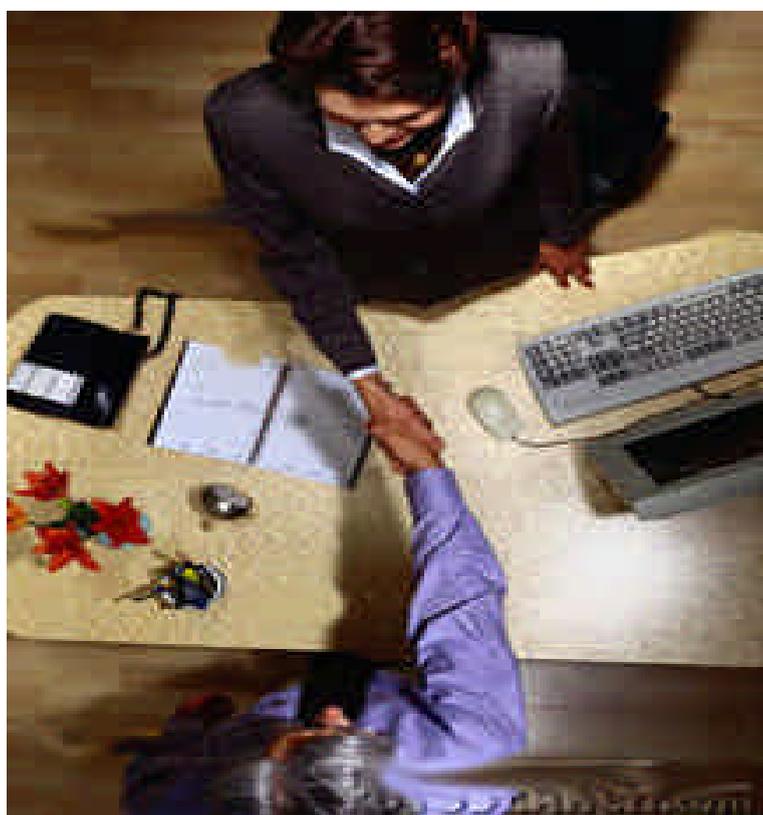


# **A Critical Assessment of Aid Management & Donor Harmonisation**



## **The Case of Malawi**



African Forum and Network  
on Debt and Development

A Critical Assessment of Aid Management and Donor Harmonisation  
The Case of Malawi

ISBN 978-0-7974-3412-7

EAN 9780797434127

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# 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.

## **Acknowledgements**

AFRODAD's work on this research would not have been possible without the input and assistance of many individuals and organizations. We are deeply grateful to all those listed here.

We owe a great debt of gratitude to Professor Chinyamata Chipeta and his research team for investing considerable time and effort in the research process of this report. The authors are indebted to various institutions and individuals which made invaluable contributions in terms of their key insights, opinion and data. We are particularly grateful to Mr. H M Kumwenda for the preliminary comments to the report. Nonetheless the views expressed in this report are those of the author. We also remain indebted to Nancy Dubosse, our new Programme Director for Research and Policy Analysis for the final edit and proof-reading of this report.

The central financial and technical support of Diakonia was invaluable to the project. We are also indebted to our colleagues, Mandla Hadebe and Taurai Chiraerae for the time and effort they put in making this study and publication a reality. Last but not least many thanks to many of our colleagues whom we cannot all name but whose input into the national research validation workshop remain vital to this output.

## 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

# Table of Contents

<b>1.0</b>	<b>Executive Summary</b>	<b>8</b>
<b>2.0</b>	<b>Introduction</b>	<b>9</b>
2.1	The Broad Paris Declaration Context for Better Aid	9
2.2	The Purpose of the Study	9
2.3	Main Messages from the Country Study	10
2.4	Aid Harmonisation - Working Definitions	12
3	Malawi Case	13
3.1	Methodology	13
3.2	Background	13
3.3	The National Development Framework	16
<b>4.0</b>	<b>Country Ownership</b>	<b>22</b>
4.1	Systemic Procedural Issues	22
<b>5.0</b>	<b>Country-led Partnership</b>	<b>25</b>
<b>6.0</b>	<b>Results Orientation And Mutual Accountability</b>	<b>27</b>
<b>7.0</b>	<b>Conclusions And Recommendations</b>	<b>29</b>
7.1	Country Ownership - Systemic Procedural Issues	29
7.2	Country Led Partnership	29
7.3	Results Orientation and Mutual Accountability for Development Results	29
Annex 1	Detailed Methodology	31
Annex 2	MDGs Targets	32
Annex 3	List Of Institutions And Persons Interviewed	34
	Endnotes	35
	References	35
	<b>List of Tables</b>	
	Table 1: Funding Gaps for the MGDS Priority 1 Activities	24
	<b>List of Figures</b>	
	Figure 1: Budget and Project Support to Government 2000 to 2006	14
	Figure 2: Aid Institutional Framework	21
	<b>List of Boxes</b>	
	Box 1: The Aid Experience of DfID in Malawi	14
	Box 2: The Aid Experience of the EU in Malawi	17
	Box 3: The Aid Experience of Germany in Malawi	19

## List of Acronyms/Abbreviations

ADB	African development Bank
AIDS	Acquired Immune Deficiency Syndrome
BWIs	Bretton Woods Institutions
CABS	Common Approach to Budget Support
CG	Consultative Group
DAC	Development Assistance Committee
DAD	Debt and Aid Management Division
DAS	Development Assistance Strategy
DfID	Department of Foreign and International Development
ECAMA	Economics Association of Malawi
EU	European Union
GDP	Gross Domestic Product
GTZ	German Technical Assistance Agency
HIPC	Highly Indebted Poor Countries
HIV	Human Immune Deficiency Virus
IDA	International Development Association
IFMIS	Integrated Financial Management Information System
IMF	International Monetary Fund
IMG	Independent Monitoring Group
JICA	Japanese International Cooperation Agency
JCPR	Joint Country Programme Review
KfW	
MEGS	Malawi Economic Growth Strategy
MEJN	Malawi Economic Justice Network
MEPD	Ministry of Economic Planning and Development
MGDS	Malawi Growth and Development Strategy
MOF	Ministry of Finance
MOU	Memorandum of Understanding
MPRSP	Malawi Poverty Reduction Strategy Paper
NAC	National Aids Commission
NGOs	Non-Governmental Organisations
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
PAP	Poverty Alleviation Programme
PFEM	Public Financial and Expenditure Management
PFM	Public Financial Management
PIUs	Project Implementation Units
PPEs	Pro-Poor Expenditures
PRGF	Poverty Reduction Growth Strategy
PRSP	Poverty Reduction Strategy Paper
SADC	Southern African Development Community
SAPs	Structural Adjustment Programmes
SWAP	Sector Wide Approach
UN	United Nations
UNDP	United NATIONS development Programme
USAID	United States Agency for International Development

## 1.0 Executive Summary

The Paris Declaration committed its signatories to moving institutional harmonisation of donors' policies, procedures, and practices to country-level implementation and alignment with the partner country's policies and systems. It goes beyond previous agreements by attempting to lay down a more practical, action-oriented roadmap to improve the quality of aid and its impact on development. It expands on the five key principles of ownership, alignment, harmonisation, managing for results, and mutual accountability and establishes a commitment to track and set targets against 12 indicators of progress.

Malawi has benefited from substantial donor support and it has implemented liberalisation and structural adjustment programmes, yet it still has high levels of poverty. A number of previous studies have focused on how Malawi has not been fully committed to these programmes or how it has misused or misappropriated aid. The effectiveness of aid depends on both donor and recipient country policies and practices. This study intends to expose the difficulties related to these issues in the context of Malawi and propose ways on how to resolve them.

While a high level of dependence on aid at this stage of Malawi's development is inevitable, the high level of dependence has created a number of problems for the country's budget process. These problems include unpredictability of aid, inflexibility of aid as most of it is project support, creation of parallel implementation units, high transactions costs and neglect of priority sectors in the allocation of the aid by donors. Despite these problems, the country has not formulated a plan for reducing dependence on aid or an aid exit strategy.

As a signatory to the 2005 Paris Declaration on Aid Effectiveness, the Government of Malawi has taken steps to strengthen the capacity of the Debt and Aid Management Division of the Ministry of Finance. However, this division does not seem to be working closely with the Ministry of Economic Planning, which is the other main official actor on aid issues. Other ministries that handle aid and interact with donors also seem to have little interaction with the Ministry of Finance on aid issues. These ministries should be encouraged to play their part in implementing the Paris Declaration.

As the ministry that has overall responsibility for managing debt and aid in the country, the Ministry of Finance has spearheaded the formulation of the Development Assistance Strategy (DAS), which sets out the policies and strategies for increasing efficiency and effectiveness in the mobilisation and utilisation of aid so as to achieve the development objectives contained in the Malawi Growth and Development Strategy (MGDS). The drafting of the DAS was completed in October 2006. The DAS seeks to improve the delivery of aid through a number of reforms to be undertaken by both the Malawi Government and donors, aimed at operationalising the five principles of the Paris Declaration on Aid Effectiveness.

Donors too have laid some foundation upon which to build in implementing the Paris Declaration; for example, the establishment of the Common Approach to Budget Support and the Health Swap, which implies that donors have already started to harmonise their aid operations in Malawi.

## **2.0 Introduction**

### **2.1 The Broad Paris Declaration Context for Better Aid**

The Declaration was the culmination of a series of international efforts to improve aid effectiveness. The first milestone was the February 2003 High-level Forum on Harmonisation in Rome. The Declaration adopted at the Forum committed the signatories to moving institutional harmonisation of donors' policies, procedures, and practices to country-level implementation and alignment with the partner country's policies and systems. The second milestone was the February 2004 Marrakech Roundtable on Managing for Development Results, in which the development community adopted a unified approach for improving the results orientation at the country level and for development agencies' practices.

