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Economic Governance in the SADC Region: Institutions and the Development State

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[1] The views expressed are those of the author and should not be attributed to United Nations Economic Commission for Africa (UNECA).

Introduction

This paper seeks to assess and analyze the implementation and operationalization of core areas of economic governance by SADC member countries. Its point of origin is that indeed the "development state" is an approach, aspects of which can be emulated by African countries, as they ponder their development paths and strategies to achieve sustainable and inclusive growth and development, and structural transformation.

In both the policy and academic fields, a well-known argument is that given the divergence in development between countries in sub-Saharan Africa and those of East Asia and the Pacific, the two regions having displayed comparable standards of living in the 1960s and 1970s, there could be lessons learned. A number of factors are presented to explain and account for this divergence including the role of public sector institutions. The SADC region is now as of June 2015, a part of a larger Tripartite Free Trade Area integrating the three 26 member country trade blocks of COMESA, EAC. An awareness of its own situation, when it comes to the quality and strength of institutions and governance can help shape decisions on institutional choice, going forward.

The paper will start by explaining the specific aspect of the development state that contributed to. It will then define and explain the importance of economic governance to structural transformation, while also providing data on the state of governance in SADC. It will then seek to use secondary data and information, collected by other entities, to assess and analyze progress by SADC member countries in the implementation of core areas of economic governance.

The Development State and Institutional Development

The "development state" approach is one that is deemed as necessary for the role that the state can play in economic transformation (UNECA, 2011:83). This approach is widely acknowledged as having contributed to the positive growth performance of countries in Asia and Latin America, including in South Korea and Brazil. Here, "the state puts economic development as the top priority of government policy, and is able to design effective instruments to promote such a goal" (UNECA, 2011:95). The formation of new formal institutions is one such instrument.

Institutions as the mechanisms of governance (UNECA, 2002), are also said to be "the fundamental cause of economic growth and development differences across countries (Acemoglu and Robinson, 2008). Based on a definition by North (1990), "institutions are the rules of the game in a society,…are the humanly devised constrains that shape human interactions" (Acemoglu, and Robinson, 2008: 2). Institutions are established by human beings and they can control human behavior through the distribution and control of incentives. From an economic perspective, institutions facilitate private investment and capital flows (UNECA, 2011:83), and they shape the actions of individuals, by defining and regulating through rules, norms and structures.

The economic functions of the public sector are influenced by the quality of institutions in a number of ways: they facilitate the making and implementing of economic policy including through the maintenance of fiscal and monetary discipline, macroeconomic planning and domestic resource mobilization; they help with the delivery of public services; institutional arrangements help with the monitoring and enforcement of rules that can ensure the accountability in the use of public resources, and also regulate the use of public power (World Bank, 2000). When institutions are strong, the intended outcomes of the roles stated above can also be positive.

In the literature, a notable explanation for the divergence in the growth trajectory between Africa South Korea, and other countries of East Asia is the quality of institutions (Presbitero, 2013; Rodrik, 2003; Mkandawire, 2001). During the period of 1960 and 1980 which saw exponential transformation in Korea, the government amplified institutional coherence through the creation of entities such as the Economic Planning Board to manage industrialization and also relations with business" (Chibber, 1999).

South Korea exemplifies a case of state capacity, through strong institutions, playing a major role in the economic growth of the country. It is often cited as an example of a “development state” (Chang, 2010) whose proactive government took deliberate strategic steps to tap into global markets and enhance social policy innovation that could then facilitate competitiveness. Specific sectors were favored and promoted, bureaucracies were streamlined through improved effectiveness and competency to facilitate national development plans which were often articulated with clear economic and social goals under the leadership of an activist government that placed economic development at the center of its national policy, planning and implementation.

In the SADC region, Botswana’s exemplary economic performance is explained by the role that institutions played. In the early 2000s, Botswana had had the highest per-capita growth of any country in the world during the previous three decades and the explanation is that “good policies were chosen in Botswana because good institutions, which we refer to as institutions of private property, were in place” (Acemoglu et al, 2003:).

Improving the capacity of all institutions, including those that in the areas of finance and commerce has to be prioritized. However, it is important to note that institution-building takes a long time (UNECA, 2015b:9); the contexts and needs of each country, also determine, the nature and type of any resultant institutions to be adopted (Chang, 2011). A country case-by-case assessment of needs and priorities can help with the process of deciding on options for institutional choice.

Economic Governance and Structural Transformation

Economic governance is the structure and practice of economic policy making and management (Henderson et al, 2002). In more concrete terms, good economic governance is about institutions of government having the capacity to manage resources efficiently; formulate, implement, and enforce sound policies and regulations; monitor and hold accountable; enforce the respect for rules and norms of economic interaction; and ensure that economic activity is unimpeded by corruption and other activities inconsistent with public trust” (UNECA, 2002: 2).

In Africa today, deficiencies in economic governance hinder macroeconomic stability, reduce accountability in the execution of public management functions and weaken the business environment and investment climate necessary for investment to happen, ultimately diminishing the ability of governments to implement development and poverty reduction policies that could facilitate improved standards of living.

Good economic governance (UNECA, 2002) is directly connected with the capacity of the state and all relevant actors to deliver on public goods in an inclusive and sustainable manner. Currently on the continent, the paradigm of structural transformation where resources and in particular new investments, are being channeled from low to high productive activities within and across sectors, (UNECA, 2015a), has been embraced by countries in their national development priorities and plans. Good economic governance ensures that institutional structures, rules and regulations that monitor and guide the functioning of the economy are in place, that they are enforced, and there are systems for ensuring accountability.

Economic governance is composed of core elements including *public financial management* and accountability, integrity of the *monetary and financial system*, and the *regulatory framework* (UNECA, 2002). While there are difficulties with measuring "governance" in general (Kaufman et al, 2009), good outcomes in these three areas underpin good economic governance.

The State of Governance in the SADC Region

The Ibrahim Index of African Governance (IIAG) is a resource for annual data on the quality of governance in Africa. Data is available from the year 2000 on four pillars including Safety and Rule of Law; Participation and Human Rights; Sustainable Economic Opportunity; and Human Development.

The categories have subcategories as follows: Safety and Rule of Law (Rule of Law, Accountability, Personal Safety and National Security); Participation and Human Rights (Participation, Rights, Gender); Sustainable Economic Opportunity (Public Management, Business Environment, Infrastructure, Rural Sector); Human Development (Welfare, Education, Health). These four categories and subcategories, each with indicators that measure an aspect of governance, which all then provide one overall measurement of governance performance for each African country. For economic governance, we will focus on performance in the subcategories of accountability, participation, public management and business environment.

