SUMMARY OF THE APR 2013

AFRICA PROGRESS PANEL

Equity in Extractives

Stewarding Africa's natural resources for all

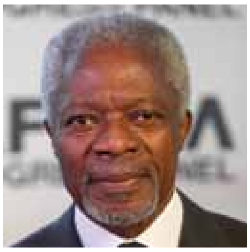
Africa Progress Report 2013

ABOUT THE AFRICA PROGRESS PANEL

The Africa Progress Panel (APP) consists of ten distinguished individuals from the private and public sector who advocate for shared responsibility between African leaders and their international partners to promote equitable and sustainable development for Africa. Mr Kofi Annan, former Secretary-General of the United Nations and Nobel laureate, chairs the APP and is closely involved in its day-to-day work.

The life experiences of Panel members give them a formidable capability to access a wide cross-section of society including at the highest levels in Africa and across the globe. As a result, the Panel functions in a unique policy space with the ability to target decision-making audiences, including African and other world leaders, heads of state, leaders of industry, plus a broad range of stakeholders at the global, regional, and national levels.

The Panel facilitates coalition building at the highest levels to leverage and to broker knowledge, break bottlenecks, and convene decision-makers to influence policy and create change for Africa. The Panel has exceptional networks of policy analysts including academics and policy practitioners across Africa. By bringing together experts with a focus on Africa, the APP contributes to evidence-based policies.



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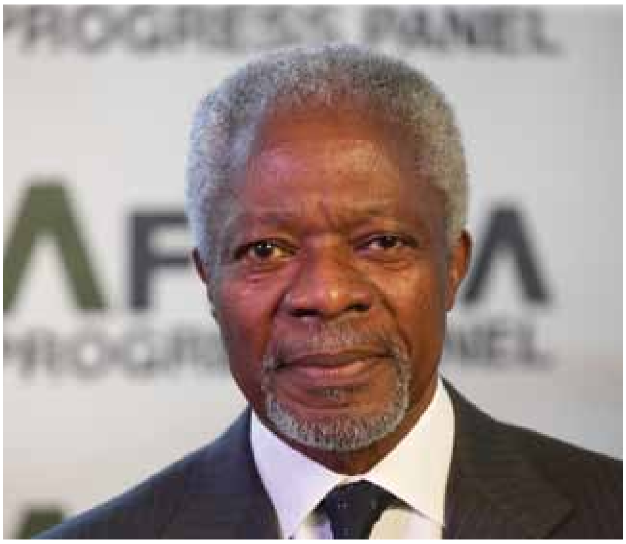
ABOUT THE AFRICA PROGRESS REPORT

Published every year, the Africa Progress Report is the Africa Progress Panel's flagship publication. The report draws on the best research and analysis available on Africa and compiles it in a refreshing and provocative manner. Through the report, the Panel recommends a series of policy choices and actions for African policy makers who have primary responsibility for Africa's progress, as well as international partners and civil society organizations.

FOREWORD
BY KOFI ANNAN



Africa is standing on the edge of enormous opportunity. Will we invest our natural resource revenue in people, generating jobs and opportunities for millions in present and future generations? Or will we squander this opportunity, allowing jobless growth and inequality to take root?

In many countries, for example, natural resource revenues are widening the gap between rich and poor. Although much has been achieved, a decade of highly impressive growth has not brought comparable improvements in health, education and nutrition.

Indeed, our continent still faces many challenges, but this year's Africa Progress Report finds good reason to be optimistic. Building on a decade of strong growth, economic governance continues to improve, providing protection against the boom-bust cycle fuelled by earlier commodity booms. Across the region, democracy is sinking deeper roots – and the accountability that comes with democracy strengthens natural resource management. Defying the predictions of those who believe that Africa is gripped by a "resource curse", many resource-rich countries have sustained high growth and improved their citizens' daily lives. Meanwhile, some foreign investors show they can make a healthy profit while also adhering to the highest international standards of social and environmental protection. And surging demand for limited resources is driving what some commentators describe as a commodity super-cycle, keeping prices high.

With a strong focus on equity, this year's report explores the potential, problems and policy options associated with natural resources by focussing on oil, gas and mining. The starting point is for all countries to develop national strategies that set up the terms under which their natural resources will be developed, including fiscal policies, contractual arrangements and tax regimes. African governments must consult widely to develop these strategies, replacing short-term calculations with the necessary long-term thinking. Critically, these national strategies must identify extractive projects that can generate more jobs, by linking effectively to the local economy. Processing natural resources before exporting them brings extra value to a country's natural resource sector. Africa cannot build dynamic growth and shared prosperity while extractive projects operate within enclaves or countries export natural resources unprocessed.

Above all, national strategies have to set out how the extractive sector fits with plans for poverty reduction, inclusive growth and social transformation.

Success will require leadership, transparency, and accountability, too. There is no substitute for public scrutiny in developing effective and equitable policies. African governments must rise to the challenges posed by fiscal policy, tax reform and the development of industrial policies. They must manage their countries' oil, gas and mining resources efficiently and share revenues fairly.

We therefore call on African governments to set out a bold national agenda for strengthening transparency and accountability to their citizens. For too long, African governments have been responding to externally driven transparency agendas. They have been following, not leading. And it is time to change this pattern.

We welcome the recent adoption by the AU of the African Peer Review Mechanism as the main framework for monitoring natural resource. Building on the Africa Mining Vision, African governments should adopt legislation that requires companies bidding for concessions and licences to fully disclose their beneficial ownership. They should institute transparent systems of auctions and competitive bidding for concessions and licences, as well as tax regimes that reflect both the real value of their countries' natural resource assets and the need to attract high quality investment.

And yet, acting alone, African governments cannot resolve the most intractable natural resource governance challenges. The international community must also shoulder responsibility. When foreign investors make extensive use of offshore companies, shell companies and tax havens, they weaken disclosure standards and undermine the efforts of reformers in Africa to promote transparency. Such practices also facilitate tax evasion and, in some countries, corruption, draining Africa of revenues that should be deployed against poverty and vulnerability. We call on the G8 and the G20 to step up to the mark, to show leadership in the development of a credible and effective multilateral response to tax evasion and avoidance.

All countries must adopt and enforce the project-by-project disclosure standards embodied in the US Dodd-Frank Act and comparable EU legislation. All countries must apply them to all extractive industry companies listed on their stock exchanges. The time is right to develop a global common standard for all countries. As major players in Africa's extractives sector, Australia, Canada and China should be the next countries to actively support this emerging global consensus.

We welcome the commitment from the current G8 presidency, the United Kingdom, and other governments to put tax and transparency at the heart of this year's dialogue. And we urge all OECD countries to recognize the cost of inaction in this vital area. Africa loses twice as much in illicit financial outflows as it receives in international aid. It is unconscionable that some companies, often supported by dishonest officials, are using unethical tax avoidance, transfer pricing and anonymous company ownership to maximize their profits, while millions of Africans go without adequate nutrition, health and education.

Different partners have similar goals. Their interests overlap. Building trust is harder than changing policies – yet it is the ultimate condition for successful policy reform. This year's report, therefore, identifies a shared agenda for change. When we build national capacity to understand natural resource sectors better – in civil society as well as government – we also build trust between government, business and citizens. Better understanding will generate fairer contracts and more equitable national strategies too. In turn, this creates local ownership, longer-lasting contracts, and a better investment climate. Satisfied local communities pose less political risk. Mutually beneficial agreements are the only ones that will stand the test of time.

The Africa Progress Panel is convinced that Africa can better manage its vast natural resource wealth to improve the lives of the region's people. And we hope this report will make a contribution. We all stand to win from an Africa that is truly prosperous, stable and fair. We are all stewards of Africa's natural resource wealth for future generations.

Kofi A. Annan
Chair of the Africa Progress Panel

INTRODUCTION

Located in a remote corner of southeastern Guinea, the lush, green highlands of Simandou are at the centre of a transformation that is being felt across Africa. Beneath the tropical forests, which are celebrated for their ecological richness, lies another prized asset: one of the world's richest but least developed, and most coveted, repositories of iron ore, the core ingredient for making steel. Fuelled by rapid growth in emerging markets, world prices for iron ore have spiralled and global investors are scrambling to unlock new sources of supply. Today, multinational companies from six continents are competing for a stake in Simandou's ore, with billions of dollars of investment in prospect. Exports are set to boom, generating a surge in economic growth.

What does this mean for the people of Guinea, one of the world's poorest countries? Will resource wealth ensure better lives for themselves and future generations? Or will Guinea become another victim of what some commentators see as Africa's endemic resource curse?

These questions go to the heart of this year's *Africa Progress Report,* which focuses on oil, gas and mining. Over the past decade, Africa's economies have been riding the crest of a global commodity wave. Extractive industries have emerged as a powerful engine of economic growth. Surging demand for natural resources in China and other emerging markets has pushed export prices to new highs – and the boom shows no sign of abating. Africa's petroleum, gas and mineral resources have become a powerful magnet for foreign investment. With new exploration revealing much larger reserves than were previously known, Africa stands to reap a natural resource windfall.