The Paris Declaration goes beyond previous agreements and their statements of general principles by attempting to lay down a more practical, action-oriented roadmap to improve the quality of aid and its impact on development. It expands on the five key principles of ownership, alignment, harmonisation, managing for results, and mutual accountability. It establishes a commitment to track and set targets against 12 indicators of progress. The Declaration thus highlights the importance of predictable, well aligned, programmed, and co-ordinated aid. Its purpose is to improve aid delivery in a way that best supports the achievement of the Millennium Development Goals by 2015.

At the global level, the Paris Declaration was given further impetus through the 2005 G8 Summit in Gleneagles with its ambition to increase aid to Africa by US\$ 25 billion by 2010. Organisation for Economic Cooperation and Development's (OECD's) Development Assistance Committee (DAC) is also playing a key role. It is, inter alia, charged with monitoring the implementation of the Paris Declaration through its Working Party on Aid Effectiveness.

Africa is central to this process. Around half of Africa's countries -although not the African Union or any of the regional organisations - are also signatories to the Paris Declaration. This includes eight SADC member countries and Malawi is one of them. The ADB together with the World Bank and the UNDP are organising workshops in Africa to facilitate implementation at the country level. The Declaration was also a strong inspiration behind the formulation of Malawi's Development Assistance Strategy (DAS).

### **2.2 The Purpose of the Study**

The purpose of this study is to identify stumbling blocks to effective aid delivery, donor practices that create a burden on the Malawi Government in terms of ownership, transaction costs, institutional capacity, as well as identify possible benefits and opportunities to cost effective development assistance delivery.

Malawi has benefited from substantial donor support and it has implemented liberalisation and structural adjustment programmes, yet it still has high levels of poverty. A number of previous studies have focused on how Malawi has not been fully committed to these programmes or how it has misused or misappropriated aid. Not much attention has been paid to how donor behaviour has impacted on the quality and effectiveness of aid. The effectiveness of aid depends on both donor and recipient country policies and practices. This study intends to expose the difficulties related to these issues in the context of Malawi and propose ways on how to resolve them.

### **2.3 Main Messages from the Country Study**

Malawi is highly dependent on foreign aid, especially for financing its development programme. Recently, the level of aid has increased markedly. In the medium term, the volume of aid is expected to rise further. While a high level of dependence on aid at this stage of the country's development is inevitable, the high level of dependence has created a number of problems for the country's budget process. These problems include unpredictability of aid, inflexibility of aid as most of it is project support, creation of parallel implementation units, high transactions costs and neglect of priority sectors in the allocation of the aid by donors. Despite these problems, the country has not formulated a plan for reducing dependence on aid or an aid exit strategy.

As a signatory to the 2005 Paris Declaration on Aid Effectiveness, Malawi takes this international agreement seriously. The Malawi Government is committed to implementing it. To this end, it has taken steps to strengthen the capacity of the Debt and Aid Management Division of the Ministry of Finance.

However, this division does not seem to be working closely with the Ministry of Economic Planning, which is the other main official actor on aid issues. Other ministries that handle aid and interact with donors also seem to have little interaction with the Ministry of Finance on aid issues. These ministries should be encouraged to play their part in implementing the Paris Declaration.

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The DAS seeks to improve the delivery of aid through a number of reforms to be undertaken by both the Malawi Government and donors, aimed at operationalising the five principles of the Paris Declaration on Aid Effectiveness. The reforms include the establishment of new aid coordination mechanisms, which, inevitably has resulted in an increase in the number of structures that manage aid in the country. Furthermore, the DAS considers the current aid relationship in Malawi in relation to each of the five principles and how to implement them to improve that relationship in the country. After clarifying the current and desired states, it examines obstacles to achieving the desired states. Then it recommends actions for both the government and development partners to take to overcome these obstacles. Performance indicators and targets are finally set to measure progress towards each of the desired outcomes. These can be found in the Annex to this study.

Donors too have laid some foundation upon which to build in implementing the Paris Declaration; for example, the establishment of the Common Approach to Budget Support and the Health Swap, which implies that donors have already started to harmonise their aid operations in Malawi

The Debt and Aid Management Division has started to monitor progress towards attaining the Paris Declaration goals, which form the basis of the DAS. While it is too early to assess progress towards implementing the provisions of the Paris Declaration and the DAS and to evaluate results as not much time has lapsed since the Paris Declaration was signed and the DAS was drafted, baseline assessments of the situation carried out by the Debt and Aid Management Division of the Ministry of Finance are useful indicators of how far Malawi has to go.

The current or baseline situation (before implementation) is that there is wide variation among donor policies and practices with regard to:

- Support for the national development strategy
- Assistance to strengthen national capacity for implementing the strategy
- Alignment of aid flows to national priorities
- Use of national financial management and procurement systems
- Strengthening capacity by avoiding parallel implementation structures
- Predictability of aid,
- Use of untied aid
- Flexibility of aid within donor funding cycles
- Procedures and systems, including monitoring and evaluation systems

The result of the baseline evaluation is that Malawi is far away from achieving any of the targets that have been set either by the Paris Declaration or by the DAS with respect to ownership of the national development strategy; alignment of aid to national priorities; harmonisation of donor plans, procedures and systems; management for results and mutual accountability.

From the point of view of the government, the main obstacles include:

- Lack of coherence between sector strategies and budgeting processes.
- Lack of decisive action by the government to guide donors and encourage harmonisation.
- Lack of capacity in ministries for implementation, monitoring and evaluation, including annual reviews
- Lack of sound analysis of target setting in relation to the realisation of the principle of results orientation
- Staffing shortages in the Ministries of Finance and Economic Planning and Development
- Lack of commitment of line ministries to the ideals of the Paris Declaration.

From the standpoint of donors, the main obstacles include:

- Use of parallel implementation structures. This applies to Germany, European Union and Britain, but not to Sweden. Nothing is known about France, as there is no information on that country.
- Inflexibility of donor processes. This applies to the European Union, but not to Britain and Sweden. Nothing is known about France and Germany, as there is no information on them.
- Use of their own monitoring and evaluation systems imposed by their governments, which differ among donors. This applies to all the five bilateral donors covered in this study,
- Fixing of some project cycles for a multi-year period, stating when reviews are required, as a result of which some donors are continuing with their individual monitoring exercises. This applies to the European Union and Sweden, but not to Britain. It is not known if it also applies to France and Germany.

Therefore, concerted efforts are required by the government and donors to ensure that progress is made. This will require reform by the government and pressure on donors to reform their systems.

The target for the implementation of some of the actions is 2011. But for other actions the targets are either 2006 or 2007. This is clearly ambitious, considering capacity constraints in the government. But, even then, progress on some actions has been made or is not difficult to achieve. As pointed out in the 2006 Annual Debt and Aid Report, the 2006/07 budget incorporates most if not all aid to the government. The Report also states that in order to achieve the indicators from the DAS on the MGDS, what remains to be done is the establishment of a resource envelope and an exercise to ensure wide support from donors. A Development Assistance Calendar has been prepared.

There are also a number of reforms that donors can implement immediately. For example, the 2006 Annual Report of the Debt and Aid Division states that progress towards increasing the predictability of aid and ensuring that new projects do not use project implementation units (PIUs) can begin now. It also states that those donors that are undertaking Country Assistance Strategies can be requested to align them to the MGDS immediately, even though the MGDS has not yet been officially launched.

Attaining the targets in the DAS and the Paris Declaration will also require well-coordinated work by sector and central ministries. The processes for ensuring that this takes place must begin immediately in the current (2006/07) financial year.

The fact that donors are already funding sectors that have been accorded priority in the MGDS implies that it may be possible to align their support to the Strategy. Another opportunity worth seizing is that the number of the main donors that support Malawi is relatively small, numbering ten. This may facilitate harmonisation of their aid operations, procedures and processes.

## **2.4 Aid Harmonisation - Working Definitions**

Aid harmonisation refers to the creation of common arrangements for managing foreign aid. It requires that donors should work together to ensure that their systems and processes are standardised to reduce transaction costs to the recipient government.

It entails adopting common procedures; e.g., by using government accounting and procurement systems and routing aid through the budget. Among other things, it also involves the use of joint aid missions to a country, carrying out joint diagnostic studies and undertaking monitoring, auditing and evaluation exercises together. By minimising or eliminating separate aid operations and managements, aid harmonisation should help to make aid more transparent, accountable and effective.

What are the challenges in ensuring more harmonised, transparent and collectively effective donor support? The Paris declaration seeks to develop common arrangements, simplify procedures and to ensure a more effective division of labour. There are several components here and some are more challenging than others. One is for recipient governments to identify and analyse the various donors' comparative advantages and to find how to achieve donor complementarities at national or sector levels. To ensure this the recipient government first needs to map what the various donors are doing through it, through subsidiary organisations and project implementation units, and through their bilateral country programming.

A second challenge is to ensure that donors work together both to harmonise separate procedures and to facilitate a division of labour between them. This is far more challenging because different donors have priorities and different management and decision-making structures. Most donors are supportive of increased harmonisation, although several express strong limitations, especially when it comes to the pooling of financial resources. A first step here is for the government to promote likeminded donors into working in each sector or sub-sector as a single group. In some instances the donors may also agree to "delegate" the co-ordination of cooperation to one donor acting as their representative.

The Paris Declaration will also make it easier for recipient governments to put demands on the donor agencies and to reduce procedural constraints. There is considerable scope to improve harmonisation through the establishment of technical theme groups in selected areas and sub-sectors. As a bare minimum, recipient governments should be able to reduce duplication in management as well as the number of donors it deals with individually; e.g., in relation to support for capacity building in recipient governments. Here there is a lot of duplication of effort.