<u>Table 1: Country-Specific Performance on Key Indicators of Economic Governance</u>

	Overall Governance		**Accountability**		**Participation**		**Public Management**		**Business Environment**	
	Rank	*Score*	*Rank*	*Score*	*Rank*	*Score*	*Rank*	*Score*	*Rank*	*Score*
Angola	44	40.9	48	15.5	34	34.8	41	40.5	42	30.6
Botswana	2	76.2	1	77.3	7	78.5	3	69.5	4	72.8
DRC	47	34.0	45	22.8	44	19.9	34	44.1	45	28.1
Lesotho	10	62.3	6	65.0	3	82.4	13	56.4	14	55.2
Madagascar	33	48.2	23	41.1	32	36.4	36	43.0	23	49.8
Malawi	16	57.6	13	45.3	17	64.2	30	47.0	24	48.7
Mauritius	1	81.7	2	74.6	2	83.9	2	70.5	1	90.4
Mozambique	22	52.2	28	36.7	20	60.7	16	55.2	30	45.7
Namibia	6	70.3	5	66.7	5	80.1	22	48.9	7	65.3
Seychelles	5	73.2	10	54.4	11	70.8	31	45.4	11	58.6
South Africa	4	73.3	4	67.4	4	81.1	1	74.5	3	77.6
Swaziland	24	51.5	12	47.2	50	11.9	23	48.9	17	53.9
Tanzania	15	58.2	24	39.9	15	65.5	15	55.2	19	51.3
Zambia	13	59.4	14	44.9	12	69.5	28	47.6	10	61.1
Zimbabwe	46	38.0	44	23.6	37	27.7	50	27.5	50	16.7
African Average										
Rank: Out of 52 countries										

Source: Ibrahim Index of African Governance (IIAG) 2014

Noting that the SADC region is made up of mostly countries from Southern Africa, this region is the best performer in overall governance according to the IIAG. Southern Africa ranks the highest in three of the four categories (Safety and Rule of Law, Participation and Human Rights, and Sustainable Economic Opportunity), with the exception of Human Development, for which it ranks second. For a total of five regions, Southern Africa ranks first in nine of the fourteen subcategories, including rule of law, accountability, personal safety, national security, participation, gender, public management, business environment, and welfare. Of the remaining five subcategories, the region ranks second for rights, infrastructure, education and health. It ranks fourth for rural sector. Countries, including Lesotho, Zambia, and Zimbabwe, have seen improvements in all the four categories. Only the DRC has seen deterioration in the subcategory of participation. Meanwhile, the top performing countries in overall governance seem to expose weaknesses, deteriorating in at least one category: Mauritius deteriorated in the category of Human Development; Botswana in Participation and Human Rights; Seychelles in Sustainable Economic Opportunity; and South Africa in Safety and Rule of Law, Participation and Human Rights; and Human Development.

From a continent-wide perspective, however, the subcategories of accountability and business environment have deteriorated the most, over the past five years. Explanations of this poor performance in the area of accountability, is as a result of weaknesses in all underlying indicators, with the exception of Public Sector Corruption Bodies (Global Integrity), which saw an improvement; These underlying indicators include: Accountability, Transparency & Corruption in the Public Sector; Accountability, Transparency &Corruption in Rural Areas; Corruption & Bureaucracy; Accountability of Public Officials; Corruption in Government & Public Officials; Prosecution of Abuse of Office; Diversion of Public Funds; Public Sector Corruption Bodies; and Access to Information. For the Business Environment, deterioration is explained by weaknesses in indicators among others, of soundness of banks and reserves. In the same category of Sustainable Economic Opportunity, the subcategory of Public Management deteriorated the most, following the Business Environment. The underlying indicators for this subcategory include: Competitive Environment; Investment Climate; Investment Climate for Rural Businesses; Rural Financial Services Development; Bureaucracy & Red Tape; Customs Procedures; and Soundness of Banks. This trend in deterioration, poses concern for economic governance.

Understanding Economic Governance: Accounting for Institutional Quality

Data on the core elements of economic governance 1) *public financial management* and accountability, integrity of the, 2) *monetary and financial system*, and 3) the *regulatory* *framework* can help to demonstrate how much progress has been made by countries in strengthening institutions.

This data is usually attained following an assessment of country implementation of specific aspects of standards and codes. According to the IMF, "'standards and codes' refers to sets of provisions relating to the institutional environment—the 'rules of the game'—within which economic and financial policies are devised and implemented. Countries whose institutions are well-regulated and transparent tend to demonstrate better economic performance and greater financial stability. It is thus in countries' own interest to adopt and implement internationally-recognized standards and codes" (IMF, 2015). Indeed, the IMF endeavors to collect data to ascertain institutional strength and effectiveness in economic and financial realms.

Public Financial Management (PFM): Effective PFM systems facilitate the efficient use of public resources. The IMF assesses PFM based on principles and practices of a good public financial management system that are stipulated in the IMF's Code of Good Practices in Fiscal Transparency. This Fiscal Transparency code is the international standard for disclosure of information about public finances (IMF, 2015). The code covers 4 key elements of fiscal transparency, including i) fiscal reporting; ii) fiscal forecasting and budgeting; iii) fiscal risk analysis and management; and iv) resource revenue management. The IMF's Code of Good Practices in PFM stipulates that the roles and responsibilities in government be clear; information on government activities should be provided to the public; budget preparation, execution and reporting should be undertaken in an open manner, and; fiscal information should attain widely accepted standards of data quality and be subject to independent assurances of integrity.

Monetary and Financial System: This element of economic governance is concerned with 1) the transparency of the monetary and financial system especially with regard to central banks and financial agencies; the 2) the independence of Central Banks to achieve stated monetary objectives alongside reasonable standards of accountability and transparency; and 3) the effectiveness of regulatory and supervisory institutions in the monetary and financial sector. Data to ascertain progress on elements 1 and 2 can be obtained from the assessments made through the IMF's Code of Good Practices on Transparency in Monetary and Financial Policies, where Good Transparency Practices for Monetary Policy by Central Banks, and Good Transparency Practices for Financial Policies by Financial Agencies are assessed (IMF, 1999). The 29 Core Principles for Effective Banking Supervision by the Basel Committee also include an assessment methodology covers element 3 above (BIS, 2012).

Regulatory Framework: Independent regulatory mechanisms help to assure stability in the regulatory environment, including the reducing of the risk that regulation may be misused to achieve short-term political ends and by fostering the development of regulatory expertise. Three major areas that have benefited and require improvement are in the areas of 1) securities (capital markets); 2) insurance and banking and monopolistic markets, including utilities. The International Organization of Securities Commissions has set out Objectives and Principles of Securities Regulation, including a Methodology for Assessing the Implementation of the IOSCO Principles. Regarding insurance regulation and supervision, the International Association of Insurance Supervisor's Insurance Core Principles, including also an assessment methodology can be referenced.

Data on the above 3 elements of economic governance is not in one place, for all SADC countries, over a multi-year time span. In the case of the IMF, assessments are usually undertaken at the request of Member States and therefore in the event that a country is not assessed, the data becomes unavailable.

As an alternative to unavailable data that is systematic, Table 2 provides information, based on IMF Article IV Country Reports, on some of the areas in which each SADC member countries has to make improvements.

According to Country Reports of Article IV Consultations, each country is given specific advice on recommendations for improvement as seen in Table 2. Botswana and Mauritius are noted as countries with strong institutions. The IMF notes that available data is adequate in the two countries. However, where there are shortcoming in terms of accuracy and reliability of the source of data and statistical techniques in compilations, the governments are trying to address them. The need to strength economic data is also stressed for Mozambique, South Africa, Namibia, Zambia. For South Africa, the regulation and supervision of banks and insurance are found to be sound, although reforms in the regulatory architecture is advised. On the other hand, countries including Angola, the Democratic Republic of the Congo (DRC), Lesotho, Madagascar, Swaziland, Tanzania, Zambia, and Zimbabwe, are strongly encouraged to make sweeping improvements in the three areas of economic governance, including with the *public financial management* system, the *monetary and financial system*, and the *regulatory framework*.

