The $3.5 Trillion Question: How to Make Natural Resource Funds Work for Citizens
What is a natural resource fund (NRF)?

- Government-owned
- Macroeconomic objective(s)
- At least a portion invested in foreign assets
- Source of financing: oil, gas or mineral revenues
- NOT a bank, national oil company or central bank reserves
Looking at governance: 2 types of NRFs

Some have helped countries escape the “resource curse.”
- Chile
- Norway
- Some Persian Gulf states
- Several U.S. states

Others have been mismanaged, not met objectives or become slush funds.
Some in:
- Central Asia (e.g., Russia)
- Latin America (e.g., Venezuela)
- MENA (e.g., Libya)
- SE Asia (e.g., Brunei)
- Africa (e.g., Equatorial Guinea)

What has made the difference are the rules, institutions and broad-based consensus.
Governance matters.

There is no international consensus on “good governance” or even “NRF”.

Policymakers need tools and resources to establish or reform funds.

Is there a governance blueprint that can be followed to make NRFs work for citizens?
Identified 54 NRFs ($3.5 trillion in assets as of end-2013)

Surveyed 22 NRFs in 18 national and subnational jurisdictions, based on institutional structure, investments, transparency, accountability and fiscal rules
Each NRF profile includes a rating of good governance standards.

What are our findings?
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- $3.5 trillion in AUM
- Massive proliferation of funds – the new “must-have” for new producers
- NRFs adopting more rules, but major problems with compliance
- Some rules more common than others; more focus on management structure than investment risk limitations, transparency or oversight
- Funds becoming more transparent; yet only about half of the funds studied release audits or publish specific investments (most do not)
How to improve governance: a 6-step process

1. Set the fund objective(s)
2. Establish fiscal rules aligned with the objective(s)
3. Establish investment rules
4. Clarify institutional structure and rules of conduct
5. Require regular and extensive disclosures and audits
6. Establish strong independent oversight bodies
Step 1: Set clear fund objectives

- Saving for future generations
- Stabilization
- Sterilizing capital inflows
- Earmarking for specific expenditures
- Ring-fencing resource revenues

What matters: clarity, consistent operational rules, adapted to the needs of the economy
Step 2: Establish fiscal rules

Fiscal space

- Government oil income
- Fiscal space under bird-in-hand rule
- Fiscal space under PIH rule
- Fiscal space under an intermediate rule
## Step 2: Establish fiscal rules

### Azerbaijan
- Lack of a withdrawal rule
  - Discretionary withdrawals
  - Government spends lavishly when oil prices are high
  - Leading to cuts when oil prices have declined

### Alberta
- Lack of a deposit rule
  - Between 1987 and 2013 only two deposits made of less that $4 billion combined.
  - Change in 2013

### Chile
- Even when fiscal rules are established by law, room for manipulation remains (e.g., Ghana, Trinidad and Tobago, Timor-Leste)
- Chile has independent committees to make forecasts and fiscal assessments
Step 3: Establish investment rules

- **Need for explicit rules that limit risk**
  - Allocation between cash, fixed income investments, equities and alternative assets
  - Prohibition of certain high-risk financial instruments or volatile currencies
  - Limit use of resource revenues as collateral?

- **Domestic investment directly by the fund or through the budget?**
  - No domestic investment: ADIA, Botswana, Chile, Kazakhstan, Norway
  - Bypass the budget: Angola, Azerbaijan, Iran, Russia
Step 3: Establish investment rules

- **Cautionary tales**
  - Angola – from 2000-04, borrowed $9 billion backed by oil during IMF debt restructuring negotiations
  - Kuwait – lost $5 billion in the 1990s on speculative investments
  - Libya – lost nearly all of $1.2 billion investment in derivatives during the 2007-08 financial crisis
Step 4: Clarify good institutional structure

Norwegian illustration

- **Stortinget (Norwegian parliament)**
  - Government Pension Fund Act

- **Ministry of Finance**
  - Management mandate
  - Ethical guidelines

- **Norges Bank (central bank) Executive Board**
  - Executive Board principles
  - Investment mandate
  - CEO job description

- **NBIM committees**
  - Advisory forum to NBIM CEO

- **NBIM CEO**
  - NBIM policies
  - The CEO also delegates investment mandates and job descriptions

- **NBIM risk management and compliance**

- **Norges Bank Investment Management (NBIM) Leader Group**
  - The leader group sets specific investment guidelines and delegates work tasks
Step 5: Require extensive disclosure and audit

- Easy access to comprehensible legislation or quarterly reports that include:
  - governance rules
  - size of funds
  - returns on investments
  - specific assets
  - investment strategy
  - names of fund managers

- Public disclosure of internal and external audits
Independent oversight promotes compliance with the rules.

Managers of NRFs should be accountable to:
- the legislature
- comptroller, auditor-general or other independent formal supervisory body
- the judiciary
- civil society and the press
- even the IMF or other policy institutes

Example:
Ghana’s Public Interest and Accountability Committee (PIAC)
Working with small budget and no enforcement powers
Uses and future issues

Strengthening governance: Making NRFs work for citizens

- Easy-to-access “benchmarks” against other NRFs:
  - Website: www.revenuewatch.org/nrf
  - Fund profiles
  - Policy memos on NRF governance
  - Interactive map

- Training, capacity building and technical assistance

- Need international consensus on what constitutes good NRFs and advocate for consensus with governments
Thank you.

The full RWI-VCC report, briefs and NRF profiles are available at www.revenuewatch.org/nrf