## 3.0 Malawi Case

### 3.1 Methodology

The Terms of Reference for this study required the researcher to choose his own methodology, but insisted that this should include visits to the relevant ministries dealing with aid management, as well as visits to relevant departments in the embassies of France, Germany, European Union Delegation, Britain and Sweden to conduct interviews with them. In addition, he must have interviews with relevant members of civil society organisations. As explained in detail in the Annex, the methodology used for this study has consisted of a desk study or literature review and interviews with key stakeholders, as suggested by the sponsors. The list of institutions and persons that were interviewed can also be found in the annex to the study.

### 3.2 Background

Why do bilateral donors give foreign aid to a country like Malawi? Why does Malawi accept foreign aid? Promoting the development of poor nations is not the chief motive for giving bilateral aid. The main objective is to promote the political and strategic interests of bilateral donors, which are to create and retain allies, support countries whose geopolitical positions are of strategic importance, militarily and/or politically. Usually, when aid is given, interest is charged. Aid in the form of outright grants is a small proportion of bilateral aid. Furthermore, the donor ensures that it is tied to the purchase of goods and services in the donor country. This tying of aid imposes enormous costs on the recipient government as it is not free to source goods and services domestically or in a third country, which may be the cheapest source (Todaro, 1994).

Although aid may not help them to achieve their development objectives, Malawi and other less developed countries continue to accept aid because they believe that it is a crucial and essential ingredient of the development process. In particular, aid supplements scarce domestic savings and foreign exchange receipts. They believe that rich nations have a moral obligation to help them. For them, the issue is not whether there is aid. The real issue is how much aid and on what conditions (Todaro, 1994)

Since independence in 1964, external assistance has financed most of the government's development budget in Malawi. In the 2006/2007 government budget, for example, official development assistance (ODA) covers around 80 percent of the development budget and around 45 percent of the total resources available to the government. As a percentage of nominal gross domestic product (GDP), development support alone rose from 16 percent in 2004/05 to 22 percent in 2006/07. A high level of dependence on aid is unavoidable at early stages of development. However, it can

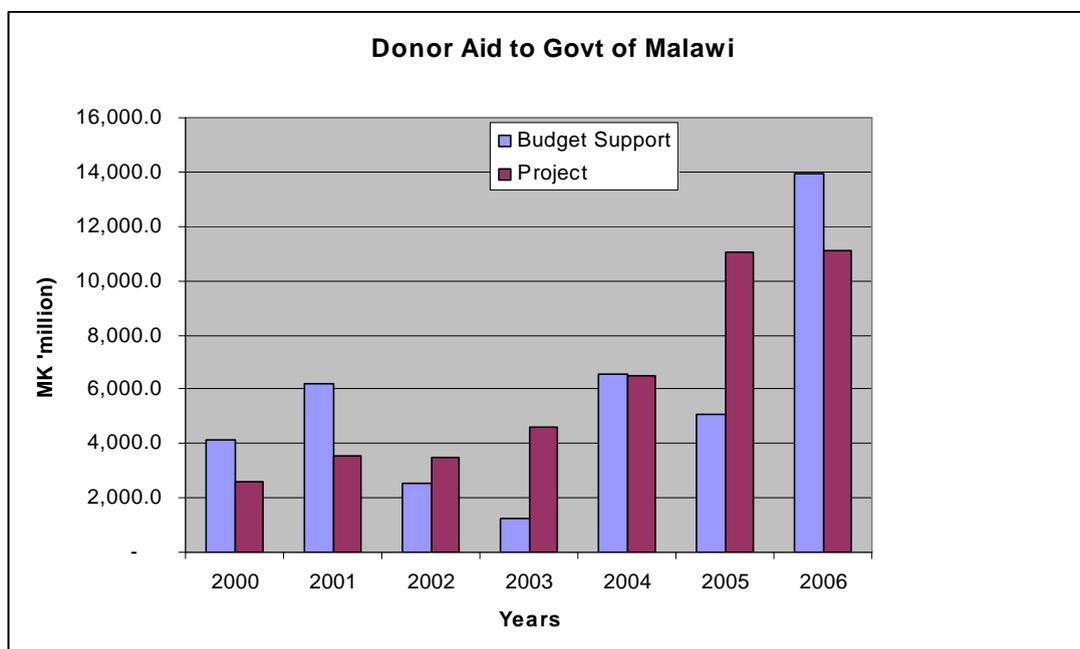
cause problems, especially when it is unpredictable, and uses modalities for aid disbursement that are not helpful, problems that we shall return to later. In spite of these problems, the government has not come up with a plan to reduce dependency on foreign aid or an exit strategy.

A breakdown of aid received in the 2005/006 fiscal year shows that DfID is the largest source of aid for Malawi, followed by the World Bank, EU and Norway, in that order. Other major sources of aid are USAID, ADB, UNDP, GTZ, JICA and KfW. Aid from these sources includes disbursements made directly to government and those disbursements that are administered by the donors themselves or Non-Governmental Organisations (NGOs). Aid from DfID includes Dutch support, which DfID administers. Similarly, aid from Norway includes support from Sweden, which is administered by the Norwegian Embassy in Malawi. The volume of aid has increased in recent years and is expected to rise further in the coming years (2).

By modality of aid, budget support seems to be getting more dominant from the 2002/2003 financial year (Figure 1 below). Project support has consistently been on the increase throughout the last seven years probably showing that, since donors have a bigger role in managing it, it has not been affected by political developments. Most of the development partners operate through this mode of support. Budget support accounted for 28 percent of aid in the 2005/2006 financial year. DfID, World Bank, EU and Norway are the donors that provided this mode of support. Dedicated grants, which came from the same donors that provided budget support, made up the remaining 12 percent of the aid received.

These are grants made to government with restrictions only as to the sector in which the funds are spent, but not the specific activities. This is unlike project support, which specifies the activities to be funded (3). The figure below helps to show trends in budget and project support to the Malawi Government starting in the year 2000.

**Figure1: Budget and Project Support to Government 2000 to 2006**



Source : Prepared on the basis of data sourced from the Ministry of Finance

**Box 1: The Aid Experience of DfID in Malawi**

According to the 2006 Annual Debt and Aid Report, DfID is the single largest donor to Malawi. During the 2005/06 financial year, for example, it accounted for 28 percent of total development support, having increased from a share of 24 percent in 2004/05. It is expected to contribute a percentage similar to the 2005/06 one during the current, 2006/07, financial year. Ninety-five percent of the aid goes through the government. Thus, DfID relies on government accounting and procurement systems.

Project support dominates its aid package. But the proportion of its aid that is given in the form of budget support is not much different from it. During the 2005/06 financial year, these proportions were 42.6 percent and 40.7 percent, respectively. The remaining 16.7 percent of the support took the form of dedicated grants, implying that project support was a smaller proportion of total British aid.

Another characteristic of British aid is that it is predictable. In the 2005/06 financial year, for example, the variance between projected and actual disbursements of project support was a positive 9 percent. For budget support, the variance between projected and actual disbursements was nil. Both sets of disbursements exclude humanitarian aid.

The focus of British aid in Malawi is on good governance, education, health, economic reform and renewable natural resources where focus is on improving food security of the smallholder farmer sector and assistance with land reform issues. This will make it easy to align its aid to the new Malawi Growth and Development Strategy in which good governance, education and health feature as priority activities.

DfID prides itself as the most advanced aid agency in terms of autonomy. The country office has a lot of discretion and a lot of decisions are made here. For expenditure of at least £7.5 million, approval is sought from London. But it does not have an incentive system to reward achievement of outcomes instead of success in spending money.

For the purpose of making long-term commitments and increasing predictability and reliability of donor funding, DfID is preparing its Country Assistance Strategy. It will give £70 million for 2007 and it has planned to give £300 million over the 2007/11 period. There are more specific commitments, but they are not the same as circumstances change and also sometimes the government wants money for other purposes. In terms of the institutional framework DfID is a member of the Common Approach to Budget Support (CABS). Currently, CABS works on a yearly basis, but it is planned to make long-term commitments through it. The Health SWAP, to which DfID subscribes, is a six-year commitment beginning 2005/06 to 2010/2011. There DfID has committed £100 million.

Aid in the form of budget support gives the government flexibility in the way that the funds can be spent. By using the government, budget support also strengthens its systems. Donors, however, prefer project support on some occasions because they are not sure that the government will spend the funds on the intended activities. This is why sometimes they even create parallel project management units, apart from lack of confidence in the accounting and procurement systems of the government or fearing that aid will be affected by corruption.

Another characteristic of aid received by Malawi is that the funds from development partners deviate widely from the aid projections that the government uses for its planning. In the 2005/2006 fiscal year, for example, excluding humanitarian aid, project support from most of the donors had negative variances, meaning that the country received less aid than was committed, except for aid from DfID, USAID and World Bank, which had positive variances. This has adverse effects since donors finance most of the development activities. It limits government's ability to plan its own activities, and it hampers the implementation of development plans. These variances partly reflect implementation problems, which result from problems of government implementation of counterpart agreements. Partly, they reflect inaccuracy of projections (4). Sometimes aid can be cut if the country fails to satisfy donors on its governance record, or if it fails to meet economic performance criteria, especially if the IMF suspends drawings on its facilities as a result of failure to satisfy conditionality.

As aid flows increase, donors are placing an ever rising burden on government ministers and senior officials, as numbers of parallel reporting requirements, donor missions and local consultation committees expand. Possible solutions to this include persuading more partners to channel support through the budget or sector baskets; establishing a well spaced annual cycle of consultation meetings to rationalise interactions with local donor groups; declaring quiet times of the year for donor missions; establishing targets for reducing mission frequency; and on occasion being ready to refuse aid offered in the wrong modalities or in the wrong form.

