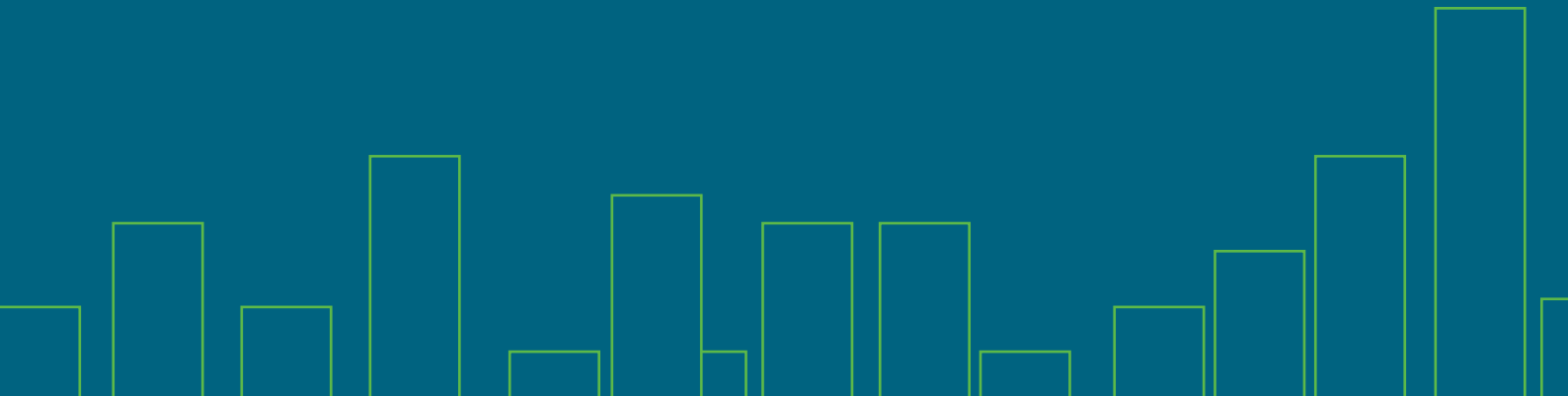


Managing the accumulation of internal arrears in Guinea

Practice Notes

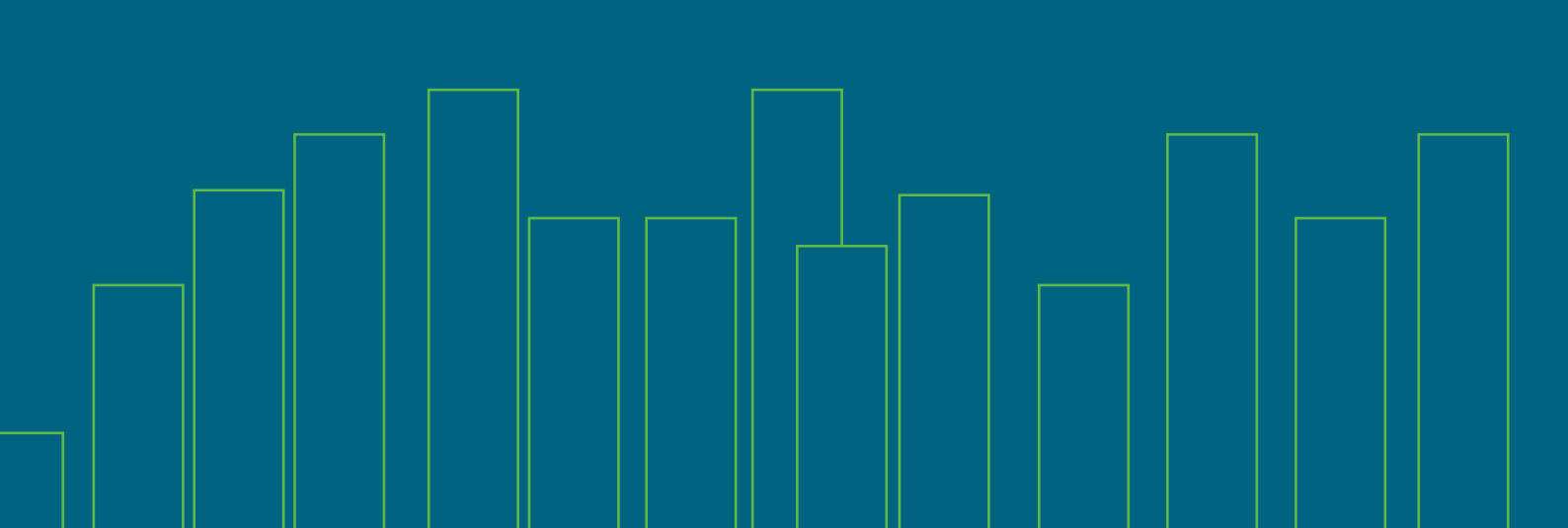


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Acronyms and abbreviations

BPFC	Building Public Finance Capabilities
EDG	<i>Électricité de Guinée</i> (Electricity of Guinea)
GDP	gross domestic product
GNF	Guinean franc
