%. However, on the whole overall financing to the common funds only fell by 7% (a much lower rate than what we would expect given the magnitude of the decline in finances available to the each of the common funds). The chief reason for this difference of magnitude is the availability of non-earmarked funds.

On the whole, 16 donors contribute to the common funds in the health sector. Of these; four donors (Ireland, SIDA Global Fund, Norway and the EU) provide 54% of the funds available to the common funds; while seven (AFD, CIDA, Finland, Global Fund - Malaria, TBC - The Netherlands, SDC and DFID) provide 39% of the funds; and five donors provide the remaining 7% of the funds.

4.7 Country-led Partnership

In general terms, the instruments utilized at central level for reporting to donors are the same ones that are used for domestic accountability purposes. Budget support donors, in collaboration with the Breton Woods institutions, have been working with the government to improve the quality and content of the REOs and the BdPES, in order to ensure that they can satisfy both internal and external reporting requirements at the same time. While this has been an important result obtained by the government, who insisted from the beginning of the PRS process on not duplicating existing efforts, consultations indicate that this has come at the cost of a heavy administrative burden on an already overstretched civil service. Both Government and Civil Society respondents feel that the joint review process, set up to provide a forum for policy dialogue around GBS, complementing existing domestic reporting processes to Parliament, is a complex exercise involving more than twenty working groups, which takes a heavy toll on the time and capacity of government officials.

There are also a number of separate reporting procedures still in place at sectoral level and for externally financed projects which do not flow through the budget system. As we saw before, this situation still provides distorted incentives in terms of ensuring full government ownership of existing programs and budgets. This is also true for local governments which receive substantial donor support directly at local level, which in some cases constitutes a large part of resources available at local level. The current situation therefore sees weak internal government capacity being stretched to serve a number of accountability 'audiences': GBS donors (increasingly involving civil society actors) through the joint review process, Parliament through the regular reporting processes involving the BdPES and the state accounts, and sector-specific processes and reviews in sectors where SWApS exist.

Over the past few years there has been a gradual move towards more integrated systems, thanks to ongoing budget reforms and to a gradual shift in donor assistance to direct budget support, which has started addressing the problems of fragmentation generated by the sectoral focus of aid. The signature of the MoU with the G-18 donors, and increasing efforts at bringing more aid 'on-budget' are likely to further strengthen such integration. Some observers argue that this process has mostly been donor-driven, and has allowed donors increasing access and control in the inner sphere of government decision-making.

At the same time, such processes have proved instrumental in strengthening domestic accountability, for example with regard to the role played by the Tribunal Administrativo, to increasing transparency and access to budget information, and to its comprehensiveness and coverage.

4.8 Results Orientation

The advent of SWApS in Mozambique has helped streamline implementation arrangements. For example, external partners support the health Swap, known as PROSAUDE, through three basket funds, including a general fund and two funds covering programs for the provinces and for pharmaceutical supplies, which channel between a third and a half of all external assistance to the health sector. Each fund is governed by a separate MoU. Partners also support the education SWAp through the Education Sector Support Fund; they rely on joint reporting and monitoring. External partners also follow joint financial management, reporting and monitoring systems to support agriculture SWAp.

Since 2000, the Government and external partners have taken action to better tailor capacity building to country needs through SWApS. This approach has contributed to reducing fragmentation of capacity building efforts. Government and its external partners are also taking action to strengthen coherence and coordination for public sector capacity support. Challenges ahead include the need to forge stronger links across sector capacity development programs. PAPs provide approximately thirty percent of their assistance through the regular budget, thus relying on country systems. The PAF monitoring process seeks to rely to the extent possible on line ministries' and decentralized government levels' monitoring and evaluation systems to track progress in implementing the PARPA, while efforts are being made to strengthen these systems.

The provision of DBS is considered to be aligned with the Government's PFM systems, and there has been considerable progress in aligning the flow of funds in the sectors with the planning, budgetary, reporting and auditing procedures of the government. However, the weight of project aid remains worrisome, requiring the use of separate cycles and management systems. Most bilateral projects and programmes are still using almost exclusively non-national rules for procurement, with the exception of a small number of sector common funds. GBS does use government procurement systems. In general, parallel implementation units are found across a range of sectors to implement stand alone projects; they are the established practice of a small number of external partners. Some external partners have already taken steps to integrate these units into Government structures.