The challenge facing the region's governments is to convert the temporary windfall into a permanent breakthrough in human development. Effective and equitable stewardship of Africa's natural resource wealth could transform the region. Apart from building manufacturing industries, the development of natural resources could provide the revenues needed for investment in smallholder agriculture, food security, employment, health and education. Governments have a responsibility to future as well as present generations to harness natural resource wealth. Sub-Saharan Africa entered the 21st century with a population of 670 million. By 2025 the region will be home to 1.2 billion – a figure that will rise to 2 billion by mid-century. The demography matters. Equipped with skills and opportunities, Africa's youthful population could become a powerful – and positive – force for change. Denied a chance to realize their potential, children born today will become a lost generation. Well-managed resource wealth has the potential to lift millions of Africans out of poverty over the next decade, while giving hope to future generations.

According to the resource pessimists, as revenues generated by extractive industries rise, the quality of governance inevitably declines, reducing economic competitiveness and leaving the poor behind. The pessimists' case is built on a long, inglorious history in which Africa's resource wealth has financed colonial-era monuments in Europe, vast private fortunes of post-independence leaders like President Mobutu Sese Seko of Zaire (and some current rulers), and numerous civil wars. Meanwhile, progress in human development has been far less impressive, and most resource-rich economies have been locked into boom-bust cycles with episodes of unsustainable debt. For those who believe that past performance is a guide to future outcomes, Africa's deepening integration into global natural resource markets points to a bleak scenario.

We do not share that belief. Far from being hostage to a non-curable resource curse, this generation of political leaders has an opportunity to harness resource wealth for a transformation in human development. There are four reasons for our guarded optimism.

The first can be traced to the human development record of the past decade. It is a matter of grave concern that Africa is not on course for achieving the 2015 Millennium Development Goals (MDGs). Yet much has been achieved. For the first time in over a generation, the number of people in poverty has fallen. Child death rates are declining. There has been progress in combating major infectious diseases. More of Africa's children are in school. All of this is evidence that a combination of stronger economic growth and strengthened policies can deliver results. If the revenues generated by Africa's natural resource wealth are invested wisely and shared fairly, there is every prospect that the region will see an accelerated drive towards the MDGs.

The second cause of optimism is informed by global commodity market projections. Any prediction about these markets is subject to large margins of uncertainty. Yet there is compelling evidence that we are not living through a normal commodity cycle. Strong and highly resource-intensive economic growth in emerging markets and population growth are driving increased demand, while constraints on increased output are holding back supply. Some commentators maintain that we are now in the early phases of a commodity super-cycle – a period of sustained high prices. Of course, governments have to make contingency plans for market volatility and uncertainty. But it appears likely that export growth will generate large revenue streams that could be used to finance the social and economic infrastructure needed to support a human development breakthrough.

The third cause for optimism is the political and economic policy environment. While there have been setbacks, democracy has taken root across Africa – and when it comes to good governance of natural resources, there is no substitute for democracy. While the quality of participation, transparency and accountability varies from country to country, Africa's citizens are claiming their right to hold their governments to account for their management of natural resources. Fiscal policy and macroeconomic management has also strengthened. Resource-rich countries in Africa are far less vulnerable today to the boom-bust economics of the past. That is one reason they were able to recover so swiftly from the global downturn in 2008. Many of the countries in the early stages of developing their non-renewable resources – including Ghana, Guinea, Kenya, Liberia, Mozambique, Sierra Leone and Tanzania – have greatly strengthened macroeconomic governance over the past decade. Governments in these countries have another great advantage: they can learn from the mistakes of the past and take a different route.

The fourth source of our optimism is grounded in the practices surrounding resource management. Fifteen years ago, most governments treated the governance of resource wealth as a state secret. Citizens were informed of decisions taken by governments on a "need to know" basis – and the assumption was that they needed to know very little. Complex commercial transactions between government agencies and foreign investors were cloaked in secrecy – an arrangement that was highly conducive to corrupt practice. There is still too much secrecy. But the world of resource governance is changing. Global partnerships such as the Extractive Industries Transparency Initiative (EITI) have helped to build a new culture of openness. Governments are making contracts on oil and minerals publicly available. Guinea has recently placed online the full text of contracts covering all major mining deals, including those planned for Simandou. Many major mining companies have strengthened their transparency and accountability standards – and they are assessing with more rigour the social and environmental consequences of their investments. Critically, a vibrant and growing national and international civil society movement is holding governments and companies to account.

Guarded optimism should not be interpreted as endorsement of the exuberance that has taken hold in some quarters. All too often, Africa is presented as a new El Dorado in the global economy – a dynamic hub of resource-led wealth creation and investment opportunity. The underlying message is that another decade of growth fuelled by extractive industries will automatically pull countries and people out of the poverty trap. That message is flawed. If the next decade looks like the last decade, Africa will unquestionably emerge with impressive gains in gross domestic product (GDP) and export activity. But the wellbeing of nations is not measured by growth alone. What matters for African people is the rate at which new resource wealth reduces poverty and expands opportunity.

Governments across the region have paid insufficient attention to this issue. The reduction in poverty achieved over the past decade should be celebrated. Yet as we demonstrate in this report, resource-rich countries have seen poverty levels fall by less than predicted on the basis of their economic growth performance. The reason: in many countries, the poor have seen their share of income shrink. Rising inequality is slowing the rate at which growth reduces poverty.

The wider human development record is also a cause for concern. Most resource-rich countries have human development indicators far below the levels that would be predicted on the basis of their average incomes. Angola and Equatorial Guinea have some of the largest gaps between income and human development as reported in the United Nations Development Programme's Human Development Index (HDI). The Democratic Republic of the Congo, one of the world's best-endowed resource economies, is at the bottom of the HDI. Progress in countries such as Ghana, Tanzania and Zambia has been held back by disparities in human development linked to poverty, the rural-urban divide and other markers for disadvantage.

In this report we set out an agenda for converting increased resource wealth into improved wellbeing. The starting point is a strengthened focus on equity and human development. Too many governments continue to view extractive industries solely as a source of growth and a magnet for foreign investment. Insufficient attention has been directed towards ensuring that the benefits of growth are distributed fairly across society. Governments also need to consider the quality of growth. In many countries, the petroleum and mining sectors continue to operate as enclaves insulated from the national economy. They create few jobs and have weak linkages to local firms. They add little value in production. Africa is exporting predominantly unprocessed natural resources and using the revenues to import consumer and agricultural goods, many of which could – and should – be produced locally. This is not a route to inclusive growth and shared prosperity. And some extractive companies generate healthy profits that do not translate into commensurate government revenues, because of excessive tax concessions, tax evasion and the undervaluation of assets.

There is no blueprint for reform. Policies have to be designed in the light of the constraints and opportunities facing individual countries. However, there are principles and examples of good practice that serve as a guide to policy. We highlight the critical importance of fiscal policy and equitable public spending. Strategies geared towards saving for the future are inappropriate given Africa's vast unmet needs for infrastructure, health, education, water and sanitation. These are all areas in which judicious public spending has the potential to yield not just high economic returns but also windfall gains for human development. Moves towards greater transparency and accountability should be broadened and deepened, not to satisfy the demands of aid donors but to respect the rights of Africa's citizens. The haemorrhaging of resource revenues that occurs through secretive deals and the operations of offshore companies is an unconscionable blight on the lives and hopes of their citizens. Full public disclosure is the most effective tourniquet. The Dodd–Frank legislation adopted in the United States and comparable measures in the European Union (EU) will greatly strengthen the momentum towards greater transparency – and African governments should apply similar principles in domestic legislation.

Breaking with the enclave model of natural resource extraction is another priority. Africa's vast mineral resources could transform social and economic development. The Africa Mining Vision sets out a compelling agenda for change. It calls on African governments to "shift focus from simple mineral extraction to much broader developmental imperatives in which mineral policy integrates with development policy." Achieving that goal will require not just new policies but also the development of institutional capacity and a wider industrial policy. Foreign investors can play a critical role in facilitating change by partnering with governments to strengthen transparency, by supporting skills development, and by carefully assessing the social and environmental impacts of their operations – and many companies are providing leadership in these areas.

In each of these areas there are examples of good practice. Some of Africa's poorest countries are demonstrating that strengthened governance is possible. Yet African governments acting alone, or even in concert, cannot solve all of the problems that are undermining the development potential of resource exports.

Foreign investors have a key role to play. Global companies operating in Africa should apply the same accountability principles and the same standards of governance as they are held to in rich countries. They should also recognize that disclosure matters. The extensive use by multinational investors of companies registered in tax havens and offshore centres, and their dealings with other offshore companies, is potentially damaging to their own corporate reputation and shareholder interests. It is also associated with practices that hurt Africa and weaken the link between resource wealth and poverty reduction.

