Policy Recommendations and Options: Harnessing Sovereign Wealth Funds for Sustainable Economic Development in Africa

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On June 14 2016, the Wilson Center hosted the second annual Signature Event of the Brown Capital Management Africa Forum, “Long-Term Sustainable Development in Africa: The Role of Sovereign Wealth Funds.” This event explored the rise of sovereign wealth funds (SWFs) in Africa, including their various roles, their governance and management, and how well SWFs have performed toward achieving their long-term development, economic stabilization, and savings goals. The speakers offered recommendations to public and private stakeholders on how to more effectively manage SWFs and support long-term sustainable development in Africa.

Speakers included: Mr. Andrew Baukol, Principal Deputy Assistant Secretary for International Monetary Policy, United States Department of the Treasury; Mr. Walé Adeosun, CFA, Founder and Chief Investment Officer, Kuramo Capital Management and Member, President’s Advisory Council on Doing Business in Africa; the Honorable Mona Quartey, Deputy Minister of Finance, Republic of Ghana; Mr. Uche Orji, CEO and Managing Director, Nigeria Sovereign Investment Authority; Mr. Malan Rietveld, Director, Kalytix Partners and former Director, Investment Institute, Investec Asset Management;
Sovereign Wealth Funds in Africa: Progress Made and Recommendations for the Way Forward

Sovereign wealth funds—state-owned investment vehicles that are often funded with revenue from oil or other natural resources—have been on the rise in Africa. At least 14 African countries currently have SWFs and another 10 or so countries are in the process of establishing one. SWFs play a variety of roles including economic stabilization, saving for future generations, and pursuing long-term development, all of which are critical goals for many African countries.

Key recommendations and considerations for managing a successful SWF include the following:

1. Determining the Purpose of the SWF

State-sponsored investment funds vary widely, with diverse legal, institutional, and governance structures. A key factor underpinning a successful SWF is the articulation of clear objectives that are in alignment with the particular needs of an individual country and the context within which the fund will operate. For example, stabilization funds—designed to provide stability through commodity price fluctuations and cycles—may be most appropriate in natural resource rich countries.

Ghana has two funds which were established with clearly delineated purposes: the Ghana Stabilization Fund serves as a contingency fund for unplanned government expenditures when oil prices are low, while the Ghana Heritage Fund seeks to achieve intergenerational equity by providing an endowment for future generations. Determining the particular objectives, appropriate structure, and subsequent management strategy of its SWFs has helped Ghana to both soften the impact of the recent crude oil price decline and to target development objectives, including the Sustainable Development Goals, while also saving for future generations.

Key recommendations and considerations:

- Governments should articulate clear policy and goals prior to the creation and launch of the fund. Goals can include infrastructure development, stabilization, or investment for future generations.

- Governments should avoid complicated investment strategies in favor of simplicity, particularly in the early stages of an SWF’s existence. This helps to reduce human capital and operational capacity gaps.
Governments should first aim to focus on a medium- to long-term investment framework, and on making investments with long maturity periods.

2. Enhancing Measures of Transparency and Accountability

Ensuring proper and effective oversight over decision-making and building a reputation for transparency and accountability in SWF management are critical components for maintaining efficient, reliable operations. Adherence to global best practices help African governments signal their commitment to high standards of predictability, openness, efficiency, and sound financial management. Additionally, international public scrutiny incentivizes regulatory compliance. SWFs and governments need to prioritize and operationalize accountability through timely, comprehensive, and accurate information sharing.

Key recommendations and considerations:

a. SWF managers should clearly articulate the goals and objectives of their SWFs; the process and procedures for how SWF monies will be accessed; and the distribution of roles and responsibilities within the organization.

b. SWFs should adhere to the Santiago Principles, which recommend transparency, sound governance structures, and mechanisms that provide operational controls, risk management, and accountability. To this end, SWF managers should provide comprehensive information including operations reports and audits, a run-down of activities, investment reports, and staff compensation and overtime pay.

c. SWF managers should seek to provide comprehensive information in a way that is easily accessible to the public, including on the Internet.

d. SWFs should also conduct due diligence and engage only partners with integrity and credibility in order to avoid the influences of corruption.