5.0 Conclusions and Recommendations

A considerable effort has been made to align the flows of aid and the mechanism of aid management with the general planning and budget cycles. The weight of project aid is still huge and dominant and in some sectors (such as Health and Agriculture) it is increasing. Of course, project aid requires its own cycles and managing systems related to the nature of the projects, which are not necessarily aligned with government financial cycles and procedures. The difficulty to change from projects to SWAPs may be related to different problems: institutionalized entrenched interest (of different agencies, donor and GoM alike); sector limited capacities to manage a SWAP; and/or nature of the activities to be financed that may be more efficiently managed as projects (as are some of the cases in large infra-structure projects such as in roads and water).

Sector aid is still strongly characterized by off budget project aid and unpredictable flows of aid (with exclusion of Education). This means that while progress has been achieved with respect to harmonization and alignment at sector level, a lot more needs to be done. Sector coordinating groups need to become better organized and to play a bigger coordinating and peer pressure role.

Many donors that are part of the PAPs group and do budget support at central level still prefer project support at sector level. Donor strategies with respect to the aid portfolio are not well understood yet, but they clearly define the possibilities for greater harmonization, alignment and budget support.

Donor preferences and sector aid flows have the potential to pervert some of the government priorities. There is a clear difference between the structure of central government budget allocation and aid allocation, particularly when off budget aid flows are included. This means that off budgets have the potential to change the hierarchy of approved priorities. The Education and Health sector cases are a good example of this.

There are strong capacity constraints at sector level that affect the quality of policy development and analysis, planning, costing, budgeting, implementation and M&E. It is important to consider that lack of harmonization and alignment worsens the constraints on capacity; and more consistent progress and on harmonization and alignment help the development of capacities and reduce the strain on existing scarce capacities. Hence, although capacity constraints shape the real possibilities for the harmonization and alignment process to develop further and faster, such constraints can only be properly and systematically addressed within the process of improving harmonization and alignment.

There are a few issues that donors, GoM and other stakeholders need to think about and address in a very clear manner. These are:

- Optimum number of donors in a sector: Large number of donors in some sectors may be a source of inefficiencies, competition, etc. Delegated cooperation and exit strategies seem to be an option for situations alike. It would be important to understand the reasons behind each donor's choices and the engine behind the changes that are happening.
- Public finance and planning issues need to move to the top of the sectors agendas, particularly in areas like analysis of portfolio composition, predictability and moving from off budget to on budget. Each sector, according to its specific circumstances, needs to devise a strategy and plan and set specific commitments to change the current situation dominated by projects, off budgets, many common funds. One first step could be to prevent new funds from being created (hence, new donors and new money should go into existing funds, particularly those that directly support and complement the state budget; and guaranteeing that all new money accruing to the sector should go into sector budget support (with exception of cases that are well justified, such as some large construction works, for example). GoM could set performance targets for state, provincial and local government is whether targets are met within the new funds stiele relevant? What are the implications of transactions cost of aid delivery?
- MoUs should be consolidated and sectors may need to share their experiences and information more actively, regarding the principles and rules adopted and the behavior of GoM and donors in different sectors. From the interviews, it is clear that some donors do not behave consistently in the same manner in all sectors, and often this has little to do with the sector idiosyncrasies and more to do with donor strategies.

The experience of the Education, Health and Agricultural sectors (working together to improve their sector MoUs and align them with the MoU for GBS) is an interesting one that may be important to extend to other sectors.

- The issue of technical assistance and, more generally, of capacity development support, needs to be looked at very seriously. Sectors need not only better planning and more resources, but also more, better organized and motivated policy, implementation and monitoring capacities. These capacities cannot be fully utilized and developed outside a clear public finance planning and management framework; and this framework cannot be implemented and positively affect the development of the sector without such policy, implementation and monitoring framework.
- Insist on not duplicating reporting mechanisms this relates to transaction costs, but rather focus on improving existing ones. The early adoption of the REOs and BdPES as donor reporting instruments for GBS related to PRS implementation contributed to the strengthening of domestic processes and promoted integration.
- The pros and cons of different aid modalities, including their side effects on incentives for integration and fragmentation are a fundamental factor in shaping how a country manages to gradually strengthen its budget and PRS processes and instruments. It would be recommended to build the right linkages from the start, for example by correcting incentives generated by a strong sector-focus by donors, or by not allowing 'off-budget' funding to persist.
- There has not been a thorough estimation of the transaction costs associated with the new aid environment in Mozambique. However, there is mounting evidence that aid management and donor harmonisation processes are ever challenging concerns that require delicate attention.