International action can create an enabling environment for strengthened governance in Africa. Tax evasion, illicit transfers of wealth and unfair pricing practices are sustained through global trading and financial systems – and global problems need multilateral solutions. African citizens should demand that their governments meet the highest standards of propriety and disclosure. Governments in developed countries should demand the same thing of companies registered in, or linked to, their jurisdictions. The G8 and the G20 should establish common rules requiring full public disclosure of the beneficial ownership of companies, with no exceptions. They should also strengthen multilateral rules on taxation to clamp down on the transfer pricing practices that cost Africa billions of dollars annually. This is an area in which Africa and the developed world have a shared interest in bringing order to a system that allows the pursuit of private profit to be placed above the public interest in transparency, accountability and financial stability.

This report does not offer easy answers. There are none. The surge in resource wealth brings with it complex challenges and very real risks. Yet it also brings an unrivalled opportunity. Effectively harnessed and well managed, Africa's resource wealth could lift millions of people out of poverty over the next decade. It could build the health, education and social protection systems that empower people to change their lives and reduce vulnerability. It could generate jobs for Africa's youth and markets for smallholder farmers. And it could put the region on a pathway towards dynamic and inclusive growth.

Seizing these opportunities will be difficult. Squandering them would be unforgivable and indefensible.

SUMMARY

For much of the region's history, Africa's resource wealth has been plundered and squandered. It has served the interests of the few, not the many. Revenues that could have been used to improve lives have instead been used to build personal fortunes, finance civil wars, and support corrupt and unaccountable political elites. This report has a simple message: history does not have to repeat itself. Today, Africa's governments have a unique window of opportunity to convert natural resource wealth into a catalyst for poverty reduction, shared prosperity and accelerated human development.

This year's Africa Progress Report rejects the view that Africa is blighted by a "resource curse" – an affliction that automatically consigns the citizens of resource-rich nations to a future of economic stagnation, poverty and poor governance. There is no curse. The malaise that has afflicted natural resource management in Africa is caused by the wrong domestic policies, weak investment partnerships and failures in international cooperation. Lifting that affliction will require decisive leadership by African governments, backed by multilateral action and a commitment by foreign investors to adopt best international practices.

There is cause for optimism. Global market conditions point to another decade of high prices for natural resources, creating an environment conducive to economic growth. The policy environment has also improved. Strengthened public finance management has enabled Africa to escape the boom-bust cycle associated with past upswings in commodity markets. There have been moves towards greater transparency and accountability – the twin pillars of good governance in natural resources. New legislation in the United States and the European Union will add further impetus to these moves. Many companies are now looking beyond short-term profits and towards long-term investment partnerships. These companies recognize the economic, as well as the ethical, case for strengthening linkages to local firms, for social and environmental impact assessments, and for engagement with local communities.

None of this is to understate the risks and challenges that come with Africa's ongoing resource boom. Surges in revenue have to potential to destabilize budget planning. Governments must make tough choices over how much to spend today and what to save for the future. There are risks that the fragile and, in some countries, still limited moves towards more open budget systems and enhanced disclosure in state extractive companies will be reversed. The Africa Progress Panel is concerned at foreign investors extensive use of offshore companies, shell companies and offshore jurisdictions. And much of Africa remains trapped in a pattern of exporting raw materials, with few countries successfully breaking into manufacturing and processing. None of this is inevitable – and our report demonstrates that the alternatives are practical, achievable and affordable.

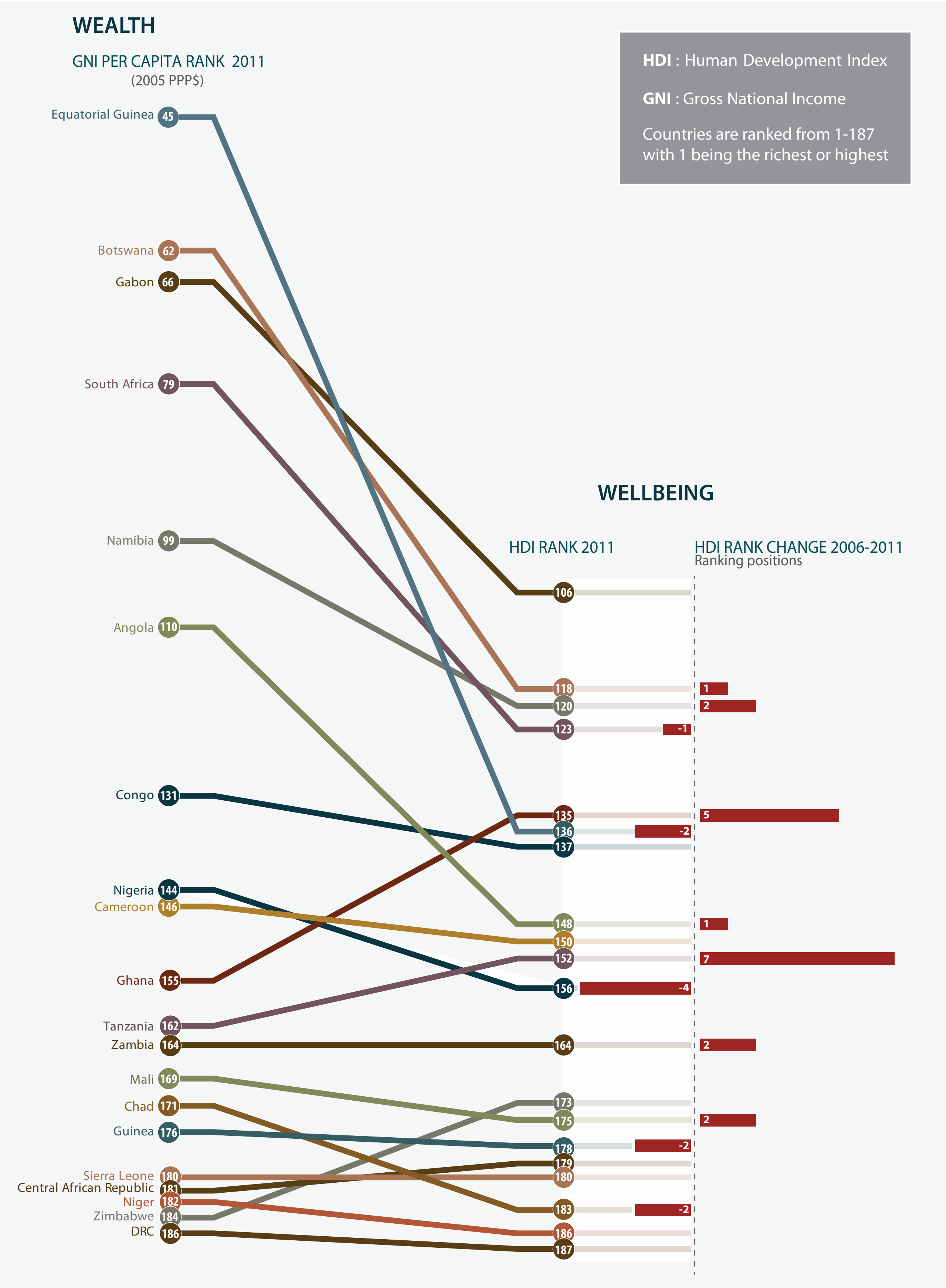
Rapid growth, but a mixed record on human development

The past decade has been a period of sustained growth in Africa. Despite a weaker global economy, regional growth has averaged over 5 per cent a year. Twenty resource-rich countries have been at the forefront of the economic recovery. These countries, accounting for 56 per cent of Africa's population, have grown on average more rapidly than other countries – and they include some of the world's fastest-growing economies. Half of the resource-rich group has seen average income rise by one-third or more. In 2012, Angola and Sierra Leone outperformed China; Ghana and Mozambique grew more rapidly than India.

Many resource-rich countries are moving up the international wealth rankings. Over the past decade, Cameroon, Ghana, Nigeria and Zambia have crossed the threshold from low-income to lower middle-income status. Another five countries – Angola, Botswana, Gabon, Namibia and South Africa – are in the upper middle-income group. Equatorial Guinea, with an average income of US$27,478 in 2011, is classed as a high-income country.