By themes in the Malawi Growth and Development Strategy (MGDS), the breakdown of aid received in 2005/2006 shows that the Social Development theme is the most highly funded theme. It received more than double the amount of aid resources received by the next highly funded theme, Social Protection. The least funded theme was Good Governance, followed by Infrastructure and Sustainable Economic Growth (see Table 1), both of which are crucial to the MGDS. Within Social Development, the sector that is attracting the most donor funding is the Health Sector, with or without HIV/AIDS. Aid to the Health Sector includes basket funding for the Health SWAP. This high level of aid there reflects relatively high donor confidence in government systems in this sector. It is also worth pointing out that, although transport and infrastructure is relatively well funded, there is very little spending on irrigation and water supply, despite the priority accorded to reducing dependence on rain-fed agriculture. The relatively low level of donor support in trade and private sector development is also a matter of concern (5).

Debt and aid management and coordination of donor assistance has always been the responsibility of the government. At first three institutions were responsible: the Economic Planning Division of the Office of the President and Cabinet, which served as the Secretariat, the Ministry of Finance and the Reserve Bank of Malawi. In the early 2000s, following the establishing of a full Ministry of Planning and Economic Development and the merger of that ministry with the Ministry of Finance, the secretariat became part of the combined ministries. The two ministries were subsequently separated, but the debt and aid secretariat remained in the Ministry of Finance and is a separate division of that ministry now. From the interviews that we had with the officials of the two ministries, it seems that there is less collaboration between them than before. This is unfortunate, as both ministries shoulder defined responsibilities under the Development Assistance Strategy, which operationalises the Paris Declaration. Information collected during interviews also suggests that although most of the ministries manage aid and deal with local donor groups, they are not familiar with the Paris Declaration or the Development Assistance Strategy.

Limited capacities in government in the past have inhibited aid management and coordination. This has resulted in donors creating separate but unsustainable aid management systems; despite the fact that it is the responsibility of donors to respect national ownership, advise and support the government in the formulation of national development strategies, plans and programmes, and subsequently to invest ODA resources in these strategies, plans and programmes.

Recently, progress has been made in clarifying national priorities and, in some cases, formulating national and sector programmes. Along with the adoption of the Medium Term Expenditure Framework, the Health SWAP and the Common Approach to Budget Support (CABS) by Britain, EU, Sweden and Norway, this should help to improve the coherence and coordination of donor responses to national needs. The establishment of the Debt and Aid Management Division in the Ministry of Finance should also assist in this task. This division has replaced an arrangement under which officials of the Ministry of Economic Planning and Development, Ministry of Finance and the Reserve Bank of Malawi performed the debt and aid management function jointly. Other government aid management and coordination efforts have included the Minister of Finance's regular meetings with donors, and meetings convened by ministers of key sector ministries. The Annual Consultative Group (CG) meetings organised by the World Bank were used for both resource mobilisation and policy cohesion purposes.

More regularly, resident donors used to meet weekly under the chair of the UN Resident Coordinator. Non-resident donors participated whenever they were in the country. In addition, the UN Resident Coordinator convened an annual donor retreat, which drew representatives from all donors, resident as well as non-resident. Furthermore, twelve informal sector/thematic groups were in existence for the purpose of coordination at the technical level. Government officials chaired a few of these groups. The working groups were: Health and Population; Education; Environment and Natural Resource Management; Economic Management; Poverty; NGOs; Governance; Transport; Water; Agriculture and Food Security; Drug Abuse Control; Enterprise and Private Sector Development; Gender; HIV/AIDS; Youth; UN Food Security; and UN Disaster Management (6).

### **3.3 The National Development Framework**

#### **3.3.1 Fiscal and Monetary Policies**

In the recent past, policies to stabilise the economy of Malawi have been implemented under a Poverty Reduction and Growth Facility (PRGF) arrangement supported by the International Monetary Fund (IMF), an IMF staff monitored programme, and an enhanced Heavily Indebted Poor Countries (HIPC) Initiative programme. Adopted in 2000 and planned to run up to 2003, the PRGF aimed at increasing the rate of economic growth, reducing the rate of inflation, improving the external financial position, and reducing poverty. The measures for attaining these objectives included reducing the rate of growth of the money supply, achieving a balanced fiscal position, improving expenditure control, deepening structural reforms, strengthening governance and prioritising pro-poor expenditure.

The PRGF programme was suspended in 2001, after Malawi had drawn only US\$6.44 million out of US\$45.11 million, owing to the country's inability to achieve the fiscal targets agreed to with the IMF. Other donors followed the IMF by suspending their aid. This adversely affected the implementation of the Malawi Poverty Reduction Strategy Paper, as explained below. If this practice continues, it could also affect the implementation of agreements that were reached under the Paris Declarations.

The staff monitored programme was adopted in 2004 in order to lay the ground upon which the country would implement a new PRGF. It was successfully completed in 2005. All the key fiscal targets were met. The target on revenues was more than met. There was also significant improvement on structural targets. The vote on special activities within the approved budget was eliminated, and ministries and departments adhered to submission of expenditure returns every month. Slippages were few, mainly relating to the inflation target and the growth of net domestic and foreign assets (7). As a result, Malawi qualified for a new three-year PRGF programme.

The main economic objectives of the PRGF are to:

- Raise the rate of economic growth to 6 percent per year, with an emphasis on rural incomes;
- Increase health services and educational opportunities;
- Reduce core inflation to the 5-8 percent range;
- Build international reserves to at least two months of imports; and
- Run a fiscal surplus to reduce the government's domestic debt to less than 15 percent of GDP from over 24 percent.

By sheer coincidence, the core inflation target is consistent with that of the SADC macroeconomic convergence programme. The targets for economic growth and international reserves are not, but could have been made consistent with SADC targets. And those for social services and domestic debt are not relevant to it.

The strategies for achieving the above objectives include zero tolerance for corruption and pursuit of good financial, economic and political governance; improving the macroeconomic environment and pursuit of sound fiscal, monetary and exchange rate policies. Malawi also intends to move towards an independent central bank as part of a SADC wide initiative (8).

Malawi did not qualify for HIPC I, which came into being in 1996, because its debt service ratio was less than the threshold of 20-25 percent. Under HIPC II, which was introduced in 1999, the threshold debt service ratio was reduced to 15 percent. This enabled Malawi to qualify. Having taken significant steps to reduce macroeconomic imbalances, broaden market-oriented reforms and improve outcomes in the social sectors, and having improved macroeconomic performance, the country reached the decision point in December 2000. Consequently, the IMF and the World Bank Group's International Development Association (IDA) agreed to support a comprehensive debt-reduction programme for Malawi. The enhanced HIPC initiative would provide total debt relief from all creditors worth around US\$1 billion. This would be used for poverty reduction efforts by releasing resources for expenditure on health, education, rural development and other priority areas.

The IMF and IDA would provide full debt relief when Malawi had reached the completion point after the following conditions had been met:

- The adoption of a full Poverty Reduction Strategy Paper (PRSP) prepared through a participatory process, and satisfactory progress in implementing and monitoring the PRSP for at least a year.
- The satisfactory implementation of financial and economic policies supported by the IMF's Poverty Reduction and Growth Facility.
- The improvement of public expenditure management and governance, through quarterly expenditure reporting on spending in high priority areas and through the separation of fiscal management and audit functions under new legislation.
- The strengthening of land and credit markets.
- The implementation of specific actions in the social sectors aimed at targeting safety net programmes to protect the poorest, improving health care delivery, slowing the spread of HIV/AIDS, and raising the quality of education.
- The confirmation of the participation of other creditors in the debt relief operation.

## Box 2 The Aid Experience of the EU in Malawi

According to the 2006 Annual Debt and Aid Report, the EU is the second largest donor to Malawi. During the 2005/06 financial year, for example, it accounted for 20 percent of total development support, up from 10 percent in 2004/05. It is expected to contribute a larger percentage to development support during the current, 2006/07, financial year.

Project support dominates its aid package. During the 2005/06 financial year, for example, project support accounted for 53.6 percent of total EU aid. Budget support accounted for the remaining 46.4 percent. Designated grants did not feature in its aid package in that year.

Unlike British aid, EU aid is not predictable. In the 2005/06 financial year, for example, the variance between projected and actual disbursements of project support was a minus 19 percent. And for budget support, the variance between projected and actual disbursements was minus 22 percent. Both sets of disbursements exclude humanitarian aid.

The EU is a member of CABS, which interfaces with the government. There are prospects for the proportion of aid channelled in this way to increase and for new partners to join the group. The EU has said that it will align its strategies with the MGDS.

The EU aid programme in Malawi is concentrated in the sectors of agriculture and natural resources, with focus on national and household food security, and natural conservation; transport concentrating road infrastructure; and on health, including planning, rehabilitation of hospitals and clinics, and training. This will make it easy to align its aid to the new Malawi Growth and Development Strategy in which agriculture, transport and health feature as priority activities.

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The Malawi Poverty Reduction Strategy Paper (MPRSP) was launched in April 2002. But, the country still failed to reach the completion point because it did not meet two of the other conditions; namely, satisfactory completion of financial and economic policies supported by the IMF's PRGF, which was suspended; and improvement of public expenditure management and governance. The implementation of the new PRGF programme has met with more success, with the country satisfying almost all the conditions of the programme. As a result, Malawi had its foreign debt cancelled at the end of August 2006.

### **3.3.2 Policies for Economic Growth and Development**

Recent policies for economic growth and development from the year 2002 are contained in the Malawi Poverty Reduction Strategy Paper (MPRSP), the Malawi Economic Growth Strategy (MEGS), the Malawi Growth and Development Strategy (MGDS) and other strategy documents. The Malawi Poverty Reduction Strategy Paper (MPRSP) was developed in the early 2000s at the request of the Bretton Woods Institutions (BWIs) so that the country could benefit from debt relief under the enhanced Highly Indebted Poor Countries (HIPC) Initiative, a Poverty Reduction and Growth Facility arrangement and other concessionary assistance.