The Article IV Country Report for Malawi and Seychelles are good examples, providing information on improvements that have been made in observing some of the codes and standards with macroeconomic rationale. For example, in order to promote competition and transparency in the banking system, as is required by the IMF’s Code of Good Practices on Transparency in Monetary and Financial Policies, the Central Bank of Seychelles, had been able to publish a commercial bank supervision report. In order to strengthen budget preparation as stipulated in the IMF’s Code of Good Practices in Fiscal Transparency, Seychelles had introduced budget submissions protocols and procedures.

Along the lines of exemplary countries whose successes could be emulated in the region include Mozambique. Following over a decade of reforms in PFM, Africa has generated mixed results. A study (Andrews, 2010) finds that “budgets are made better than they are executed, practice lags behind the creation of processes and laws, and processes are stronger where concentrated actors are engaged. In respect of the latter, the study finds that different countries fall into different ‘PFM performance leagues’ and countries in the different leagues look very different to each other. A range of factors influence which league a country is associated with; including economic growth, stability, reform tenure and colonial heritage. Mozambique is known to have created a link between planning and budgeting, setting the foundation for further reform.

Table 2: Economic Governance in SADC Region: Country-Specific Recommendations

	Public Financial Management	Monetary & Financial System	Regulatory Framework
Angola (2014)	Further improve public financial management systems to avoid, inter alia, a recurrence in the future of domestic payments arrears.	Enhance the central bank's capacity to collect and analyze high-frequency economic data, and continue de-dollarizing the economy. Further strengthen the financial system, by continuing to improve the transparency and accountability of banks, and enhancing bank supervision.	Continue improving the business climate to boost economic development, diversification, and competitiveness.
Botswana (2014)		The timeliness of the central bank survey and detailed government expenditure data by economic classification needs to be increased to better support economic analysis and prepare Botswana for an eventual subscription to the Special Data Dissemination Standard (SDDS). Further improvements would include dissemination of readily available information on monthly production of diamonds and quarterly aggregate financial soundness indicators.	
DRC (2014)	Maintain the fiscal anchor of no (net) central bank financing of the budget while creating fiscal space through enhanced domestic revenue mobilization, and improving the quality of public spending through public financial management (PFM) reforms, and building more robust buffers against external shocks.	Accelerate reforms of the Central Bank of the Congo (BCC) and the financial sector by (i) passing the central bank law to strengthen its independence and governance, (ii) completing its recapitalization, and (iii) strengthening its analytical capacity, (iv) disengaging from non-core activities, and (v) implement FSAP recommendations to promote financial sector stability and development.	Implement measures included in the updated governance matrix agreed with the World Bank and the recommendations of the Extractive Industries Transparency Initiative (EITI) and the National Conference on Mineral Resources Management (NCMRM) to enhance transparency and good governance in the management of natural resources.
Lesotho (2014)	Public financial management in Lesotho is weak, seriously impairing budget planning, execution, and monitoring and the overall delivery of government services. Efforts need to be stepped up in the following areas: (i) strengthening the PFM Secretariat so that it can advance the reform agenda and coordinate the contributions of development partners; (ii) making the Cash Management Unit (CMU) operational and introducing the monthly reconciliation of all Treasury accounts to strengthen the auditing of government operations; (iii) implementing the IFMIS upgrade; (iv) finalizing the draft regulations for the Public Financial Management Act (PFMA); (v) strengthening the Medium Term Expenditure Framework (MTEF) to ensure meaningful medium-term expenditure ceilings	Finalize regulations supporting the implementation of the 2012 Financial Institutions Act (FIA); strengthen on- and off-site supervision; and gradually adopt pillar II of the Basel II capital accords. Given the dominant role of South Africa's banks in Lesotho, it is important to strengthen cross-border supervision by enhancing coordination with the South Africa Reserve Bank, including the updating of the memorandum of understanding for cooperation and information sharing. In addition, the CBL needs to formulate a training curriculum for staff, especially new employees, that among other things builds capacity in risk-based supervision and to pursue a human resources policy that would increase retention of high-performers, including career advancement.	Over the medium term, moving toward a rules-based fiscal policy framework could reduce Lesotho's vulnerability to volatile SACU (South African Customs Union) revenue. That is, a rules-based approach could reduce the pro-cyclicality of government spending and, by budgeting appropriately for the volatility of revenues, reduce the exposure to revenue shortfalls. Transparency and quality public financial management (PFM) are critical to the success of a rules-based approach.

	to line ministries; and (vi) building government's capacity for project appraisal to enable capital spending to generate high returns.	The approval of the Financial Sector Development Strategy (FSDS)—an important milestone in financial sector development—needs to be followed by its expedient implementation.	
Madagascar (2015)	There has been some deterioration in PFM performance in recent years, as evidenced by their CPIA rating and the recently published 2013 PEFA self-assessment. The overall performance of the PFM system has not improved since the period 2006-2008 and nine performance indicators have been downgraded. Based on these findings, the authorities have adopted in October 2014 a Priority Action Plan (PAP) for PFM reforms to address several weaknesses by the end of 2015 and prepare the ground for a PFM reform strategy covering the period 2016–18.	The central bank needs to be able to pursue an independent monetary policy. Important components of this would include increasing the independence of the Central Bank, strengthening its oversight mechanisms, and recapitalizing it. This would also facilitate a more active monetary policy that would give priority to mopping up excess liquidity and give more significance to the reference rate. The use of statutory advances to the budget from the central bank should be avoided. Challenges in banking supervision should be tackled proactively. Ongoing efforts to upgrade the quality of supervision, including launching of a financial stability report and preparing a three-year strategic plan, are welcome. Continued monitoring of risk in both the banking and microfinance sectors is critical. Impactful supervision will involve both a sound regulatory framework and timely actions.	Governance and government institutions have deteriorated in recent years. The uncertainty created by weak governance, recurrent political crises, and short-term rent seeking are important reasons for Madagascar's poor economic performance. It will be important to give priority to structural reforms with the potential for (i) creating a stable environment and level playing field for the private sector; (ii) reinforcing anti-corruption institutions (a more professional judicial system and stronger supervisory bodies, and mobilizing the anti-money laundering/combating the financing of terrorism (AML/CFT) regime); and (iii) encouraging foreign investment.
Malawi (2012)	Enhance Public Financial Management. In order to ensure that spending is in line with the government's priorities, the authorities need to strengthen commitment control and enforce procurement rules.	Strengthen supervision of financial institutions. Given the recent history of fiscal dominance, the discussions on monetary policy emphasized the need for increased operational independence of the RBM.	Malawi ranks behind its neighbors in indicators of the business environment such as business operating conditions and business transaction costs.
Mauritius (2014)	Including all extra-budgetary funds in the budget should increase fiscal transparency and better measure the fiscal stance. In addition, passing the new Public Financial Management (PFM) Act, should alleviate some of the budget execution difficulties.		Advance structural reforms and initiate fiscal consolidation to improve growth prospects and reduce external imbalances. Reforms to increase local governments' own resources and improve spending efficiency should contain fiscal risks and improve efficiency.
Mozambique (2013)	Reforms to modernize revenue administration and PFM need to continue across the board, and steps taken to ensure timely settlement of VAT refunds.	Ongoing reforms of financial and prudential regulations aiming at strengthening the soundness and supervision of the banking system and financial deepening should be swiftly implemented along the lines of the Financial Sector Development Strategy.	Prompt adoption by Parliament of the draft AML/CFT law would contribute to further support anti-corruption efforts.
Namibia (2014)			Boosting potential growth would require a set of reform-oriented innovative policies to reinvigorate total factor productivity. These include increasing the quality of public spending through ongoing reforms in public financial management and the government tender system.