3. Minimizing Political Interference in the Management of SWFs

Determining national investment on a commercial basis is a difficult task. It requires finding a balance between avoiding political interference in investment decisions while remaining accountable to politicians and the public. Commercial-based investment frameworks help facilitate the growth of SWFs over time, and funds that face less political interference are more likely to have higher long-term returns.

The Nigeria Sovereign Investment Fund (NSIA), for example, is not part of the government’s fiscal framework, but rather is managed by an independent and highly engaged oversight board with demonstrable professional capital investment experience. This structure has proven critical for maintaining institutional integrity and enforcing clear rules about when and how the government can request funds from the SWF.

Key recommendations and considerations:
a. Governments should set strong oversight standards and procedures for SWFs.

b. SWFs should clearly articulate the rights and responsibilities of the fund-sponsoring authority, its governing board, and its management team.

c. SWFs should establish robust processes for the appointment and removal of board members.

4. Understanding the Limitations of Sovereign Wealth Funds and Developing SWFs within Integrated Financial Management Frameworks

SWFs offer a significant opportunity for sustainable development in Africa. However, a SWF is only one tool for economic development, and policymakers should not overestimate the ability of SWFs to solve all development challenges. As such, it is critical that SWFs are crafted within the larger context of comprehensive, integrated fiscal policy and resource management frameworks. In this regard, SWFs in Africa vary widely. The Angolan SWF, for example, is not integrated into the national budget nor does it have a stabilization function. The Ghana Petroleum Funds, in contrast, are integrated into the budget and are a crucial part of how the country manages its natural resource revenues over time.

Key recommendations and considerations:

a. Governments should seek to utilize SWFs as a fiscal tool and acknowledge that SWFs are one piece of a larger resource management strategy, particularly in resource-dependent countries.

b. Governments should focus first on developing a medium- and long-term fiscal framework and identifying the role of the SWF therein.

c. Governments should take advantage of periods during which commodity prices are low to lay the groundwork for establishing an SWF.

d. SWF development must be paralleled by the promotion of economy-wide good governance and the implementation of strong overall public finance management systems.

5. Engaging Public and Private International Actors

International actors and third-party managers, such as private asset managers, are indispensable for increasing Africa's capacity to manage and invest capital. An international presence can lower investment risks, yield premiums on foreign investments, and bolster institutional capacity. International actors can also serve as mentors or (customizable) models to SWF. Using models and mentors in the process of building institutional frameworks can help to reduce the human capital demanded by a young SWF. Additionally, the presence of the right international actors can incentivize better practices to promote transparency and accountability.

Foreign governments, international financial institutions, and independent fund managers can potentially contribute to the success of African SWFs by:
a. Supporting projects for professional capacity building, asset management, peer review, networking, and knowledge-sharing.

b. Enforcing prudent policies and providing support in addressing transparency concerns, particularly in regard to illicit financial flows.

African SWF managers can most effectively engage international actors by:

c. Adopting internationally accepted best practices, such as the Santiago Principles.

d. Clearly demonstrating a sound framework for the segregation of duties in the management of SWFs between various domestic and international agents. This will help increase investor confidence and attract international investment.

e. Determining the most investable sectors in the SWF host country, based on the priorities of the national economy and the ability for the investment to generate commercial and social returns.

f. Partnering with other SWFs through the creation of co-investment funds, which can inform better decision-making, encourage peer review and knowledge sharing, and provide financial support for SWFs, particularly those that are still in the early stages of development.

To watch the full video recording of the event, please visit: https://www.wilsoncenter.org/event/long-term-sustainable-development-africa-the-role-sovereign-wealth-funds


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