The MPRSP had two key elements; namely, a set of government policies and priorities, both overall and for individual sectors; and broad expenditure allocations, covering both domestic and donor funding. Its purpose was to try and ensure that scarce resources were allocated in accordance with government policies and priorities for poverty reduction. In varying degrees, the MPRSP drew upon and learnt from a number of previous national development strategies; namely, the 1987-1996 Statement of Development Policies, which was developed through extensive consultations within government, contained a profile of the poor, the causes of poverty and the measures for addressing the problem of poverty; the Social Dimensions of Adjustment Project, which aimed at minimising the adverse effects of Structural Adjustment Programmes (SAPs) on the poor and to strengthen capacity for integrating the poor in the national development process; the Policy Framework for the Poverty Alleviation Programme (PAP); and Vision 2020.

Implementation of a PRSP entails ensuring that actual public sector expenditure, both government and donor funded, is consistent with PRSP allocations, and that the policies described in the PRSP are carried out. Implementation of the MPRSP started in 2002 and ended in 2005. The first progress report covering the 2002/2003 fiscal year concluded that the implementation of the MPRSP had been unsatisfactory as actual funds allocated for pro-poor activities had been substantially lower than envisaged in the strategy paper. One of the main reasons for this is that Malawi's economic programme supported by the IMF's Poverty Reduction and Growth Facility (PRGF) had been off track since November 2001, as mentioned above.

This had led to suspension of external budgetary assistance and to increased recourse to domestic borrowing to cover large budget deficits. As a result, the stock of domestic debt increased from MK26.017 billion at the end of June 2002 to MK67.741 billion at the end of June 2004, before falling slightly to MK67.564 billion at the end of June 2005. The debt service needs of this domestic debt required more resources, so the resources available for financing pro-poor activities were reduced. Some pro-poor activities were not even allocated resources, whereas non-priority activities got more resources than were envisaged in the MPRSP. The first progress report did not analyse in detail the implementation of the sectoral and policy reforms identified in the MPRSP. Many of these reforms were initiated, but the pace was slower than envisaged in the MPRSP. Examples include land policy and privatisation. But substantial progress was reported in tracking pro-poor expenditures, preparing and approving the micro-finance policy, developing the wage policy, and developing and passing the new Public Finance Management, Public Audit and Public Procurement Bills.

The second annual progress report concluded that implementation of the MPRSP during the 2003/2004 fiscal year was characterised by policy slippages, particularly in the field of fiscal management, and under-funding of pro-poor activities as compared to the MPRSP. It noted that fiscal indiscipline led to increases in domestic debt, interest rates and inflation. This strained relations with donors, resulting in reduced budgetary assistance. Consequently, the share of resources allocated to pro-poor activities was much lower than planned in the MPRSP.

### **Box 3 The Aid Experience of Germany in Malawi**

According to the 2006 Annual Debt and Aid Report, Germany is not a major donor to Malawi. During the 2005/06 financial year, for example, it accounted for a mere 5 percent of total development support. It is expected to contribute a similar percentage to development support during the current, 2006/07, financial year.

It seems that all its aid is given in the form of project support. During the 2005/06 financial year, aid from Germany amounted to about \$7 million.

Like EU aid, German aid is not predictable. In the 2005/06 financial year, for example, the variance between projected and actual disbursements of project support was minus 9 percent.

German development assistance to Malawi is primarily concentrated on technical cooperation and capital investment. In addition, Germany supports the country's structural adjustment efforts through balance of payments support. The major sectors benefiting from German assistance are: health, education, natural resources, infrastructure and agriculture. This will make it easy to align its aid to the new Malawi Growth and Development Strategy in which agriculture, transport and health feature as priority activities.

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The new government, which took office in May 2004, successfully adopted measures to restore fiscal discipline. An inherent problem with pro-poor expenditures (PPEs) was that since they were supposedly protected and hence could not suffer a cut in budgetary resources, ministries and cost centres prioritised too many activities, including those that were not relevant, as pro-poor. Hence, there was misallocation of resources. On top of that ministries are known to have been diverting funds from the identified pro-poor activities.

Sometimes resources were left unused because cost centres did not know how HIPC funds should be utilised or because they were not sure. The third annual progress report for the 2004/2005 fiscal year noted that expenditure on protected pro-poor activities had been less than budgeted, except under Pillar I.

The Malawi Economic Growth Strategy (MEGS) was launched in 2004 after nearly two years of formulation. MEGS was aimed at complementing the MPRS by stimulating private sector growth and ensuring that the poor are key participants and beneficiaries of economic growth. It owed its origin to two missing links in the MPRSP with which both the government and the private sector were concerned. The first is that while the MPRSP contained a pro-poor growth strategy for stimulating economic growth in ways that directly attack poverty, it focused on the role of micro and small-scale enterprises to the exclusion of large-scale ones. The second is that the MPRSP neither planned for a sufficiently high rate of economic growth, which is considered necessary for poverty reduction, nor gave sufficient attention to the role of the private sector, investment and trade, which are considered to be the main drivers of economic growth. Part I of MEGS set out the background to the strategy, the framework for delivering growth and the strategy for dealing with the macroeconomic constraints that affect enterprises. Part II analysed the main sectors of the economy, the strategies for the growth of the core and other sub-sectors of the economy. There was also a review of key public institutions that support and regulate the private sector. Donors did not support MEGS when it lasted as they had already committed their assistance to the MPRSP.

Both the MPRSP and MEGS expired in 2005 and they have been succeeded by a new strategy called the Malawi Growth and Development Strategy (MGDS). MGDS draws upon and combines critical issues in the MEGS, MPRSP, Vision 2020, the Millennium Development Goals and sector strategies. Like the MEGS, the MGDS focuses on achieving strong and sustainable economic growth that will enable Malawians to create their own wealth through economic empowerment. Some of the specific aims of the MGDS are to:

- (i) Resume economic growth fast enough to bring about the Government's vision;
- (ii) Create new wealth for the people and more jobs;
- (iii) Gradually emerge as an industrial nation capable of transforming agricultural primary commodities, other raw materials and minerals;
- (iv) Transform Malawi from a predominantly importing and consuming country to a producing and exporting country;
- (v) Increase supply of goods and services for domestic and international markets; and
- (vi) Increase domestic and foreign financing and investment in agricultural processing, industrial production and manufacturing.

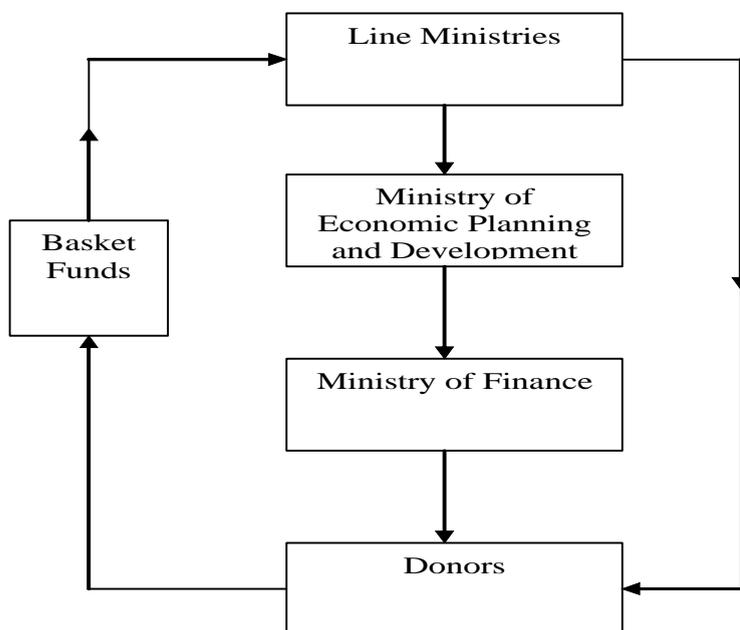
The Strategy is comprehensive, with six priorities in this order: agriculture and food security; irrigation and water development; transport and infrastructure development; energy generation and supply; integrated rural development; and prevention and management of nutrition disorders, HIV and AIDS. Inside The MGDS document, these six priorities were organised around five broad thematic areas; namely, economic growth, social protection, social development, infrastructure development, and improved governance. Improving food security so as to ensure that Malawi is a hunger free nation takes a prominent position, as does the achievement of other MDGs. Macroeconomic stabilisation remains an important feature in the Strategy. This is a mirror image of the macroeconomic stabilisation programme contained in the PRGF.

The process of developing MGDS, like the process of developing MEGS and the MPRSP before it, was consultative. Most of the key stakeholders, namely the private sector, civil society, donors, and the three arms of government were consulted through appropriate structures. Furthermore, the private sector through the National Action Group, which brings together representatives of donors, government and the business community, and civil society were involved in writing the MGDS, and will be involved in monitoring and evaluation.

The government approved the MGDS in December 2006. Afterwards, line ministries are supposed to prepare the projects or programmes contained in the MGDS that they are required to implement. Once this is done, the projects or programmes are submitted to the Ministry of Economic Planning and Development.

The Ministry of Economic Planning and Development assesses them and it can either accept or reject them. After acceptance by the Ministry of Economic Planning and Development, they are sent to the Debt and Aid Management Division of the Ministry of Finance, which is responsible for seeking assistance from donors.

**Figure 2: Aid Institutional Framework**



The process of doing so will be done through an investors' conference, which will be held soon. In theory, this is how the process of seeking aid is supposed to work. In practice, sometimes line ministries bypass this process and approach donors directly, something that the Ministry of Finance is discouraging.

In allocating aid resources, donors follow priorities set by their governments. Since these priorities are similar, it means that they are competing for sector support, with the result that some sectors get a lot of support while others do not get much support. In order to mitigate this, there is a need for mechanisms for matching donor support to sector strategies. Unfortunately, there are not many such mechanisms. The best known mechanism in Malawi is the Health SWAP through which a number of donors support the Ministry of Health and other health institutions.