			Other measures include improving the efficiency and effectiveness of the tax system, reducing the cost of doing business and the skill mismatch in the labor market, and diversifying the economy.
Seychelles (2011)	Enhancing public financial management (PFM) is a key area of structural reforms. To assess the progress authorities will undertake a new assessment under the Public Expenditure and Financial Accountability (PEFA) standards in early 2011. A new chart of accounts will be introduced for the 2012 budget to support improved decision making on the allocation of resources. The amendments to the Public Finance Act will reflect recent operational improvements in PFM, introducing principles of transparency, accountability, medium-term stability and budget performance and extending its coverage to budget formulation and budget execution processes; the act will also extend the National Assembly's oversight of the budget to capital expenditures.		Improve governance and financial management for two strategic enterprises, Air Seychelles and the Public Utilities Corporation (PUC).
South Africa (2014)		Early intervention powers of the South African Reserve Bank (SARB) and other prudential regulators should be enhanced. Reforms of the financial architecture should include closing supervisory and regulatory gaps and strengthening the financial safety net. Group-wide supervision, clear demarcation of accountability, and greater coordination among supervisory authorities are needed. Group-wide supervision and greater coordination between supervisory authorities are essential given high interconnectedness and a large financial system.	Improving the business environment and allowing greater private participation in infrastructure projects could attract more FDI.
Swaziland (2014)	The enactment and effective implementation of the PFM Bill are critical to strengthen PFM and macroeconomic analysis. Furthermore, in line with the authorities' PFM action plan, key reform measures include (i) preparing a coherent medium-term fiscal and expenditure framework; (ii) improving cash management; and (iii) strengthening commitment control to prevent arrears.13 It is important to enhance fiscal reporting and transparency (posting the budget outturn on the website is a good step forward), while effectively addressing the issues identified in the auditor general's reports. Reconciliation exercises should also be	The Financial Services Regulatory Authority (FSRA) is to further step up its efforts to strengthen the supervision and regulation for nonbank financial institutions (including the implementations of legal frameworks for the regulations for insurance companies and capital market institutions).	To raise potential growth (and then to enhance employment and reduce poverty and inequality), it is essential to improve the efficiency of the public sector and promote private sector-led, inclusive growth, through wide-ranging structural reforms. Improvement in Swaziland's competitiveness, through these reforms, is also called.

	conducted on regular basis.		
Tanzania (2014)	Weaknesses in public financial management undermine the quality and timeliness of fiscal data available to policymakers. The three main problems are: (i) recurrence of large domestic unpaid claims (with duration above 90 days);; (ii) growing expenditure "floats" (estimated at 6 percent of domestically financed spending or 1.3 percent of GDP in 2012/13);4 and considerable delay in coming close to reconciling the discrepancies between "above the line" deficit figures and the financing data. These issues point to weaknesses in budget formulation, execution and monitoring, including difficulties in aligning expenditures with available financing resources during the year. Improving public financial management remains a priority. In particular, guidelines to prevent arrears accumulation need to be implemented and a plan is required for the gradual reduction of the existing stock, with appropriate verification and safeguards. More generally, the accuracy and timeliness of fiscal data is necessary for better informed policymaking. Priority areas include: a net reduction in the stock of arrears; diminished use of expenditure floats at the end of the fiscal year; and more timely compilation of fiscal outturn data consistent with financing data.	The Financial System Stability Assessment (FSSA) update of June 2010 recommended several actions, such as addressing data gaps to strengthen the oversight of banks, developing credit information tools to mitigate systemic credit risk, and improving the framework for dealing with banking crises. Progress to date includes collaboration committees of relevant supervisors and policymakers for effective surveillance and crisis management/resolution, as well as the establishment of a credit reference database and bureaus. The frameworks for monetary policy and financial supervision will need to keep pace with the economy's modernization and its growing international integration. In the financial sector, technological innovations and international integration are creating new opportunities for financial deepening and inclusion, but also call for speedy implementation of reforms of the financial supervision framework to reduce or manage any ensuing vulnerabilities. A priority is to ensure effective collaboration among regulators, both domestically and with international counterparts.	A key challenge will be to set up appropriate institutional arrangements to ensure that any gains from natural resources accrue to the benefit of all citizens. In the next few years, this will involve establishing a clear taxation framework that retains good revenues for citizens while providing reassurance to natural gas companies that their investments will remain worthwhile; transparency in the contracts signed with private companies; a fiscal framework that smoothes the use of natural resources and aims at intergenerational equity; ensuring that all spending financed by natural resource revenues (including those collected by public enterprises involved in the sector) is determined and undertaken through the general budget process and is subject to the same degree of public scrutiny as that financed by other revenues. The long-term outlook will be influenced by the business climate and its impact on investment. There seems to be considerable room for improvement through structural and institutional reforms.
Zambia (2010)	Public financial management reforms need to continue. The alignment of the budget cycle to the fiscal year is a welcome development that should strengthen budget execution. However, it is necessary to ensure closer conformity between the adopted and executed budget. A new budget act represents one step in that direction, as do the ongoing reforms related to the TSA and IFMIS. In general, PFM reforms should aim to ensure that government spending becomes more efficient.	Continued financial sector reforms will serve towards enhancing financial intermediation. Further financial sector reforms and changes in how the Bank of Zambia interacts with financial markets are needed. The implementation of the second phase of the financial sector development plan should be pursued assiduously.	The government needs to reverse the erosion of tax revenue by reforming tax policy and administration.
Zimbabwe (2014)	Rebalancing the expenditure mix and advancing public financial management (PFM) reforms remain critical for medium-term fiscal sustainability.	Despite efforts to enhance the legal and regulatory framework, financial sector vulnerabilities persist. The planned amendments to the Banking Act, which are aimed at improving corporate governance and strengthening the Troubled and Insolvent Bank Resolution Framework, will help to enhance stability. Authorities remain committed to restoring the role of the central bank in their efforts to enhance financial intermediation. Enhancing financial sector stability and	Addressing infrastructure deficits, enhancing the business climate, and improving governance and policy consistency are critical for boosting productivity and competitiveness. Continued strengthening of debt management legislation is critical. The first step is Cabinet approval of the principles for a Public Debt Management Bill. When enacted, the new bill will provide MoFED with a stronger

		restoring confidence in the banking system must remain a priority.	and more effective mandate to plan, negotiate, and monitor external borrowing operations. It will also bolster the institutional role of the Debt Management Office at MoFED. Increasing transparency in the diamond sector remains critical for improving fiscal management and good governance.