Progress on reducing poverty and improving human development has been less impressive. Resource-rich countries have some of the world's largest gaps between their global ranking on wealth, as measured by average income, and their performance on wider indicators for wellbeing, as captured by the Human Development Index (HDI). Equatorial Guinea's HDI ranking is 91 places below its average income rank, and Angola's is 38 places below. Moreover, resource-rich countries are heavily concentrated in the lower reaches of the HDI ranking. They account for 9 of the 12 last places, with the Democratic Republic of the Congo, bottom. (Figure 1)

Figure1: WEALTH/WELLBEING GAP



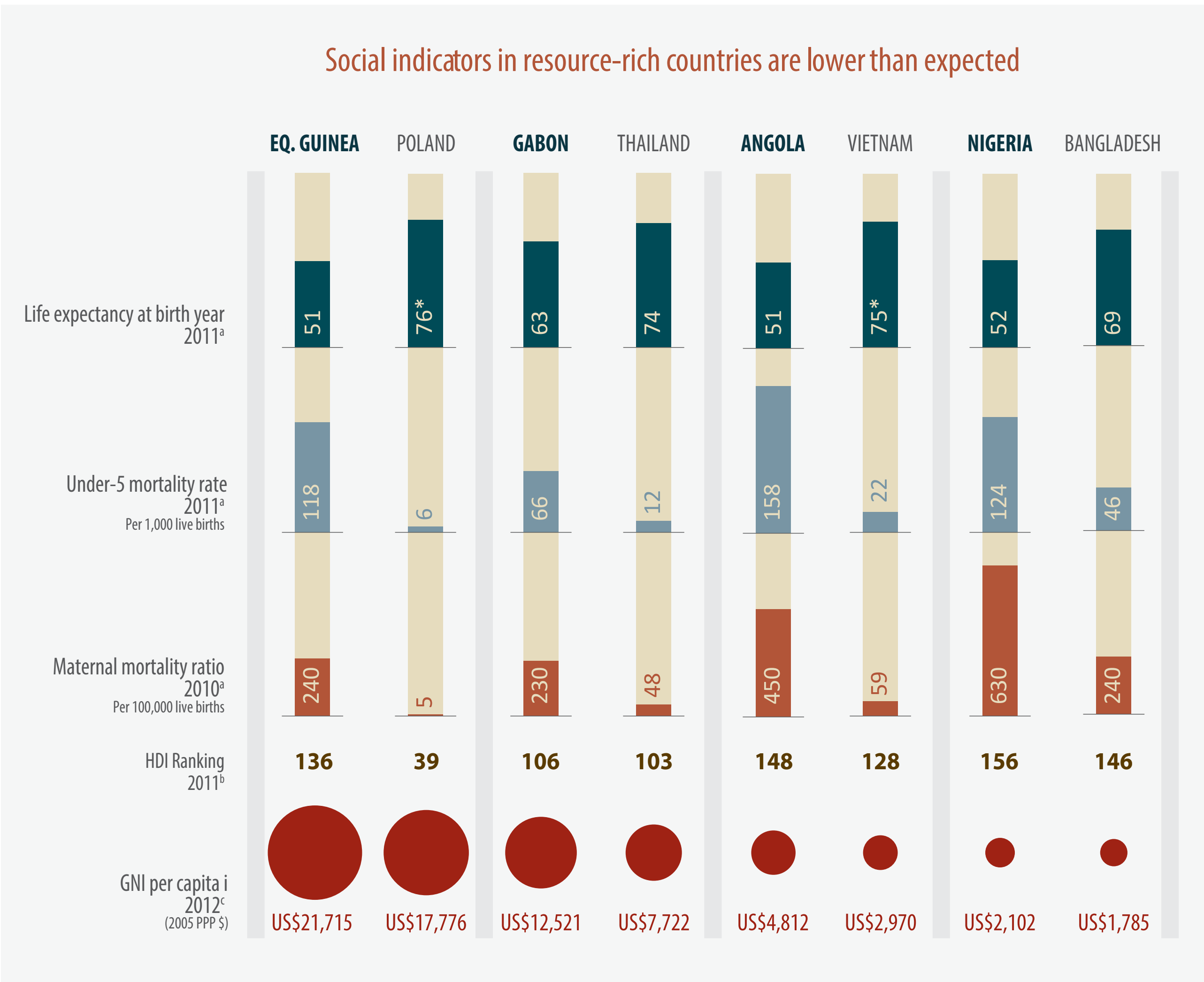
Source: UNDP (2011), Human Development Report.

International comparisons graphically illustrate the failure of many countries to convert resource wealth into expanded opportunities for human development. Bangladesh has a far lower average income than Nigeria, yet the country's children are three times less likely to die before their fifth birthday. And while Bangladesh has achieved universal primary education and gender parity, Nigeria has 10 million children out of school and some of the world's largest gender gaps. Angola has one of the world's highest maternal mortality rates. Eleven of the resource-rich countries – including high-income Equatorial Guinea – are in the group of 20 countries with the highest child mortality rates. (Figure 2)

High growth has not always reduced poverty. New research undertaken for the *Africa Progress Report* has explored the interaction between average income and the incidence of poverty in four countries. Both Ghana and Tanzania reduced poverty, though by far less than the amount predicted on the basis of their growth performance: Tanzania should have lifted another 720,000 people out of poverty. While Zambia registered strong growth, poverty levels increased by over half-a-million people. Nigeria also saw an increase in poverty.

Why have resource-rich countries been unable to use stronger economic growth to accelerate poverty reduction? While the precise answer to that question varies across countries, the underlying problem can be summarized in two words: rising inequality. In each of the four countries explored, almost all of the benefits of economic growth were captured by the richest 10 per cent. In Zambia, the income share of the poorest 10 per cent fell by half over the survey period examined, while the richest decile increased its share of national income by almost one-third, from 33 per cent to 43 per cent of the total.

Figure 2: LEFT BEHIND IN HUMAN DEVELOPMENT



Sources: a/ World Bank (2013), World Development Indicators. - b/ UNDP (2011), Human Development Report. - c/ UNDP (2013), Human Development Report.

* 2010

This pattern is consistent with the wider drift towards rising inequality. In last year's Africa Progress Report we cautioned that the rising disparities in wealth evident across the region are both unsustainable and unfair. That assessment applies with special force to resource-rich countries. These countries have an unprecedented opportunity to use resource wealth to reduce poverty faster. It is vital that governments seize that opportunity by distributing resource revenue more fairly.

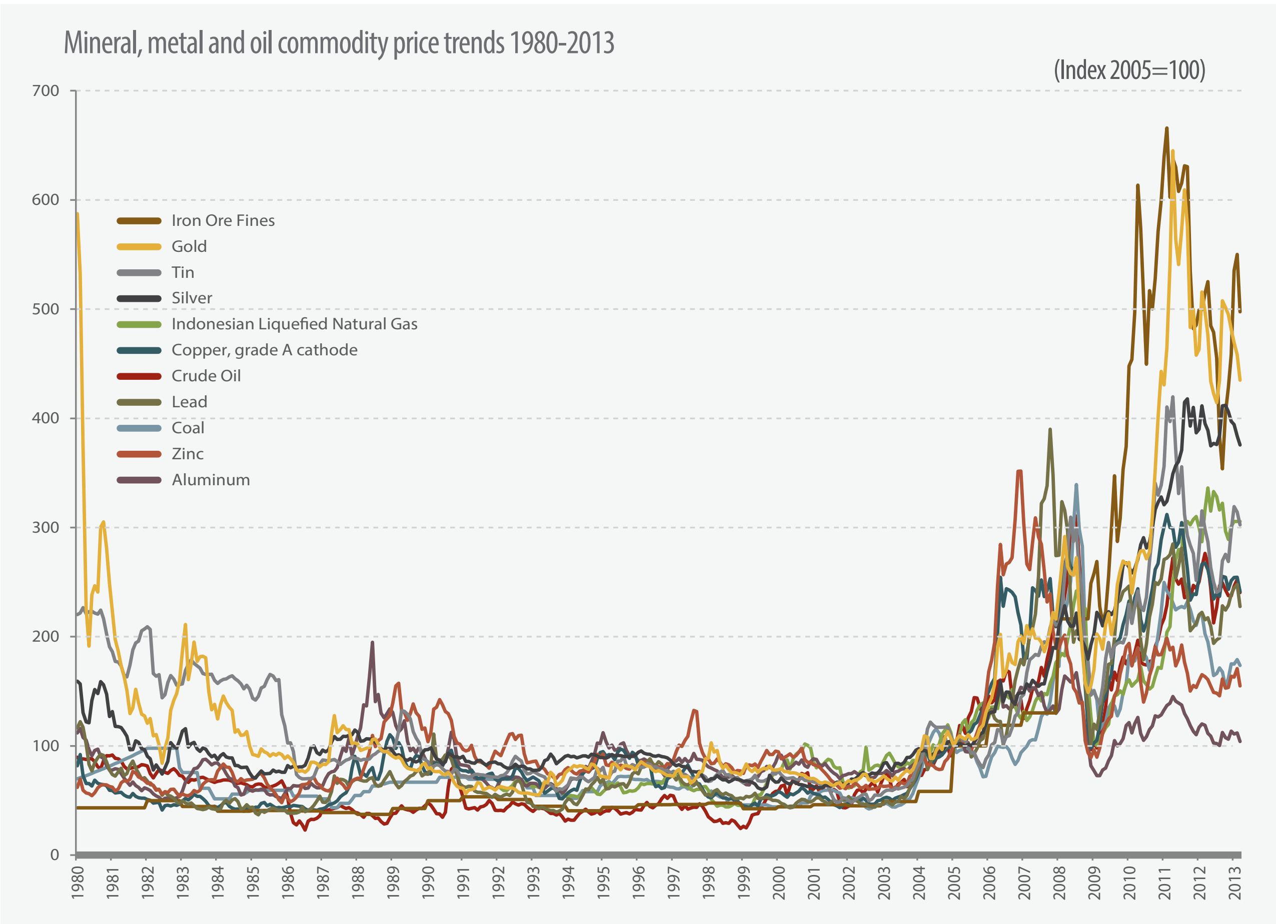
The same is true for other areas. Some countries have invested resource revenues in health, education, water and sanitation, expanding opportunities for the majority of their citizens. Yet the record is checkered. Some political elites continue to seize and squander the revenues generated by national resource, purchasing mansions in Europe and the United States or building private wealth at public expense. Angola's oil revenues have been used to amass personal fortunes and subsidize cheap water and electricity for the wealthy, while the poor are left without basic services.