Coherent, comprehensive arrangements for policy dialogue with donors are very important, especially in an aid-dependent country like Mozambique. When the government takes the lead, and donors collaborate constructively, incentives can shift dramatically in a limited timeframe.

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Annex 1 Detailed Methodology

The study is based on the assessments of the recent past and current situation of aid and donor behaviour in Mozambique. A comprehensive review of the literature was undertaken prior to the meetings and interviews with donor representatives and key government officials and the representatives of civil society organizations. As per initial terms of reference, the study was estimated to take place between mid December and mid January. Reality, however, has shown that in this period, most of the government and donor agencies are either closed or their representatives are on holiday.

Under these circumstances, the consultant proceeded with desk review based on the readily available documents and other sources of information while awaiting partner's arrival or back into the offices. The meetings and the interviews were then made possible basically from the second week on January 2007. The main issues addressed in the meetings were based on the detailed terms of reference presented below in the annexes.

The inputs collected from the meetings were then consolidated and cross-checked with the available literature on aid and donor behaviour in the country. Similar exercise was carried out on a reverse manner: and several reviews were taken to ensure that the report critically addresses the issues as presented in the terms of reference. Finally, the consultant debriefed the preliminary findings of the study to government officials and received comments, with which he improved the report presented herein.

Annex 2 PAPs Share Per Aid Item 2005 (in % of the group total)

	DBS	Sector Aid	Program Aid	Project Aid	Aid to GoM	Total Aid
Belgium	0.91	0.51	0.72	0.00	0.43	0.53
Canada	0.69	5.54	2.98	2.47	2.77	3.00
Denmark	3.58	15.51	9.21	0.41	5.63	5.66
EC	19.84	14.86	17.49	12.35	15.40	15.59
Finland	1.81	2.96	2.35	2.76	2.52	2.57
France	1.36	1.60	1.47	3.00	2.09	1.87
Germany	1.59	2.78	2.15	5.81	3.64	3.73
Ireland	2.72	10.15	6.22	0.70	3.97	4.61
Italy	1.51	1.01	1.27	3.88	2.33	2.31
Norway	5.32	8.26	6.71	6.09	6.45	5.87
Portugal	0.54	0.00	0.29	2.13	1.04	1.11
Spain	1.36	1.01	1.20	3.71	2.22	2.86
Sweden	6.64	5.73	6.21	9.39	7.50	7.61
Switzerland	2.91	1.57	2.28	0.61	1.60	2.16
Netherlands	8.15	6.95	7.59	3.35	5.86	7.04
World Bank	21.07	17.76	19.51	38.56	27.26	24.97
UK	20.01	3.81	12.37	4.78	9.28	8.52
Total Group	100.00	100.00	100.00	100.00	100.00	100.00

Sources: PAP

Annex 3 Budget Support Programme Commitments (2000-2005)

	Disbursements (millions US\$)			Pledges
	2000	2001 (G9)	2003 (G11)	2005 (G15)
Belgium				2.4
Canada				1.2
Denmark	0 (a)	14.6 (b)	8.8	10
EC	52.2	61.0	71.0	58.0
Finland			3.2	4.8
France		1.8	3.2	3.6
Germany				4.2
Ireland		4.5	6.6	7.2
Italy				3.8
Netherlands	6.3	9.0	17.8	16.8
Norway	9.1	6.7	10.5	
Portugal				1.5
Sweden	10.9	9.8		13.3
Switzerland	4.7	5.0	5.3	7.4
UK	15.2	14.4	15.6	50.0
World Bank				60.0
Total	98.4	65.8	169.0	223.5

Source: Adapted from Swiss cooperation

Annex 4 List of People Interviewed

Name	Institution
Abilio Gune	Ministry of Planning and Development
Lourenço Sambo	Ministry of Planning and Development
Rogério Nkomo	Ministry of Finance
Agonias Macia	Ministry of Industry and Trade
Cardoso Muendane	Faculty of Economics - UEM
Gamiliel Munguambe	Ministry of Foreign Affairs
Francisco Macaringue	INE - National Statistics Bureau
Cristina Dimande	Ministry of Finance
Chabir Hassam	SNV - Netherlands
Per Mogstad	Royal Norwegian Embassy
Isabel Ramos	UN Resident Coordinator Office
Eva Pascoal	World Health Organization
Wallace Siakachoma	African Banking Cooperation
Paulo Cuinica	G20
Ramon Ynaraja	European Commission
Andrew Preston	DFID
Aniceto Bila	World Bank