As far as budget support is concerned, on their part line or sector ministries do not compete for it. The Ministry of Finance allocates all such support.

## 4.0 Country Ownership

### 4.1 Systemic Procedural Issues

One of the principles of the Paris Declaration stipulates that developing countries should exercise effective leadership, including coordination of development efforts, and donors should be responsible for supporting this and for helping to strengthen national capacity to implement. The Paris Declaration indicator for the first part of this principle, which concerns developing countries, is that partners should have operational development strategies that have clear strategic priorities linked to a medium term expenditure framework and reflected in annual budgets.

Drawing on the Paris Declaration, the Malawi Government has prepared a Development Assistance Strategy (DAS) for the purpose of implementing the declaration. In relation to the above principle, DAS has set forth three indicators, which are that:

- the Malawi Growth and Development Strategy (MGDS) should be in place and publicly launched;
- sector strategies should be in place and aligned to the MGDS; and
- that the 2007/2008 budget should reflect the MGDS priorities and be organised to allow easy identification of MGDS themes and sub-themes.

Government approved the final version of the MGDS in September 2006 and this has been posted on the government website. The Ministry of Economic Planning and Development is publishing it for wide distribution. But it has not yet been officially launched. According to the 2006 Annual Debt and Aid Management Report, some sector strategies or sector plans are in place, but many are not aligned to the MGDS. Furthermore, a Charter of Accounts has been drafted and is being reviewed to assess compatibility with the Integrated Financial Management Information System (IFMIS). But no resource envelope has been enumerated for the MGDS and a further round of prioritisation is widely considered necessary. Therefore, the MGDS is still being operationalised.

The main problem here is inadequate capacity in terms of skills and numbers of personnel in the government. In order to address the problem of inadequate capacity, job descriptions will be revised to fit the new financial management systems, and technical assistance will be used as a stop gap (5).

The Paris Declaration indicators concerning the second part of the above principle, which concerns donors, are:

- Reliable country systems in the form of procurement and public financial management (PFM) systems that either (a) adhere to broadly accepted good practices or (b) have a reform programme in place to achieve these.
- Alignment of aid flows to national priorities.
- Strengthening of capacity by support provided through coordinated programmes consistent with the partners' national development strategies.
- Use by donors and aid flows of partner country procurement systems, which either (a) adhere to broadly accepted good practices or (b) have a reform programme in place to achieve these.
- Use of country public financial management systems, which either (a) adhere to broadly accepted good practices or (b) have a reform programme in place to achieve these.
- Strengthening capacity by avoiding parallel implementation structures.
- Aid is more predictable.
- Aid is untied.

The DAS indicators for this are:

- The percentage of donor funds that are administered outside government procurement and financial systems.

- Elimination of Project Implementation Units (PIUs) except in defined circumstances.
- Alignment of Country Assistance Strategies to the MGDS, as verified by the Ministry of Economic Planning and Development and the Ministry of Finance.
- Narrowing of inter-thematic funding gaps for the MGDS Priority 1 activities.
- Increased flexibility within donor funding cycles.
- More predictable aid as indicated by the percentage of aid disbursed according to previously agreed schedules.

The relevant targets for these and other indicators are in the Annex to this study.

Current donor practices are mixed. Some funds are channelled through government. Other funds are not channelled through government. France does not channel funds through the government budget. Germany channels some funds through the government. Most of the aid from the EU, Britain and Sweden is channelled through the government. All the bilateral donors mentioned above use the public financial management and procurement systems, but not for all of their aid. The PFM system is said to be comparatively weak. The procurement system only partially achieves the Joint Roundtable on Procurement Assessment criteria. But all donors believe that both the PFM and procurement systems have improved since the current government took over power in 2004. Their confidence in them has thus increased. The Audit Function of government has been strengthened, but more needs to be done.

The main obstacle to greater alignment to government procedures and systems is the slow implementation of public sector management reforms, which is partly due to inadequate technical capacity. As a result of this, donors often insist on conditionalities that are inconsistent with national procedures, thus undermining alignment to government systems. Another obstacle is the inflexibility of donor processes, which make alignment more difficult. The DAS has called upon the government to implement the Public Financial and Economic Action Plan, to make key public sector management reforms and to undertake a programme of capacity development. Donors will be required to channel more aid through the budget process, to use national systems and procedures, to orient Country Assistance Strategies towards the MGDS and to follow multi-year indicative financial plans.

The EU's country assistance strategy is aligned to the MGDS. Britain is drafting a new country assistance strategy that will be aligned to the MGDS. Sweden does not prepare a country assistance strategy. Instead, it operates through a Memorandum of Understanding (MOU). The other bilateral donors are in the process of preparing their country assistance strategies. On capacity building support or Technical Assistance, there is little coordination between donors. Only 12 percent of capacity development support is provided through coordinated programmes. The absence of a Technical Assistance Policy in the Malawi Government implies that its impact is neither measured nor evaluated.

Most of the aid flows fit under the MGDS themes and most if not all government-administered aid is in the 2006/07 budget. However, this does not imply close alignment with the MGDS activities. According to an International Monetary Fund (IMF) estimate, only 50-70 percent of support to government is in the budget.

One possible explanation for lack of greater alignment to MGDS activities is that donors have raised questions about certain aspects of the MGDS. They believe that it lacks adequate prioritisation. They are of the view that the inclusion of a budget that looks like a medium term expenditure plan is inappropriate as no one can budget accurately budget government expenditure five years in advance given uncertainties about future movements of prices and exchange rates. Some donors have also questioned the desirability of the Shire-Zambezi Waterway. These concerns do not amount to questioning the credibility of the MGDS. Nevertheless, government intends to address them by reprioritising the MGDS after launch and carrying out further consultations and hold seminars with stakeholders to improve advocacy and support for the strategy.

There are at least 250 active foreign-financed projects in Malawi. Most of these projects use parallel implementation structures. All the five bilateral donors covered in this study use parallel implementation structures for some of their assistance. The Debt and Aid Management Division (DAD) will establish a baseline in conjunction with the Ministry of Economic Planning and Development (MEPD) for their elimination.

Current funding gaps for MGDS Priority 1 activities are nil for Sustainable Economic Growth, K1 billion for Social Protection, K 68 billion for Social Development, K 31 billion for Infrastructure, and K8 billion for Good Governance, giving a total of K108 billion for all themes.

**Table 1 Funding Gaps for the MGDS Priority 1 Activities**

	Total Budget (K billion)	Funding Gap (K billion)	Gap/Budget Percent
Sustainable Economic Growth	42	30	71
Social Protection	23	1	4
Social Development	70	68	97
Infrastructure	33	31	94
Good Governance	18	8	44
<b>TOTAL</b>	<b>186</b>	<b>108</b>	<b>58</b>

**Source: MGDS 2006-11**

As regards increased flexibility within donor funding cycles, practices vary among donors. Some donors, such as DfID and Sweden, are very flexible. They are able to bring disbursements forward from one financial year to another. The EU is not flexible. About France and Germany we do not know, as we do not have information on them. Those that are not flexible stick to their procedures and provide no room for changes. Similarly, regarding predictability of aid, practices vary among donors, as pointed out above, and according to mode of support. Some donors do not provide schedules for disbursements. And concerning tied aid, only EU funding for balance of payments support is explicitly tied to conditions. For projects, some donors disburse only after certain conditions have been met.

## 5.0 Country-led Partnership

The Paris Declaration principle on harmonisation states that donors will aim to be more harmonised, collectively effective and less burdensome and to establish common arrangements at country level for planning, funding and implementing development programmes. The Paris Declaration indicators for this principle are two. One, the use of common arrangements or procedures, as validated by the percentage of aid provided as programme-based approaches. Two, shared analysis, as validated by the percentage of (a) field missions and/or country analytic work, including diagnostic reviews carried out jointly.

DAS has a more comprehensive set of indicators. These are:

- Harmonisation of development partners project annual work plans, including monitoring and evaluation systems and their alignment to the MGDS monitoring requirements.
- Holding of a Joint Country Programme Review (JCPR) every year, and linking annual sectoral reporting to the JCPR.
- Holding of annual sectoral reviews to feed into the JCPR process.
- Percentage of missions that are joint between four or more development partners.
- Formulation of an annual development calendar to which development partners stick.

According to interviews conducted with representatives of donors for this study and other information, the EU, Britain and Sweden disburse aid through a programmed approach in the form of budget support, Health SWAP and National Aids Commission (NAC). France and Germany do not. Budget and corresponding balance of payments support is from the EU and Britain only, among the bilateral donors in question. Aid for the Health SWAP is from Britain only. Otherwise, all the bilateral donors covered in this study, with the possible exception of France, take part in some joint missions and some joint analytical projects with other donors. In addition, all the five bilateral donors have their own monitoring and auditing requirements. The EU admitted that it has a project cycle fixed for a multi-year period. So does Sweden.

The above findings are consistent with those of a baseline assessment of progress made by the Debt and Aid Management Division of the Ministry of Finance using the Paris Declaration indicators, which shows that only 22 percent of the aid is disbursed as a programme-based approach and that only a handful of donors provide balance of payments support. Also few donors contribute basket funds for the Health SWAP. Project support is predominant. Furthermore, the baseline assessment, which uses information on the number of missions, shows that few joint missions or joint analytical projects are carried out. To be specific, only 16 percent of missions are joint between two or more donors or by one donor on behalf of others; and only 17 percent of country analytic work is done by two or more donors or by one donor on behalf of others.

The baseline assessment based on the DAS indicators, also carried out by the Debt and Aid Management Division of the Ministry of Finance, has come up with similar results. It states that none of the donor actions is currently aligned to MGDS systems. The first Joint Country Programme Review was held in 2006. As far as annual sector reviews are concerned, those sectors that have annual reviews are not synchronised. Other sectors have no annual reviews at all. Some missions are joint between two or more development partners, but none are joint between four or more. Lastly, no annual development calendar is in place. However, a draft has been prepared. It is planned to launch this in June 2007. The calendar will specify quiet periods and busy periods.