Looking back over the past decade, it is clear that growth alone will not transform human development prospects in resource-rich countries. Governments need to ensure that the revenue streams that come with the growth of extractive industries are invested efficiently and equitably. Part of that investment has to be directed towards inclusive economic growth, since it is growth that will generate the jobs and future revenues needed to sustain progress. But for the millions of people lacking access to health, education, clean water, social protection and other basic services, it is imperative that governments use resource revenues to increase the quality and accessibility of those services.

Africa and the commodity super-cycle

Africa's resource-rich countries have been riding the wave of a global commodity market tide. Even though supply of some commodities is unpredictable, markets are set to remain tight over the coming years, with real prices remaining well above the average level of the 1990s. (Figure 3)

Figure 3: THE RISING TIDE OF COMMODITY MARKETS



Source: IMF Commodity Prices; World Bank Global Economic Monitor.

By the end of 2011, average prices for energy and base metals were three times as high as they had been a decade earlier, and were approaching or surpassing record levels over the past 40 years. Reflecting the underlying market conditions, mining investments increased more than fourfold between 2000 and 2010, reaching almost US$80 billion annually, and the value of world metals production rose at twice the rate of global GDP – a marked contrast with the stagnation in value of the previous decade. The upshot is that Africa has been integrating into one of the most dynamic sectors of world trade.

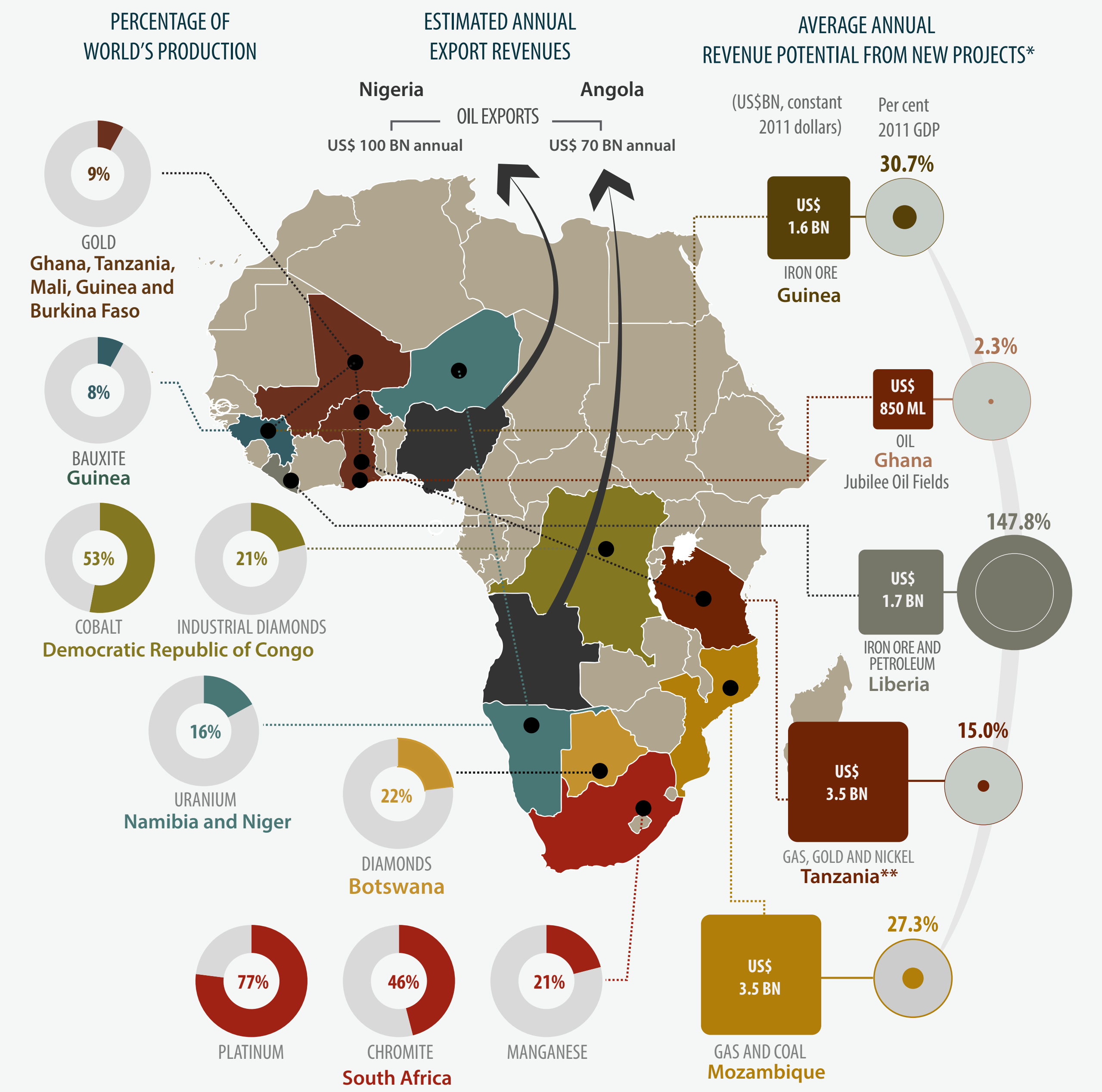
There is little evidence to suggest that a downturn is imminent. Some commentators maintain that the world is still in the middle phase of a commodity "super-cycle". Fuelled by high growth in emerging markets and constraints on supply, prices are set to remain high. Compared with prices in 2005, which were already well above average levels for the 1990s, projected prices for 2025 are around 20 per cent higher for metals and minerals, 25 per cent higher for energy commodities, and over 90 per cent higher for precious metals.

Such projections should not be interpreted as cause for over-exuberance. Africa is still a relatively minor player in inherently unpredictable global markets. Slower growth in China, global recession, increased investment in new sources of supply – such as natural gas extracted by "fracking" – and new technologies could fundamentally change underlying market conditions. African governments need to plan for uncertainty and the risks that come with dependence on exports, while preparing to manage increased revenues.

Increased exploration and rising foreign investment are deepening Africa's integration into global natural resource markets. In the energy sector, established oil producers are expanding production. The US Geological Survey estimates that the coastal areas of the Indian Ocean could hold more than 250 trillion cubic feet of gas in addition to 14.5 billion barrels of oil. To put this figure in context, it exceeds the known reserves of the United Arab Emirates and Venezuela. Africa's share of world gold exports is rising. Countries such as Zambia and the Democratic Republic of the Congo occupy a strategic place in world markets for copper and cobalt. More recently, there has been a global scramble to secure access to some of the world's largest and least developed iron ore deposits in Guinea, Liberia and Sierra Leone.

The revenue flows associated with Africa's natural resources are potentially transformative. The IMF estimates that revenue from Mozambique's natural gas and coal could reach US$3.5 billion annually. Iron ore exports from Guinea could generate over US$1.6 billion annually. Exports of natural gas, gold and other minerals could produce a revenue stream equivalent to 15 per cent of Tanzania's GDP. (Figure 4)