Source: Adopted from IMF Article IV Consultations Country Reports for each country

Conclusion: The Way Forward

This paper presented the case for how South Korea, an example of a development State, was able to grow at rates much higher than those of African countries, making the case for the importance of institutional quality for economic performance. It then presented a snapshot—a point in time—of the state of governance in general and economic governance in particular of SADC Member countries using secondary data and information, highlighting specific areas in which SADC countries need to make improvements.

Quality institutions that are able to achieve stated objectives, including the implementation of a “development state agenda” possesses specific characteristics. They must be effective and efficient. The must embrace principles of participation, accountability, facilitating access, decision making and results-orientation.

Assessments through standards and codes can prove to be comprehensive and useful tools for enhancing the regulatory and supervisory frameworks of countries. Going forward, the paper advocates for an in-depth country-by-country case study analysis of economic governance to provide a more nuanced picture of how institutions can best perform and contribute in this area. It suggests the undertaking of primary data collection using guidelines in Standards and Codes, provided in the Annexes as the basis for analysis. This would be compounded by consistent, multi-year quantitative data on economic governance indicators (if available from institutions including the IMF) on performance, highlighting trends, results and findings. This would then enable the making of recommendations for improvements of economic governance in SADC countries that is based on empirical findings in the region.

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Annex I: Code of Good Practices on Fiscal Transparency (2007)

I. Clarity of Roles and Responsibilities

1.1. The government sector should be distinguished from the rest of the public sector and from the rest of the economy, and policy and management roles within the public sector should be clear and publicly disclosed.

1.1.1 The structure and functions of government should be clear.

1.1.2 The fiscal powers of the executive, legislative, and judicial branches of government should be well defined.

1.1.3 The responsibilities of different levels of government, and the relationships between them, should be clearly specified.

1.1.4 Relationships between the government and public corporations should be based on clear arrangements.

1.1.5 Government relationships with the private sector should be conducted in an open manner, following clear rules and procedures.

1.2. There should be a clear and open legal, regulatory, and administrative framework for fiscal management.

1.2.1 The collection, commitment, and use of public funds should be governed by comprehensive budget, tax, and other public finance laws, regulations, and administrative procedures.

1.2.2 Laws and regulations related to the collection of tax and non-tax revenues, and the criteria guiding administrative discretion in their application, should be accessible, clear, and understandable. Appeals of tax or non-tax obligations should be considered in a timely manner.

1.2.3 There should be sufficient time for consultation about proposed laws and regulatory changes and, where feasible, broader policy changes.

1.2.4 Contractual arrangements between the government and public or private entities, including resource companies and operators of government concessions, should be clear and publicly accessible.

1.2.5 Government liability and asset management, including the granting of rights to use or exploit public assets, should have an explicit legal basis.

II. Open Budget Processes

2.1. Budget preparation should follow an established timetable and be guided by well-defined macroeconomic and fiscal policy objectives.

2.1.1 A budget calendar should be specified and adhered to. Adequate time should be allowed for the draft budget to be considered by the legislature.

2.1.2 The annual budget should be realistic, and should be prepared and presented within a comprehensive medium-term macroeconomic and fiscal policy framework. Fiscal targets and any fiscal rules should be clearly stated and explained.

2.1.3 A description of major expenditure and revenue measures, and their contribution to policy objectives, should be provided. Estimates should also be provided of their current and future budgetary impact and their broader economic implications.

2.1.4 The budget documentation should include an assessment of fiscal sustainability. The main assumptions about economic developments and policies should be realistic and clearly specified, and sensitivity analysis should be presented.

2.1.5 There should be clear mechanisms for the coordination and management of budgetary and extrabudgetary activities within the overall fiscal policy framework.

2.2 There should be clear procedures for budget execution, monitoring, and reporting.

2.2.1 The accounting system should provide a reliable basis for tracking revenues, commitments, payments, arrears, liabilities, and assets.

2.2.2 A timely midyear report on budget developments should be presented to the legislature. More frequent updates, which should be at least quarterly, should be published.

2.2.3 Supplementary revenue and expenditure proposals during the fiscal year should be presented to the legislature in a manner consistent with the original budget presentation.

2.2.4 Audited final accounts and audit reports, including reconciliation with the approved budget, should be presented to the legislature and published within a year.

III. Public Availability of Information

3.1 The public should be provided with comprehensive information on past, current, and projected fiscal activity and on major fiscal risks.

3.1.1 The budget documentation, including the final accounts, and other published fiscal reports should cover all budgetary and extrabudgetary activities of the central government.

3.1.2 Information comparable to that in the annual budget should be provided for the outturns of at least the two preceding fiscal years, together with forecasts and sensitivity analysis for the main budget aggregates for at least two years following the budget.

3.1.3 Statements describing the nature and fiscal significance of central government tax expenditures, contingent liabilities, and quasi-fiscal activities should be part of the budget documentation, together with an assessment of all other major fiscal risks.

3.1.4 Receipts from all major revenue sources, including resource-related activities and foreign assistance, should be separately identified in the annual budget presentation.

3.1.5 The central government should publish information on the level and composition of its debt and financial assets, significant nondebt liabilities (including pension rights, guarantee exposure, and other contractual obligations), and natural resource assets.

3.1.6 The budget documentation should report the fiscal position of subnational governments and the finances of public corporations.

3.1.7 The government should publish a periodic report on long-term public finances.

3.2 Fiscal information should be presented in a way that facilitates policy analysis and promotes accountability.

3.2.1 A clear and simple summary guide to the budget should be widely distributed at the time of the annual budget.

3.2.2 Fiscal data should be reported on a gross basis, distinguishing revenue, expenditure, and financing, with expenditure classified by economic, functional, and administrative category.

3.2.3 The overall balance and gross debt of the general government, or their accrual equivalents, should be standard summary indicators of the government fiscal position. They should be supplemented, where appropriate, by other fiscal indicators, such as the primary balance, the public sector balance, and net debt.

3.2.4 Results achieved relative to the objectives of major budget programs should be presented to the legislature annually.

3.3 A commitment should be made to the timely publication of fiscal information.

3.3.1 The timely publication of fiscal information should be a legal obligation of government.

3.3.2 Advance release calendars for fiscal information should be announced and adhered to.

IV. Assurances of Integrity

4.1 Fiscal data should meet accepted data quality standards.

4.1.1 Budget forecasts and updates should reflect recent revenue and expenditure trends, underlying macroeconomic developments, and well-defined policy commitments.

4.1.2 The annual budget and final accounts should indicate the accounting basis used in the compilation and presentation of fiscal data. Generally accepted accounting standards should be followed.

4.1.3 Data in fiscal reports should be internally consistent and reconciled with relevant data from other sources. Major revisions to historical fiscal data and any changes to data classification should be explained.

4.2 Fiscal activities should be subject to effective internal oversight and safeguards.

4.2.1 Ethical standards of behavior for public servants should be clear and well publicized.

4.2.2 Public sector employment procedures and conditions should be documented and accessible to interested parties.

4.2.3 Procurement regulations, meeting international standards, should be accessible and observed in practice.

4.2.4 Purchases and sales of public assets should be undertaken in an open manner, and major transactions should be separately identified.

4.2.5 Government activities and finances should be internally audited, and audit procedures should be open to review.

4.2.6 The national revenue administration should be legally protected from political direction, ensure taxpayers' rights, and report regularly to the public on its activities.