The obstacles to operationalising this norm or principle are found on the sides of both donors and the government. All the five bilateral donors have their own monitoring and auditing requirements imposed by their governments. These differ among donors, thus impeding harmonisation. In addition, the EU and Swedish project cycles have already been fixed for a multi-year period, stating when reviews are required. As a consequence, the EU and Sweden are continuing individual monitoring exercises in parallel to the JCPR.

Government has not acted decisively to guide donors and encourage harmonisation. Then, there is the problem of perceived weakness of domestic systems and lack of technical capacity in some ministries to organise sufficiently robust annual reviews.

On the donors' side, the required actions include moving towards standard systems of reporting on aid programmes and projects to government by all donors; refraining from undertaking individual reviews in addition to the JCPR/MGDS Annual Review by all donors; disbursing aid through programmed approaches by France and Germany; and increasing the number of donors that undertake joint missions and analytical work to a minimum of four countries. On its part, the government should improve its monitoring and evaluation systems for the MGDS; agree on a standard common framework for monitoring of aid programmes and projects; strengthen economic governance and public sector reform programmes; and produce guidance to facilitate harmonisation of processes.

Some donors do not consult civil society, others do. For example, Swedish aid does not consult civil society organisations. Britain too does not consult civil society organisations, but it intends to start doing so. The EU consults civil society organisations through two channels. Every six months, it holds meetings with civil society organisations in the regional capitals of the country to discuss the country allocation with them. And every year, it holds consultations with a smaller number of civil society organisations on the way EU aid has been implemented. All donors are urged to consult CSOs on aid matters.

Similarly, some ministries do not consult civil society organisations (CSOs). These ministries are urged to consult them. Of the ministries that consult CSOs, the Ministry of Health allows civil society organisations to serve on technical working groups of the Health SWAP. The Debt and Aid Management Division of the Ministry of Finance consults the Malawi Economic Justice Network (MEJN), as does the Common Approach to Budget Support (CABS). The view of MEJN is that aid issues should be taken seriously, that government needs a clear aid and debt policy and that the government and donors should fast track implementation of the provisions of the Paris Declaration. While it welcomes the Development Assistance Strategy (DAS), MEJN believes that it is important for the government and donors to commit themselves to its speedy and full implementation. The Ministry of Finance consults other civil society organisations like the Economics Association of Malawi (ECAMA); however, the consultations relate more to budget matters than to issues of aid coordination, and take place at scheduled seminars on the budget.

## 6.0 Results Orientation And Mutual Accountability

Results orientation means managing for results. Aid should be implemented in such a way as to ensure that it has an effective impact on those whom it is intended to benefit. This requires monitoring for targets and results. Mutual accountability for development results means that both donors and government should be answerable for results being monitored. Developing country governments spend more time being accountable to donors than to their own people. Implementing joint accountability systems can help to reduce this problem

The relevant Paris Declaration principle states that both donors and partner countries should improve decision-making for results and donors should support efforts by developing countries in improving performance assessment that measures progress. A related principle is that donors and developing countries should pledge that they will hold each other mutually accountable for development results based on the above principles and develop aid coordination mechanisms.

The Paris Declaration indicators for these principles are two. First, results oriented frameworks, consisting of transparent and monitorable performance assessment frameworks to assess progress against (a) the national development strategies and (b) sector programmes. Second, mutual accountability as validated by the number of countries that undertake mutual assessment of progress in implementing agreed commitments on aid effectiveness.

The DAS stipulates that effective monitoring systems for the MGDS should be in place. These should consist of monitoring indicators; a management information system for monitoring inputs and outputs; and annual reports. It also stipulates that:

- An independent monitoring group should be empanelled to assess the implementation of the Paris Declaration and Development Assistance Strategy every two years.
- The JCPR should be held annually, with specific actions for both development partners and government to act on the further realisation of the Paris Declaration ideals.
- The Aid Coordination mechanisms proposed are meeting as scheduled.

All the bilateral donors on whom we have information, except France, welcome these principles. They believe that decision-making for results has improved on the part of the government. In varying degrees, they are supporting efforts by government to improve performance assessment. For projects, donor accountability is results oriented. But for programmes, donor accountability is outcome oriented. All bilateral donors, except France attended the 2006 Joint Country Programme Review. They welcome the establishment of aid coordination committees, which are the Donor-Government High Level Group, the Donor-Government Sector Level Group, the Internal Government Dialogue Group, the Joint Country Programme Review (JCPR) and the Donor-to-Donor Dialogue Group. They also favour the establishment of an independent aid-monitoring group (IMG). All these, of course, will result in an increase in the number of structures dealing with aid management.

A baseline assessment of the Paris Declaration indicators has concluded that some action has been taken. A monitoring framework for the MGDS is currently being established, but is not yet finalised; and some sectors have strategies. The baseline assessment has also pointed out that the Joint Country Programme Review held a meeting in 2006. This meeting brought together five development partners to review progress and challenges in a number of sectors.

The baseline assessment of the DAS has acknowledged that the first JCPR meeting was held in 2006. But it points out that work on indicators has begun, but they are not yet finalised; no management information system has been put in place yet; annual reports are not yet made; and that no monitoring group has been set up. On aid coordination mechanisms, it is saying that some sector level groups are already meeting regularly; for example, the Health SWAP.

The key obstacles to realising the principle of results orientation in Malawi include lack of sound analysis of target setting; and staffing shortages in the Ministry of Economic Planning and Development, which make effective monitoring and dissemination of information regarding targets difficult. Government needs to set realistic baselines and targets for national and sector strategies, and ensure that effective monitoring systems are put in place to follow up on these targets.

The main obstacle to realising the norm concerning mutual accountability is capacity constraint. Aid coordination meetings and annual reviews are resource intensive. And a lot of information will be required to create a league of donor performance. Well-functioning SAWPs would help, but there are not many in Malawi. The Joint Country Programme Review and the MGDS Review will promote mutual accountability, along with the sector reviews. So will the reports of the IMG. While a support project will address capacity constraints.

## **7.0 Conclusions And Recommendations**

### **7.1 Country Ownership - Systemic Procedural Issues**

Relatively little progress has been made so far in implementing in Malawi the global agreements to better harmonise and coordinate donor practices and procedures set out in the Paris declaration. Comparatively little progress has also been made towards achieving the various ideals of the Paris Declaration. Much remains to be done if the government is to have a complete picture of donor activities in Malawi; and it will take further effort to provide the kind of country leadership that has been shown in other countries to be needed to make progress in better coordinating and harmonising donor practices and procedures.

That said, Malawi has laid the groundwork for implementing the Paris Declaration on Aid Effectiveness. It has strengthened the Debt and Aid Management Division of the Ministry of Finance by recruiting additional professional staff. This division has led the formulation of the DAS as the instrument for implementing the Paris Declaration. Drawing on the Paris Declaration, the DAS spells out the goals that the government and donors must pursue, the actions that they must take to achieve those goals, and specific targets that must be met at particular time periods. Among other things, the DAS also sets out the mechanisms for better aid coordination.

The government has also formulated a comprehensive development strategy known as the Malawi Growth and Development Strategy (MGDS) as a basis for all development efforts in the country. Although donors have raised some concerns about aspects of the strategy, they have not questioned its credibility. The EU has already aligned its country assistance strategy to it. Donors that have not yet aligned their country assistance strategies to it, intend to do so once they have completed preparing their assistance strategies. On its part, the government must expedite the launch of the MGDS, carry out further prioritisation and hold more consultations and seminars with stakeholders to popularise it and garner support.

All donors have aligned some but not all of their assistance to government procurement and public financial management systems. The main obstacle to greater alignment to government procedures and systems is the slow implementation of public sector management reforms, which is partly due to inadequate technical capacity. Another obstacle is the inflexibility of donor processes, which make alignment more difficult. Government is urged to implement the Public Financial and Economic Action Plan, to make key public sector management reforms and to undertake a programme of capacity development. France is urged to channel its funds through the budget. Germany is urged to channel more of its aid through the budget. All donors are urged to make more use of national systems and procedures, to follow multi-year indicative financial plans and to eliminate parallel implementation structures. The EU is urged to be flexible in its aid operations.

### **7.2 Country Led Partnership**

Unlike the EU, Britain and Sweden, France and Germany do not disburse any of their aid through a programmed approach. The latter countries are urged to provide their support through a programmed approach. While all donors, with the possible exception of France, take part in joint missions and analytical studies, they do not use the minimum number of four countries. Hence, they are urged to involve more countries in their joint missions and analytical studies.

The investigation that has been carried out has also revealed that all countries have their own monitoring and auditing requirements, implying that they carry out individual reviews; and that the EU and Sweden have project cycles for fixed time periods. Donors are urged to use standard systems for reporting on aid programmes and projects, and to refrain from mounting individual reviews in addition to JCPR/MGDS Annual Reviews. On its part, the government is urged to improve monitoring and evaluation systems for the MGDS, agree on a standard common framework for monitoring aid programmes and projects, and to produce guidelines to facilitate harmonisation of donor procedures.

### **7.3 Results Orientation and Mutual Accountability for Development Results**

Germany, Britain, the EU and Sweden all welcome the principles of management for results and mutual accountability. They believe that decision-making for results has improved on the part of the government. In varying degrees, they are supporting efforts by government to improve performance assessment.

But, their approach to accountability differs between projects and programmes. For projects, donor accountability is results oriented. While for programmes, it is outcome oriented and so it is not consistent with the Paris Declaration. It is recommended that all bilateral donors should make accountability for programmes results oriented.