Figure 4: MAPPING AFRICA'S NATURAL RESOURCE WEALTH: SELECTED COUNTRIES AND COMMODITIES



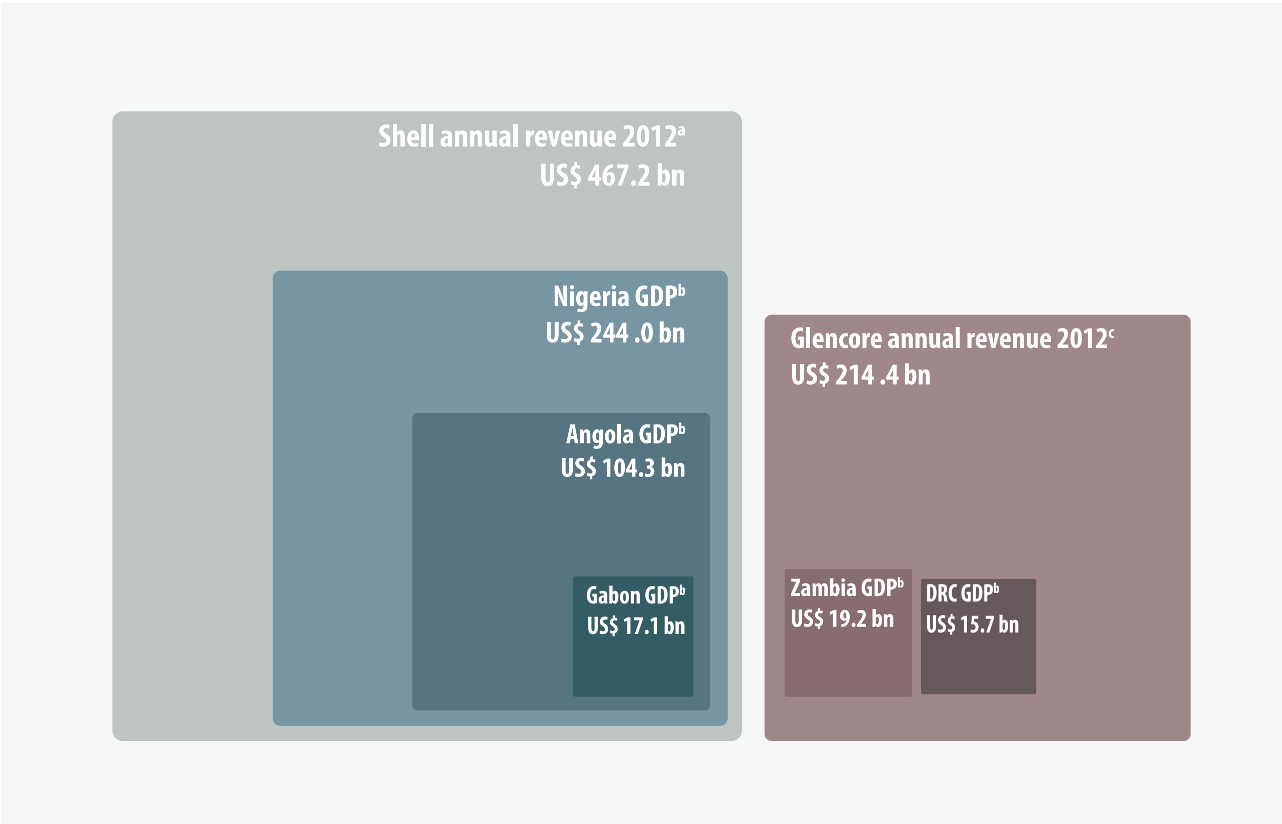
Sources:
Raw Materials Data, IntierraRMG, 2013
World Bank, Africa Pulse October 2012, Volume 6
IMF, Fiscal Regimes for Extractive Industries: Design and Implementation, 2012
U.S. Geological Survey, Mineral commodity summaries 2013
*Estimates are intended to show order of magnitude. Revenue projections are highly sensitive to assumptions about prices, phasing of production, and underlying production and capital costs
**Data represents annual revenue at peak production

The past decade has witnessed not just a surge in foreign investment activity, but a proliferation of actors. Companies active in Africa's extractive sectors range from the multinational firms that dominate world petroleum and mining to smaller and more specialized regional actors. State and private Chinese companies occupy an increasingly prominent role, as do firms from other emerging markets. Many of the foreign investors operating in Africa are following international best practice, often in a difficult operating environment. However, the Africa Progress Panel has identified two major areas of concern.

The first concerns the structure of investment activity. Foreign companies operating in Africa make extensive use of offshore-registered companies and low-tax jurisdictions. In some cases, multinational companies are also linked through their investment activities to complex webs of shell companies. These arrangements come with weak public disclosure and extensive opportunities for tax evasion. This is bad for efforts to strengthen transparency and accountability in Africa – and jeopardizes the reputations foreign investors.

The second area of concern relates to the linkages between foreign investment activity and local markets. Extractive industries typically operate as low-value added enclaves with weak linkages to local firm and employment markets. Over a decade into the commodity boom, Africa continues to export predominantly unprocessed raw material, and to import consumer goods and agricultural commodities. This is not a sustainable model of development. It is imperative that governments develop industrial strategies for adding value to raw materials prior to their export – and that foreign investors do more to build local linkages. (Figure 5)

Figure 5: MULTINATIONAL CORPORATION ANNUAL REVENUE VERSUS NATIONAL GDP DATA



Source: a/ Royal Dutch Shell plc (2012), Annual report: Building an energy future. - b/ World Bank (2011), World Development Indicators (GDP Data). - c/ Glencore (2012), Annual Report.

In 2012, overall private capital flows are estimated to exceed aid transfers by 8 per cent.[76] Foreign direct investment was similar to aid flows before the 2008 global recession before falling back slightly (Figure 6). That position has now been reversed, with the latest data pointing to a rise in FDI and a decline in aid. While the increase in private capital flows has reduced financial dependence on aid, development assistance remains a critical source of finance for a significant group of countries. Moreover, well-designed development assistance can support national efforts to use resource wealth to accelerate poverty reduction, notably by building institutional capacity.

Figure 6: PRIVATE FLOWS AND AID IN SUB-SAHARAN AFRICA

Source: OECD and UNECA (2013), Mutual Review of Development Effectiveness and the OECD-DAC International Development Statistics database.

From natural resources to human development

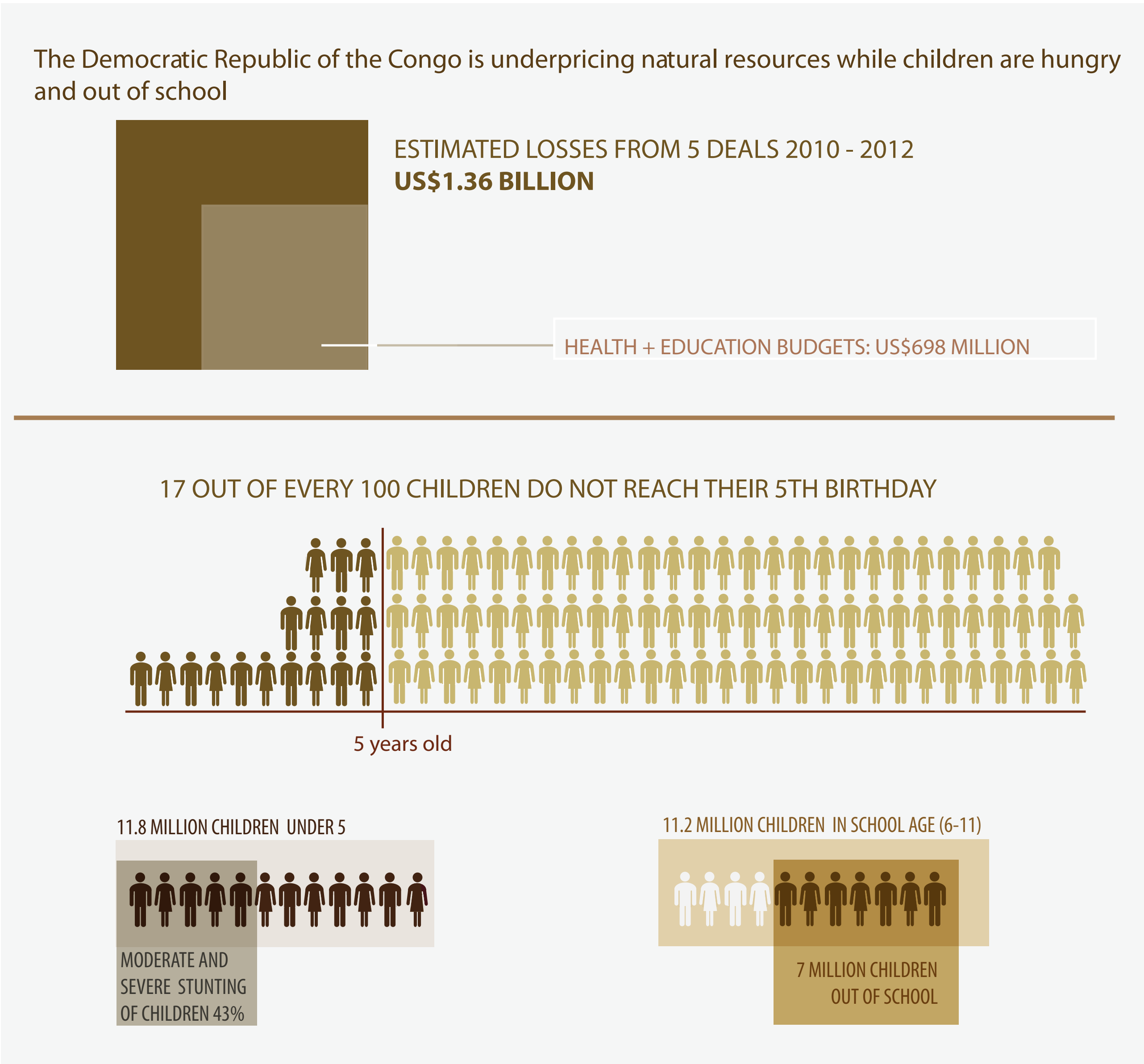
Translating natural resource wealth into human development requires integrated policies across a wide range of areas. Governments need national strategies that set out the terms on which resource wealth will be exploited, including provisions on sustainability, the regulatory environment and licensing. They also need to ensure that revenues are collected, accounted for and allocated efficiently and equitably to advance public policy goals. Moving from good principles to practice is not an easy journey.