4.3 Fiscal information should be externally scrutinized.

4.3.1 Public finances and policies should be subject to scrutiny by a national audit body or an equivalent organization that is independent of the executive.

4.3.2 The national audit body or equivalent organization should submit all reports, including its annual report, to the legislature and publish them. Mechanisms should be in place to monitor follow-up actions.

4.3.3 Independent experts should be invited to assess fiscal forecasts, the macroeconomic forecasts on which they are based, and their underlying assumptions.

4.3.4 A national statistical body should be provided with the institutional independence to verify the quality of fiscal data.

Source: http://www.imf.org/external/np/fad/trans/code.htm

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Annex II: Code of Good Practices on Transparency in Monetary and Financial Policies

A. GOOD TRANSPARENCY PRACTICES FOR MONETARY POLICY BY CENTRAL BANKS

I. Clarity of Roles, Responsibilities and Objectives of Central Banks for Monetary Policy

1.1 The ultimate objective(s) and institutional framework of monetary policy should be clearly defined in relevant legislation or regulation, including, where appropriate, a central bank law.

1.1.1 The ultimate objective(s) of monetary policy should be specified in legislation and publicly disclosed and explained.

1.1.2 The responsibilities of the central bank should be specified in legislation.

1.1.3 The legislation establishing the central bank should specify that the central bank has the authority to utilize monetary policy instruments to attain the policy objective(s).

1.1.4 Institutional responsibility for foreign exchange policy should be publicly disclosed.

1.1.5 The broad modalities of accountability for the conduct of monetary policy and for any other responsibilities assigned to the central bank should be specified in legislation.

1.1.6 If, in exceptional circumstances, the government has the authority to override central bank policy decisions, the conditions under which this authority may be invoked and the manner in which it is publicly disclosed should be specified in legislation.

1.1.7 The procedures for appointment, terms of office, and any general criteria for removal of the heads and members of the governing body of the central bank should be specified in legislation.

1.2 The institutional relationship between monetary and fiscal operations should be clearly defined.

1.2.1 If credits, advances, or overdrafts to the government by the central bank are permitted, the conditions when they are permitted, and any limits thereof, should be publicly disclosed.

1.2.2 The amounts and terms of credits, advances, or overdrafts to the government by the central bank and those of deposits of the government with the central bank should be publicly disclosed.

1.2.3 The procedures for direct central bank participation in the primary markets for government securities, where permitted, and in the secondary markets, should be publicly disclosed.

1.2.4 Central bank involvement in the rest of the economy (e.g., through equity ownership, membership on governing boards, procurement, or provision of services for fee) should be conducted in an open and public manner on the basis of clear principles and procedures.

1.2.5 The manner in which central bank profits are allocated and how capital is maintained should be publicly disclosed.

1.3 Agency roles performed by the central bank on behalf of the government should be clearly defined.

1.3.1 Responsibilities, if any, of the central bank in (i) the management of domestic and external public debt and foreign exchange reserves, (ii) as banker to the government, (iii) as fiscal agent of the government, and (iv) as advisor on economic and financial policies and in the field of international cooperation, should be publicly disclosed.

1.3.2 The allocation of responsibilities among the central bank, the ministry of finance, or a separate public agency, for the primary debt issues, secondary market arrangements, depository facilities, and clearing and settlement arrangements for trade in government securities, should be publicly disclosed.

II. Open Process for Formulating and Reporting Monetary Policy Decisions

2.1 The framework, instruments, and any targets that are used to pursue the objectives of monetary policy should be publicly disclosed and explained.

2.1.1 The procedures and practices governing monetary policy instruments and operations should be publicly disclosed and explained.

2.1.2 The rules and procedures for the central bank's relationships and transactions with counter parties in its monetary operations and in the markets where it operates should be publicly disclosed.

2.2 Where a permanent monetary policy-making body meets to assess underlying economic developments, monitor progress toward achieving its monetary policy objective(s), and formulate policy for the period ahead, information on the composition, structure, and functions of that body should be publicly disclosed.

2.2.1 If the policy-making body has regularly scheduled meetings to assess underlying economic developments, monitor progress toward achieving its monetary policy objective(s), and formulate policy for the period ahead, the advance meeting schedule should be publicly disclosed.

2.3 Changes in the setting of monetary policy instruments (other than fine-tuning measures) should be publicly announced and explained in a timely manner.

2.3.1 The central bank should publicly disclose, with a preannounced maximum delay, the main considerations underlying its monetary policy decisions.

2.4 The central bank should issue periodic public statements on progress toward achieving its monetary policy objective(s) as well as prospects for achieving them. The arrangements could differ depending on the monetary policy framework, including the exchange rate regime.

2.4.1 The central bank should periodically present its monetary policy objectives to the public, specifying, inter alia, their rationale, quantitative targets and instruments where applicable, and the key underlying assumptions.

2.4.2 The central bank should present to the public on a specified schedule a report on the evolving macroeconomic situation, and their implications for its monetary policy objective(s).

2.5 For proposed substantive technical changes to the structure of monetary regulations, there should be a presumption in favor of public consultations, within an appropriate period.

2.6 The regulations on data reporting by financial institutions to the central bank for monetary policy purposes should be publicly disclosed.

III. Public Availability of Information on Monetary Policy

3.1 Presentations and releases of central bank data should meet the standards related to coverage, periodicity, timeliness of data and access by the public that are consistent with the International Monetary Fund's data dissemination standards.

3.2 The central bank should publicly disclose its balance sheet on a preannounced schedule and, after a

predetermined interval, publicly disclose selected information on its aggregate market transactions.

3.2.1 Summary central bank balance sheets should be publicly disclosed on a frequent and preannounced schedule. Detailed central bank balance sheets prepared according to appropriate and publicly documented accounting standards should be publicly disclosed at least annually by the central bank.

3.2.2 Information on the central bank's monetary operations, including aggregate amounts and terms of refinance or other facilities (subject to the maintenance of commercial confidentiality) should be publicly disclosed on a preannounced schedule.

3.2.3 Consistent with confidentiality and privacy of information on individual firms, aggregate information on emergency financial support by the central bank should be publicly disclosed through an appropriate central bank statement when such disclosure will not be disruptive to financial stability.

3.2.4 Information about the country's foreign exchange reserve assets, liabilities and commitments by the monetary authorities should be publicly disclosed on a preannounced schedule, consistent with the International Monetary Fund's Data Dissemination Standards.

3.3 The central bank should establish and maintain public information services.

3.3.1 The central bank should have a publications program, including an Annual Report.

3.3.2 Senior central bank officials should be ready to explain their institution's objective(s) and performance to the public, and have a presumption in favor of releasing the text of their statements to the public.

3.4 Texts of regulations issued by the central bank should be readily available to the public.

IV. Accountability and Assurances of Integrity by the Central Bank

4.1 Officials of the central bank should be available to appear before a designated public authority to report on the conduct of monetary policy, explain the policy objective(s) of their institution, describe their performance in achieving their objective(s), and, as appropriate, exchange views on the state of the economy and the financial system.

4.2 The central bank should publicly disclose audited financial statements of its operations on a preannounced schedule.

4.2.1 The financial statements should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements.

4.2.2 Internal governance procedures necessary to ensure the integrity of operations, including internal audit arrangements, should be publicly disclosed.