The baseline assessments of the Paris Declaration indicators and the DAS have concluded that some action has been taken. A monitoring framework for the MGDS is currently being established, but is not yet finalised; and some sectors have strategies. The baseline assessments have also pointed out that the Joint Country Programme Review held a meeting in 2006 to review progress and challenges in a number of sectors. However, it has been noted that no management information system has been put in place yet; annual reports are not yet made; and that no monitoring group has been set up. On aid coordination mechanisms, it is saying that some sector level groups are already meeting regularly; for example, the Health SWAP.

Among the obstacles to realising the principle of results orientation in Malawi include lack of sound analysis of target setting; and staffing shortages in the Ministry of Economic Planning and Development, which make effective monitoring and dissemination of information regarding targets difficult. Government needs to set realistic baselines and targets for national and sector strategies, and ensure that effective monitoring systems are put in place to follow up on these targets.

The main obstacle to realising the norm concerning mutual accountability is capacity constraint. Aid coordination meetings and annual reviews are resource intensive. And a lot of information will be required to create a league of donor performance. Well-functioning SAWPs would help, but there are not many in Malawi. The Joint Country Programme Review and the MGDS Review will promote mutual accountability, along with the sector reviews. So will the reports of the IMG. While a support project will address capacity constraints.

## **Annex 1 Detailed Methodology**

The methodology for this study has consisted of a desk study and interviews with key stakeholders. The principal researcher has carried out extensive review of existing literature on aid effectiveness and harmonisation. Some of the literature that has been consulted is general in character. Other literature is specific to Malawi. Some of the literature is official in nature. Other literature is non-official. In addition, the principal researcher has conducted interviews with officials in the Ministries of Finance, Economic Planning and Development and Health responsible for aid and debt management; and with representatives of DfID (a British aid agency), the European Union Delegation and the Norwegian Embassy, which handles Swedish aid in Malawi. GTZ (a German aid agency) declined our request for an interview. France does not have an embassy in Malawi. So no interview with it was arranged. He has also conducted interviews with representatives of four civil society organisations; namely, Economics Association of Malawi (ECAMA), Centre for Social Concern, Centre for Social Research and the Malawi Economic Justice Network (MEJN).

## Annex 2 MGDS Targets

- i. The MGDS is approved formally by Cabinet by December 2006, and formally launched by end-January 2007. Baseline: Comments from Cabinet have been received and are being incorporated, but the MGDS has not yet been launched)
- ii. The key priorities and activities for sector strategies, including Education, Agriculture, Infrastructure and Irrigation and Water Development have been agreed with MEPD and MOF by June 2007. Baseline: Some sector strategies or sector investment plans are in place, but some are not closely aligned to the MGDS
- iii. A concept note is produced by February 2007 for tracking expenditure against the MGDS, with a dry run of the system conducted in April 2007. Baseline: A Charter of Accounts has been drafted and is being reviewed to assess IFMIS compatibility. If instituted, the new accounts system will allow expenditure on activities to be tracked.
- iv. If PFEM Priorities are implemented within 12 months: · A two thirds reduction in aid flows that do not use country PFM systems by 2011· A two thirds reduction in aid flows that do not use country procurement systems by 2011 If PFEM Priorities are not implemented within 12 months· A one third reduction in aid flows that do not use country PFM systems by 2011· A one third reduction in aid flows that do not use country procurement systems by 2011 Aid flows measured by volume of aid. Baseline: Current practices are mixed. Even those donors who channel funds through Government make conditions on processes that need to be used for procuring goods.
- v. If PFEM Priorities are not implemented within 12 months· A one third reduction in aid flows that do not use country PFM systems by 2011· A one third reduction in aid flows that do not use country procurement systems by 2011 Aid flows measured by volume of aid. Baseline: Current practices are mixed. Even those donors who channel funds through Government make conditions on processes that need to be used for procuring goods.
- vi. By 2011 no PIUs are in place except for SWAPs (i.e. one implementation structure for the whole sector) and for large projects (DAD to set the cut-off line for size. Baseline: Not yet determined.
- vii. 100% of CASs are assessed by MoF and MEPD as aligned to the MGDS. A definition of what constitutes alignment is required from MEPD. Baseline: No active CASs are currently aligned, as the MGDS has only been available in draft form for a limited period of time.
- viii. By the 2007/08 budget, no MGDS theme has a funding gap of more than 50%. Baseline: Current P1 gaps for all five years: Sustainable Economic Growth - K 30 billion; Social Protection - K 1 billion; Social Development - K 68 billion; Infrastructure - K 31 billion; Good Governance - K 8 billion; All Themes - K 108 billion
- ix. All donors provide information on their spending plans for the 07/08 using the Malawi fiscal calendar to calculate projections. Baseline: Practices are varied. Some donors, such as DfID are very flexible, able to bring disbursements forward from one financial year to another. Others are required to follow procedures and provide no leeway for changes. The following donors provided information for 2006/07: EU, DFID, World Bank, ADB, UNDP, JICA, GTZ, KfW, USAID, Norway
- x. All donors pledge by the end of April what they plan to disburse in the next financial year (and beyond if possible); (2) The actual pattern of disbursements compared to pledged funding should not vary by more than 50%. Baseline: Practices are varied. Some donors do not provide schedules for disbursements
- xi. After 1 year (by December 2007), all are harmonised to match MGDS requirements. Baseline: None are currently aligned to MGDS systems, which are still being finalized
- xii. The JCPR / MGDS Annual Review is held each year in March. Baseline: The first JCPR was held in 2006.
- xiii. Each sector review is completed by February each year, to feed into the JCPR / MGDS Annual Review. Baseline: Varied - some sectors have annual reviews, but these are not synchronized. Others have no review at all
- xiv. (1) By 2008, all missions looking at sector wide issues should be conducted jointly between all the development partners active in the sector. (2) By 2011, 50% of all missions are joint between four or more development partners. Baseline: Some missions are joint between two or more donors, but none are joint between four or more.

- xv. By end-January 2007, DAD develop a development calendar, governing the timing of missions and stipulating 'quiet periods'. Baseline: No such calendar yet exists.
- xvi. Effective monitoring systems for the MGDS are in place by December 2006: (1) Monitoring indicators are in place by December 2006; (2) A management information system, monitoring inputs and outputs towards targets, is in place by December 2006; (3) Annual reports are released by January each year. Baseline: Work on indicators has begun, but they are not yet finalised. No management information system, specifying the data and collection procedures, has been put in place yet Annual reports not yet made, though these are planned. Formats not usually decided until the report is drafted.
- xvii. A baseline report of the Independent Monitoring Group to be disseminated by February 2007. Baseline: The group have been empannelled to undertake a baseline survey
- xviii. The JCPR is held each year in March. Baseline: The first JCPR was held in 2006. Baseline: The first JCPR was held in 2006.
- xix. An annual mutual assessment of progress in implementing agreed commitments on aid effectiveness is undertaken through the JCPR (Paris Declaration Indicator 12). Baseline: No such assessment is currently made.
- xx. Formulate new SWAPs in 3-4 key sectors by January 2008. Baseline: SWAPs are being prepared in Agriculture, Roads, Education and Irrigation and Water Development, though these are at different stages of their development.
- xxi. A baseline league table on donor performance is produced for the 2006/07 Annual Debt and Aid Report, and updated annually. Baseline: No such table exists
- xxii. The Aid coordination mechanisms, consisting of a Donor-Government High Level Group, Donor-Government Sector Level Groups, an Internal Government Dialogue Group, Joint Country Programme Review (JCPR)/MGDS Annual Review and Donor-to-Donor Dialogue Group, are meeting to schedule. Baseline: The High level coordination meeting is convening infrequently.

## **Annex 3 List of Institutions and Persons Interviewed**

### **Donors**

#### **DfID**

Mr. A. Whitworth, Economic Adviser

Mr. B. Sanchez, Economist

#### **EU**

Mr. J. Ponds, Head of Economics and Public Affairs Section

#### **Norwegian Embassy on Behalf of Swedish Aid**

Mr. L.B. Sauvik, Counsellor – Deputy Head of Mission

### **Ministries**

#### **Ministry of Finance**

Dr. A. Nyasulu

Dr. R. Dissanayake

Mr. Stan Nkata

#### **Ministry of Economic Planning and Development**

Mr. C. Chiunda

#### **Ministry of Health**

Mr. C. Moyo

### **Civil Society Organisations**

#### **Economics Association of Malawi**

Mr. G.H Thindwa

Centre for Social Concern

Fr. J. Kupens

Centre for Social Research

Mr. M. Tsoka

Malawi Economic Justice Network

Mr. M. Bamusi

## End Notes

(1) The exact title of this document and international agreements is the Paris Declaration on Aid Effectiveness: Ownership, Harmonisation, Alignment, Results and Mutual Accountability (available on [www.oecd.org](http://www.oecd.org)). It was endorsed on 2 March 2005 and is signed by 100 countries representing recipients of aid and donors and a number of international organisations.

(2) According to the 2006 Annual Debt and Aid Report, donors disbursed development support amounting to \$318.4 million in the 2004/05 financial year, and \$497.2 million in the 2005/06 financial year. The projection for the 2006/07 financial year is \$466.9 million. These figures do not represent the total amount of development support. Some donors did not submit figures. Therefore, the data are underestimates.

(3) As stated in the same document, the 2006 Annual Debt and Aid Report.

(4) The biggest negative variances were associated with the ADB (65 percent), KfW (38 percent), JICA (22 percent), EU (19 percent), and Norway (10 percent). The biggest positive variances were associated with the World Bank (108 percent) and USAID (23 percent).

(5) This is a matter of concern to the extent that trade and private sector development is a priority activity. But the nature of the activity of promoting this development may not easily lend itself to support from donors.

(6) UNDP, Malawi's Partners in Development Profiles of Donors and Programmes, March 1998.

(7) Malawi Government, 2005 Economic Report.

(8) National Action Group Forum, "The IMF - Government of Malawi Agreement 2005-2008", August 2005.

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