Poor governance of state companies and assets is associated with extensive revenue losses. In 2012, Angola was unable to account for US$4.2 billion in "financing residuals", essentially missing money, in the accounts of the state oil company. Nigeria is estimated to have lost US$6.8 billion between 2010 and 2012. Revenue losses on this scale cause immense damage to public finance – and to national efforts to reduce poverty.

Concession trading arrangements are often associated with undervaluation of assets. No country has lost more from this practice than the Democratic Republic of the Congo. This report includes a detailed analysis of five privatization deals conducted through the sale of state-owned assets to foreign investors operating through offshore companies registered in the British Virgin Islands and other jurisdictions. We estimate the total losses sustained in these deals as a result of undervaluation of the assets at US$1.3 billion - –more than double total budget spending on health and education. In a country with 7 million children out of school, the sixth highest child mortality rate in the world, and endemic malnutrition, losses of this order carry high human costs. (Figure 7)

The underpricing of concessions generates large returns for offshore companies. In the case of the Democratic Republic of the Congo, we estimate that underpricing generated returns of around 500 per cent for the offshore companies involved. In Guinea, the price secured by another offshore company for a concession in iron ore

Figure 7: DEMOCRATIC REPUBLIC OF THE CONGO LOSSES IN CONCESSION TRADING VERSUS BUDGETS FOR HEALTH AND EDUCATION



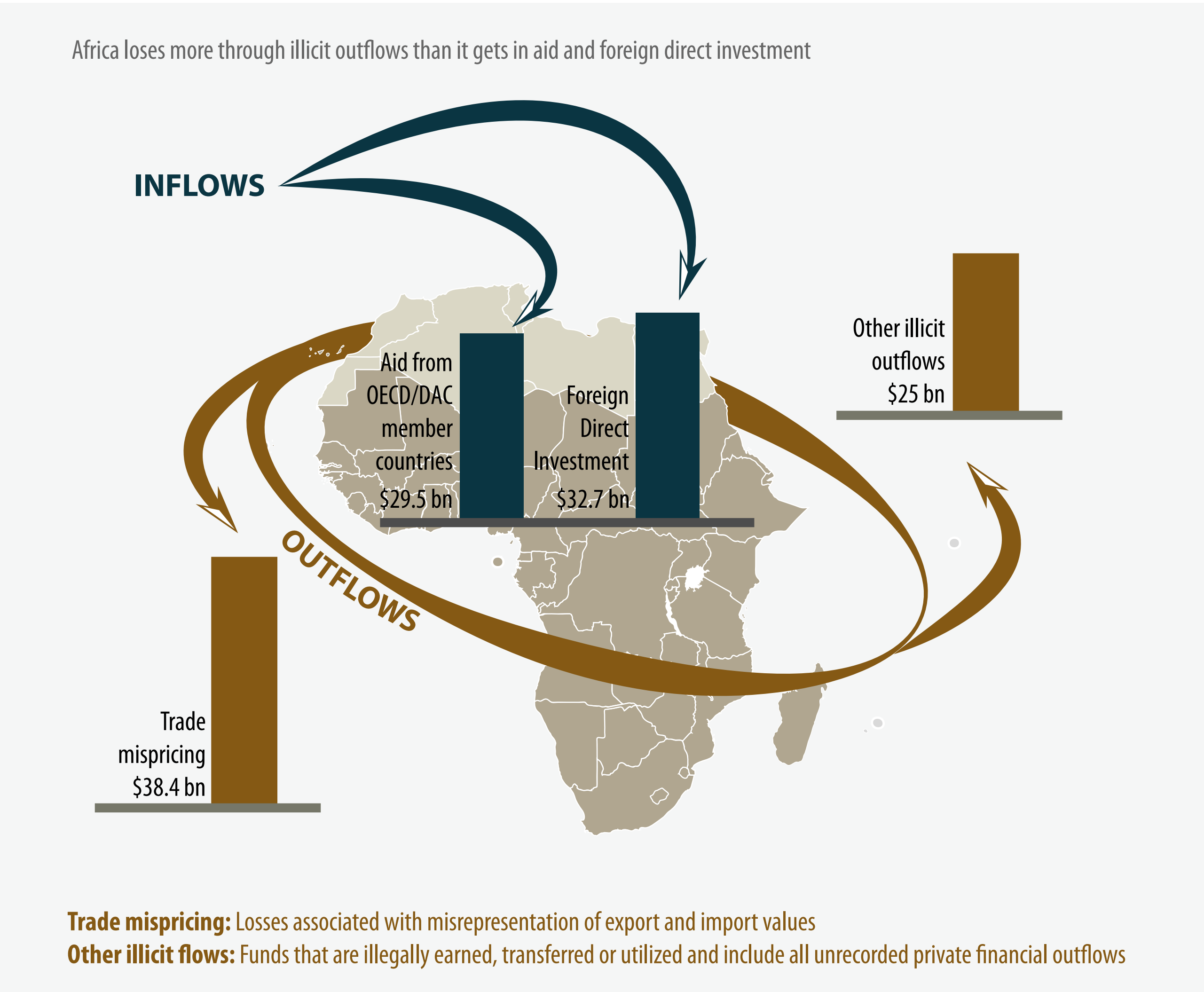
Source: IRIN (2011), DRC: Millions miss out on basic education. UNDP (2012), The Nutrition Challenge in Sub-Saharan Africa. UNESCO (2012), Global Monitoring Report. World Bank (2013), World Development Indicators represented a return in excess of 3,000 per cent, with the agreed price exceeding Guinea's GDP.

Lack of transparency remains a major concern. Resource-rich countries in Africa score poorly on the Resource Governance Index (RGI), a measure of the level of disclosure in the natural resource sector. Cameroon, the Democratic Republic of the Congo, Equatorial Guinea and Mozambique register some of the lowest scores reported on the RGI. Opaque practices in the natural resources sector are reinforced by opaque national budgets, with citizens routinely denied access to key budget documents.

Many resource-rich countries need urgently to review the design of their tax regimes. Most were designed to attract foreign investment during a period of low commodity prices. Countries have provided extensive tax concessions, including "tax holidays", low royalty payments, and exemptions from corporation tax. One review in Zambia found that between 2005 and 2009, half a million workers in the country's copper mines were paying a higher rate of taxation than major multinational mining companies. The IMF and the African Development Bank have urged governments to reconsider the level of tax concessions that they provide.

Tax evasion continues to erode the revenue base for public finance in many countries. It is impossible to quantify the scale of the problem. However, high levels of intra-company trade create extensive scope for trade "mispricing", enabling companies to report profits in low-tax jurisdictions; and the extensive use of offshore companies and shell companies makes it difficult for African tax authorities to assess profits and enforce compliance. Trade mispricing alone is estimated to have cost Africa on average US$38 billion annually between 2008 and 2010 – more than the region received in bilateral aid from OECD donors. Put differently, Africa could double aid by eliminating unfair pricing practices. (Figure 8)

Figure 8: AFRICA'S ILLICIT OUTFLOWS



(All figures are average annual 2008-2010 for Sub-Saharan Africa)

Source: OECD (n.d.), OECD Stats Extracts.
Global Financial Integrity (2012), Illicit Financial Flows from Developing Countries 2001-2010.
World (2013), Global Economic Prospects – January 2013.

Converting resource revenues into tangible human development gains and expanded opportunity requires efficient and equitable public spending. The record of resource-rich countries in this area is mixed, but far from encouraging. Several countries – Chad is a notable example – under-invest in basic services. Countries such as Ghana, Kenya and Zambia skew public spending on health, education and infrastructure away from the most disadvantaged areas. As a group, resource-rich countries under-invest in social protection. The 1.5 per cent of GDP spent by Nigeria provides limited coverage. One of the main programmes, Care of the People, provides modest grants to only 22,000 households (0.001 per cent of the poor).

Unlocking the potential

The immense challenges that African governments face have practical and achievable solutions. Governments can also draw upon a wide range of guides to action. The Africa Mining Vision, jointly prepared by the African Union and the Economic Commission for Africa, sets out a compelling agenda for using resource wealth to boost inclusive growth, expand opportunities and reduce poverty faster. The Natural Resource Charter, which draws on international best practice, is another valuable tool that can help to frame policies.