4.3 Information on the expenses and revenues in operating the central bank should be publicly disclosed annually.

4.4 Standards for the conduct of personal financial affairs of officials and staff of the central bank and rules to prevent exploitation of conflicts of interest, including any general fiduciary obligation, should be publicly disclosed.

4.4.1 Information about legal protections for officials and staff of the central bank in the conduct of their official duties should be publicly disclosed.

B. GOOD TRANSPARENCY PRACTICES FOR FINANCIAL POLICIES BY FINANCIAL AGENCIES

V. Clarity of Roles, Responsibilities and Objectives of Financial Agencies Responsible for Financial Policies

5.1 The broad objective(s) and institutional framework of financial agencies should be clearly defined, preferably in relevant legislation or regulation.

5.1.1 The broad objective(s) of financial agencies should be publicly disclosed and explained.

5.1.2 The responsibilities of the financial agencies and the authority to conduct financial policies should be publicly disclosed.

5.1.3 Where applicable, the broad modalities of accountability for financial agencies should be publicly disclosed.

5.1.4 Where applicable, the procedures for appointment, terms of office, and any general criteria for removal of the heads and members of the governing bodies of financial agencies should be publicly disclosed.

5.2 The relationship between financial agencies should be publicly disclosed.

5.3 The role of oversight agencies with regard to payment systems should be publicly disclosed.

5.3.1 The agencies overseeing the payment system should promote the timely public disclosure of general policy principles (including risk management policies) that affect the robustness of systemically important payment systems.

5.4 Where financial agencies have oversight responsibilities for self-regulatory organizations (e.g., payment systems), the relationship between them should be publicly disclosed.

5.5 Where self-regulatory organizations are authorized to perform part of the regulatory and supervisory process, they should be guided by the same good transparency practices specified for financial agencies.

VI. Open Process for Formulating and Reporting of Financial Policies

6.1 The conduct of policies by financial agencies should be transparent, compatible with confidentiality considerations and the need to preserve the effectiveness of actions by regulatory and oversight agencies

6.1.1 The regulatory framework and operating procedures governing the conduct of financial policies should be publicly disclosed and explained.

6.1.2 The regulations for financial reporting by financial institutions to financial agencies should be publicly disclosed.

6.1.3 The regulations for the operation of organized financial markets (including those for issuers of traded financial instruments) should be publicly disclosed.

6.1.4 Where financial agencies charge fees to financial institutions, the structure of such fees should be publicly disclosed.

6.1.5 Where applicable, formal procedures for information sharing and consultation between financial agencies (including central banks), domestic and international, should be publicly disclosed.

6.2 Significant changes in financial policies should be publicly announced and explained in a timely manner.

6.3 Financial agencies should issue periodic public reports on how their overall policy objectives are being pursued.

6.4 For proposed substantive technical changes to the structure of financial regulations, there should be a presumption in favor of public consultations, within an appropriate period.

VII. Public Availability of Information on Financial Policies

7.1 Financial agencies should issue a periodic public report on the major developments of the sector(s) of the financial system for which they carry designated responsibility.

7.2 Financial agencies should seek to ensure that, consistent with confidentiality requirements, there is public reporting of aggregate data related to their jurisdictional responsibilities on a timely and regular basis.

7.3 Where applicable, financial agencies should publicly disclose their balance sheets on a preannounced schedule and, after a predetermined interval, publicly disclose information on aggregate market transactions.

7.3.1 Consistent with confidentiality and privacy of information on individual firms, aggregate information on emergency financial support by financial agencies should be publicly disclosed through an appropriate statement when such disclosure will not be disruptive to financial stability.

7.4 Financial agencies should establish and maintain public information services.

7.4.1 Financial agencies should have a publications program, including a periodic public report on their principal activities issued at least annually.

7.4.2 Senior financial agency officials should be ready to explain their institution's objective(s) and performance to the public, and have a presumption in favor of releasing the text of their statements to the public.

7.5 Texts of regulations and any other generally applicable directives and guidelines issued by financial agencies should be readily available to the public.

7.6 Where there are deposit insurance guarantees, policy-holder guarantees, and any other client asset protection schemes, information on the nature and form of such protections, on the operating procedures, on how the guarantee is financed, and on the performance of the arrangement, should be publicly disclosed.

7.7 Where financial agencies oversee consumer protection arrangements (such as dispute settlement processes), information on such arrangements should be publicly disclosed.

VIII. Accountability and Assurances of Integrity by Financial Agencies

8.1 Officials of financial agencies should be available to appear before a designated public authority to report on the conduct of financial policies, explain the policy objective(s) of their institution, describe their performance in pursuing their objective(s), and, as appropriate, exchange views on the state of the financial system.

8.2 Where applicable, financial agencies should publicly disclosed audited financial statements of their operations on a preannounced schedule.

8.2.1 Financial statements, if any, should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements.

8.2.2 Internal governance procedures necessary to ensure the integrity of operations, including internal audit arrangements, should be publicly disclosed.

8.3 Where applicable, information on the operating expenses and revenues of financial agencies should be publicly disclosed annually.

8.4 Standards for the conduct of personal financial affairs of officials and staff of financial agencies and rules to prevent exploitation of conflicts of interest, including any general fiduciary obligation, should be publicly disclosed.

8.4.1 Information about legal protections for officials and staff of financial agencies in the conduct of their official duties should be publicly disclosed.

Source: IMF, 1999. Available at http://www.imf.org/external/np/mae/mft/code/

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Annex III: Core Principles for Effective Banking Supervision by the Basel Committee

A. Supervisory powers, responsibilities and functions

Principle 1 – Responsibilities, objectives and powers: An effective system of banking supervision has clear responsibilities and objectives for each authority involved in the supervision of banks and banking groups. A suitable legal framework for banking supervision is in place to provide each responsible authority with the necessary legal powers to authorise banks, conduct ongoing supervision, address compliance with laws and undertake timely corrective actions to address safety and soundness concerns.

Principle 2 – Independence, accountability, resourcing and legal protection for supervisors: The supervisor possesses operational independence, transparent processes, sound governance, budgetary processes that do not undermine autonomy and adequate resources, and is accountable for the discharge of its duties and use of its resources. The legal framework for banking supervision includes legal protection for the supervisor.

Principle 3 – Cooperation and collaboration: Laws, regulations or other arrangements provide a framework for cooperation and collaboration with relevant domestic authorities and foreign supervisors. These arrangements reflect the need to protect confidential information.

Principle 4 – Permissible activities: The permissible activities of institutions that are licensed and subject to supervision as banks are clearly defined and the use of the word "bank" in names is controlled.

Principle 5 – Licensing criteria: The licensing authority has the power to set criteria and reject applications for establishments that do not meet the criteria. At a minimum, the licensing process consists of an assessment of the ownership structure and governance (including the fitness and propriety of Board members and senior management) of the bank and its wider group, and its strategic and operating plan, internal controls, risk management and projected financial condition (including capital base). Where the proposed owner or parent organisation is a foreign bank, the prior consent of its home supervisor is obtained.

Principle 6 – Transfer of significant ownership: The supervisor has the power to review, reject and impose prudential conditions on any proposals to transfer significant ownership or controlling interests held directly or indirectly in existing banks to other parties.