Many African governments are leading by example. Reform-minded political leaders, supported by civil society, have used the Extractive Industries Transparency Initiative (EITI) to strengthen disclosure standards. Sierra Leone now publishes contracts and concessions online. In February 2012, Guinea published on a government website more than 60 contract documents covering 18 mining projects, along with a searchable summary of contract terms, allowing non-experts to find key sections and understand the obligations of companies and the government. The new Liberian Draft Petroleum Policy has a section devoted to transparency measures that will influence the eventual drafting of sector legislation. It includes provisions requiring the disclosure of the beneficial ownership structure of mining companies, revenue forecasts and oil sale price information. Ghana's 2011 Petroleum Revenue Management Act exceeds EITI reporting standards. These initiatives reflect the political impetus towards greater transparency and accountability in Africa.

International initiatives are supporting Africa's efforts. Under the Dodd-Frank legislation introduced in the United States, the Securities Exchange Commission will require companies involved in extractive industries to publicly disclose all payments on a project-by-project basis. The legislation, which has prompted parallel moves from the European Union, provides an opportunity for foreign investors to support Africa's efforts to strengthen transparency and accountability. Unfortunately, many companies have failed to grasp that opportunity. Some have initiated legal challenges seeking to overturn Dodd-Frank provisions. Others have embarked on a campaign of attrition aimed at diluting mandatory reporting requirements. This is short-sighted – and the commercial arguments deployed in favour of weaker disclosure lack credibility.

Not all of the opposition emanates from industry. The Canadian government has opposed the introduction of mandatory disclosure standards. This matters because companies listed on the Toronto stock exchanges control global mining assets in excess of US$109 billion and in 2011 were involved in over 330 projects in Africa. China's stock exchanges, most notably in Hong Kong and Shanghai, also need to be brought into a more transparent multilateral regime.

Several governments in Africa are introducing more efficient and balanced tax regimes. Royalty rates have been increasing, reflecting the escalation in world prices. The African Development Bank has proposed indexing royalty payments to world prices, which would improve stability and predictability in tax administration. The IMF has urged governments to avoid negotiating tax deals on an investor-by-investor basis, and several countries have successfully renegotiated what were unbalanced arrangements.

However, African governments acting alone cannot resolve some of the most pressing tax problems facing the region. Tax evasion is a global problem facilitated by a mixture of intra-company trade practices, the extensive use made by foreign investors of offshore centres, shell companies and low-tax havens, and weak disclosure standards in a number of financial and commodity trading centres, including Switzerland, the United Kingdom and the United States. While there have been encouraging moves towards greater international dialogue on taxation, what is lacking is decisive international action – and this is an area in which the G8 and the G20 can make a difference.

In the past, fiscal policy has been an Achilles' heel of resource governance in Africa. Surges of revenue have led to bouts of uncontrolled public spending, without subsequent adjustment during downturns in the commodity cycle. This picture is changing. Governments are setting a reference price for resource exports, smoothing flows into the budget across the commodity cycle and placing surpluses into sovereign wealth funds and other instruments. Nigeria's recently established sovereign wealth fund has drawn on the experience of other countries in the region and beyond – including Botswana and Chile – to establish clear and transparent rules managing resource flows.

Effective fiscal management does not provide answers to key questions over spending. All governments have to consider the capacity of national economies to absorb increased spending financed by resource revenues. Saving for the future is an important policy goal. However, the Africa Progress Panel believes that there should be a presumption in favour of "front-loaded" expenditure – investing early in infrastructure and basic services. Evidence shows that returns to investment in infrastructure can be very high, typically ranging between 15 per cent and 20 per cent, and the World Bank estimates that infrastructure investments could raise Africa's long-term growth rate by 2 per cent a year. By contrast, returns to savings in secure bond markets are currently well below 1 per cent, implying a negative return when adjusted for inflation.

Spending priorities have to be determined in the light of national dialogue. Two guides to action stand out. The first is that investment geared towards long-term, inclusive growth is critical. Governments need to ensure that the revenues generated by non-renewable natural resource assets are turned into permanent improvements in economic infrastructure and in people's health, education, welfare and livelihoods. Unless growth continues, increased spending in basic services will become unsustainable. At the same time, it is difficult to make a case for saving a large share of resource revenues when some 30 million African children are out of school, when the region's health system is unable to deliver basic care to a large share of its population, and when climate risk continues to trap smallholder farmers.

The second priority, therefore, is to use the revenues generated by resource exports to break the cycle of poverty trapping millions of Africans, and to unlock opportunities. These revenues can be used to eliminate charges on basic services, to expand provision for the most marginalized groups and areas, and to raise both the quality and accessibility of health care and education. Part of the resource windfall could also be invested in developing national social protection systems, drawing on the best regional practices of countries such as Rwanda and Ethiopia, and on relevant experience from other regions.

SHARED AGENDA FOR CHANGE THAT BENEFITS ALL

Africa's natural resource wealth is an asset with the potential to lift millions of people out of poverty and build shared prosperity for the future. This report has identified some of the policies that could realize that potential by enabling Africa's people, governments, civil society, foreign investors and the wider international community to come together around a shared agenda for change.

These policies offer pathways towards win-win scenarios. When governments strengthen disclosure standards and improve accountability, they improve their legitimacy in the eyes of their citizens. When foreign investors adopt more stringent disclosure standards and avoid irresponsible practices including tax evasion, they stand to gain from improved standing in the host countries – and from the avoidance of risks that could damage shareholder interests. If the international community comes together to tackle tax evasion, rich countries as well as poor will gain as the losses associated with aggressive tax planning diminish.

By the same token, when there is a deficit of trust there are no winners – and resource governance in Africa has long been blighted by a lack of trust. Millions of Africans have lost trust in the capacity and concern of their governments to manage what are public natural resource assets in the public interest.

Governments and many of their citizens question the motives and practices of foreign investors, while the companies themselves often have little confidence in the governments that shape the policy environment in which they operate. Building trust is harder than changing policies – yet it is the ultimate condition for successful policy reform. Civil society organizations have played a central role in strengthening transparency and accountability and they often partner effectively with all key stakeholders groups highlighted below. Their role is fundamental to implementing most of the recommendations below.

Africa has never suffered from a "resource curse". What the region has suffered from is the curse of poor policies, weak governance and a failure to translate resource wealth into social and economic progress. The favourable market conditions created by global resource constraints provide no guarantee that the growth of extractive industries will lead to improvements in the lives of people. But if governments seize the moment and put in place the right policies, Africa's resource wealth could permanently transform the continent's prospects.

RECOMMENDATIONS FOR IMMEDIATE ACTION

TRANSPARENCY AND ACCOUNTABILITY	**Adopt a global common standard for extractive transparency:** All countries should embrace and enforce the project-by-project disclosure standards embodied in the US Dodd-Frank Act and comparable EU legislation, applying them to all extractive industry companies listed on their stock exchanges. It is vital that Australia, Canada and China, as major players in Africa, actively support the emerging global consensus on disclosure. It is time to go beyond the current patchwork of initiatives to a global common standard. **Realize the Africa Mining Vision:** Adopt the Africa Mining Vision's framework for "transparent, equitable and optimal exploitation of mineral resources to underpin broad-based sustainable growth and socio-economic development" as the guiding principle for policy design. Immediately equip the African Minerals Development Centre with the technical, human and financial resources it needs to help governments develop national strategies. Implement the Africa Mining Vision at country level, including a strenghtened EITI provision. **Use the African Peer Review Mechanism:** Assert African leadership in reforming the international architecture on transparency and accountability by implementing the African Peer Review Mechanism's codes and standards on extractive industry governance.
DISTRIBUTION OF BENEFITS	**Build a multilateral regime for tax transparency:** The G8 should establish the architecture for a multilateral regime that tackles unethical tax avoidance and closes down tax evasion. Companies registered in G8 countries should be required to publish a full list of their subsidiaries and information on global revenues, profits and taxes paid across different jurisdictions. Tax authorities, including tax authorities in Africa, should exchange information more systematically.
ECONOMIC TRANSFORMATION	**Boost linkages, value addition and diversification:** Add value by processing natural resources before export. Forge links between extractive industries and domestic suppliers and markets to contribute towards value addition. Structure incentives to favour foreign investors who build links with domestic suppliers, undertake local processing and support skills development. Use linkages to diversify national economies away from dependence on extraction.
RESOURCE REVENUES AND PUBLIC SPENDING	**Ensure equity in public spending:** Strengthen the national commitment to equity and put in place the foundation for inclusive growth: African governments should harness the potential for social transformation created by increased revenue flows. Finance generated by the development of minerals should be directed towards the investments in health, education and social protection needed to expand opportunity, and towards the infrastructure needed to sustain dynamic growth.
SOCIAL AND ENVIRONMENTAL SUSTAINABILITY	**Protect artisanal mining:** Support artisanal mining, which is labour-intensive and provides precious jobs. The formal extractive sector and informal artisanal mining both stand to gain from constructive arrangements that recognize the rights of artisanal miners and protects the interests of all investors.

The Africa Progress Panel promotes Africa's development by tracking progress, drawing attention to opportunities and catalyzing action.

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