Principle 7 – Major acquisitions: The supervisor has the power to approve or reject (or recommend to the responsible authority the approval or rejection of), and impose prudential conditions on, major acquisitions or investments by a bank, against prescribed criteria, including the establishment of cross-border operations, and to determine that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.

Principle 8 – Supervisory approach: An effective system of banking supervision requires the supervisor to develop and maintain a forward-looking assessment of the risk profile of individual banks and banking groups, proportionate to their systemic importance; identify, assess and address risks emanating from banks and the banking system as a whole; have a framework in place for early intervention; and have plans in place, in partnership with other relevant authorities, to take action to resolve banks in an orderly manner if they become non-viable.

Principle 9 – Supervisory techniques and tools: The supervisor uses an appropriate range of techniques and tools to implement the supervisory approach and deploys supervisory resources on a proportionate basis, taking into account the risk profile and systemic importance of banks.

Principle 10 – Supervisory reporting: The supervisor collects, reviews and analyses prudential reports and statistical returns from banks on both a solo and a consolidated basis, and independently verifies these reports through either on-site examinations or use of external experts.

Principle 11 – Corrective and sanctioning powers of supervisors: The supervisor acts at an early stage to address unsafe and unsound practices or activities that could pose risks to banks or to the banking system. The supervisor has at its disposal an adequate range of supervisory tools to bring about timely corrective actions. This includes the ability to revoke the banking licence or to recommend its revocation.

Principle 12 – Consolidated supervision: An essential element of banking supervision is that the supervisor supervises the banking group on a consolidated basis, adequately monitoring and, as appropriate, applying prudential standards to all aspects of the business conducted by the banking group worldwide.

Principle 13 – Home-host relationships: Home and host supervisors of cross-border banking groups share information and cooperate for effective supervision of the group and group entities, and effective handling of crisis situations. Supervisors require the local operations of foreign banks to be conducted to the same standards as those required of domestic banks.

B. Prudential regulations and requirements

Principle 14 – Corporate governance: The supervisor determines that banks and banking groups have robust corporate governance policies and processes covering, for example, strategic direction, group and organisational structure, control environment, responsibilities of the banks' Boards and senior management, and compensation. These policies and processes are commensurate with the risk profile and systemic importance of the bank.

Principle 15 – Risk management process: The supervisor determines that banks have a comprehensive risk management process (including effective Board and senior management oversight) to identify, measure, evaluate, monitor, report and control or mitigate all material risks on a timely basis and to assess the adequacy of their capital and liquidity in relation to their risk profile and market and macroeconomic conditions. This extends to development and review of contingency arrangements (incuding robust and credible recovery plans where warranted) that take into account the specific circumstances of the bank. The risk management process is commensurate with the risk profile and systemic importance of the bank.

Principle 16 – Capital adequacy: The supervisor sets prudent and appropriate capital adequacy requirements for banks that reflect the risks undertaken by, and presented by, a bank in the context of the markets and macroeconomic conditions in which it operates. The supervisor defines the components of capital, bearing in mind their ability to absorb losses. At least for internationally active banks, capital requirements are not less than the applicable Basel standards.

Principle 17 – Credit risk: The supervisor determines that banks have an adequate credit risk management process that takes into account their risk appetite, risk profile and market and macroeconomic conditions. This includes prudent policies and processes to identify, measure, evaluate, monitor, report and control or mitigate credit risk (including counterparty credit risk) on a timely basis. The full credit lifecycle is covered including credit underwriting, credit evaluation, and the ongoing management of the bank's loan and investment portfolios.

Principle 18 – Problem assets, provisions and reserves: The supervisor determines that banks have adequate policies and processes for the early identification and management of problem assets, and the maintenance of adequate provisions and reserves.

Principle 19 – Concentration risk and large exposure limits: The supervisor determines that banks have adequate policies and processes to identify, measure, evaluate, monitor, report and control or mitigate concentrations of risk on a timely basis. Supervisors set prudential limits to restrict

Principle 20 – Transactions with related parties: In order to prevent abuses arising in transactions with related parties and to address the risk of conflict of interest, the supervisor requires banks to enter into any transactions with related parties on an arm's length basis; to monitor these transactions; to take appropriate steps to control or mitigate the risks; and to write off exposures to related parties in accordance with standard policies and processes.

Principle 21 – Country and transfer risks: The supervisor determines that banks have adequate policies and processes to identify, measure, evaluate, monitor, report and control or mitigate country risk and transfer risk in their international lending and investment activities on a timely basis.

Principle 22 – Market risks: The supervisor determines that banks have an adequate market risk management process that takes into account their risk appetite, risk profile, and market and macroeconomic conditions and the risk of a significant deterioration in market liquidity. This includes prudent policies and processes to identify, measure, evaluate, monitor, report and control or mitigate market risks on a timely basis.

Principle 23 – Interest rate risk in the banking book: The supervisor determines that banks have adequate systems to identify, measure, evaluate, monitor, report and control or mitigate interest rate risk in the banking book on a timely basis. These systems take into account the bank's risk appetite, risk profile and market and macroeconomic conditions.

Principle 24 – Liquidity risk: The supervisor sets prudent and appropriate liquidity requirements (which can include either quantitative or qualitative requirements or both) for banks that reflect the liquidity needs of the bank. The supervisor determines that banks have a strategy that enables prudent management of liquidity risk and compliance with liquidity requirements. The strategy takes into account the bank's risk profile as well as market and macroeconomic conditions and includes prudent policies and processes, consistent with the bank's risk appetite, to identify, measure, evaluate, monitor, report and control or mitigate liquidity risk over an appropriate set of time horizons. At least for internationally active banks, liquidity requirements are not lower than the applicable Basel standards.

Principle 25 – Operational risk: The supervisor determines that banks have an adequate operational risk management framework that takes into account their risk appetite, risk profile and market and macroeconomic conditions. This includes prudent policies and processes to identify, assess, evaluate, monitor, report and control or mitigate operational risk on a timely basis.

Principle 26 – Internal control and audit: The supervisor determines that banks have adequate internal control frameworks to establish and maintain a properly controlled operating environment for the conduct of their business taking into account their risk profile. These include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding the bank's assets; and appropriate independent internal audit and compliance functions to test adherence to these controls as well as applicable laws and regulations.

Principle 27: Financial reporting and external audit: The supervisor determines that banks and banking groups maintain adequate and reliable records, prepare financial statements in accordance with accounting policies and practices that are widely accepted internationally and annually publish information that fairly reflects their financial condition and performance and bears an independent external auditor's opinion. The supervisor also determines that banks and parent companies of banking groups have adequate governance and oversight of the external audit function.

Principle 28 – Disclosure and transparency: The supervisor determines that banks and banking groups regularly publish information on a consolidated and, where appropriate, solo basis that is easily accessible and fairly reflects their financial condition, performance, risk exposures, risk management strategies and corporate governance policies and processes.

Principle 29 – Abuse of financial services: The supervisor determines that banks have adequate policies and processes, including strict customer due diligence rules to promote high ethical and professional standards in the financial sector and prevent the bank from being used, intentionally or unintentionally, for criminal activities.

Source: Bank for International Settlements, 2012. Available at http://www.bis.org/publ/bcbs230.pdf

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