IMF	International Monetary Fund
MDAs	ministries, departments and agencies
MoEFP	Ministry of the Economy, Finances and Planning
PDIA	Problem-Driven Iterative Adaptation
PFM	public financial management
STA	Single Treasury Account

Acknowledgements

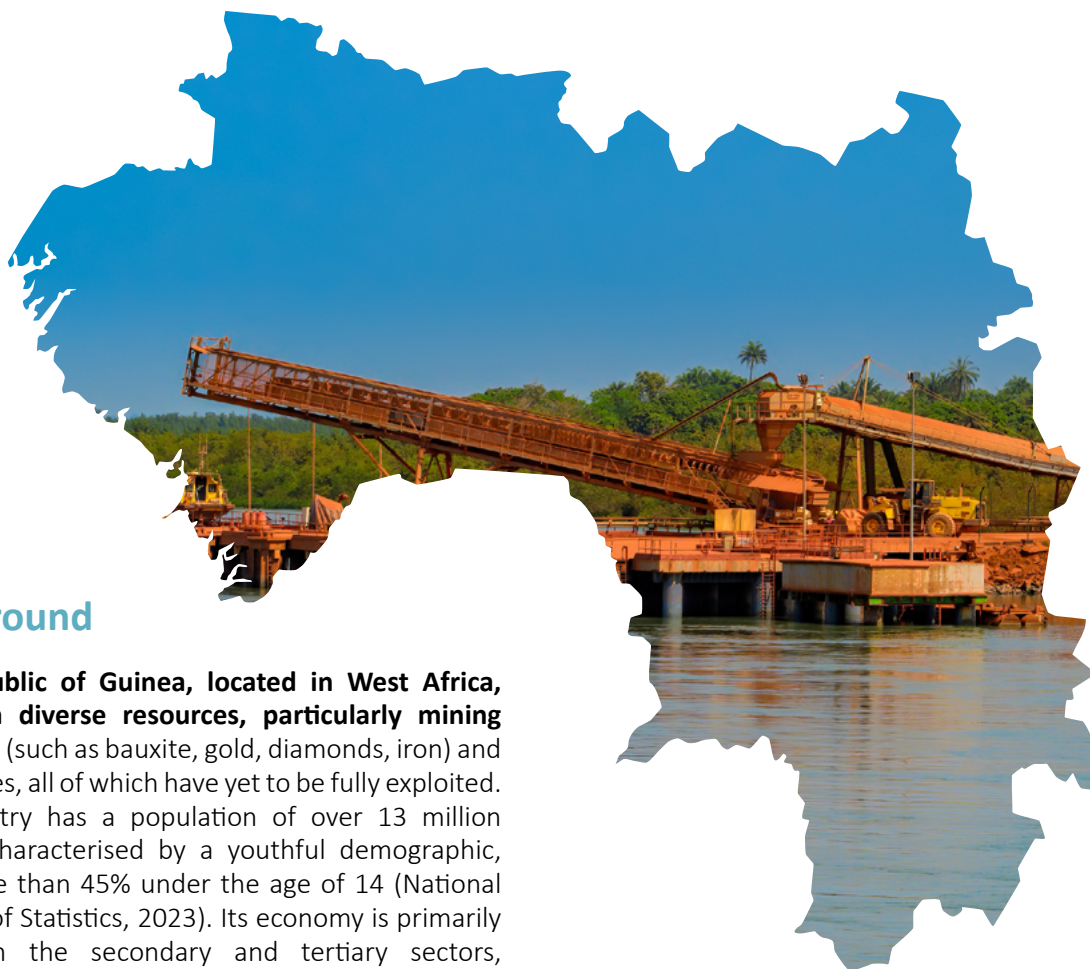
This report was originally prepared in French and translated into English. It was prepared by Mrs Yacine Bio-Tchané, in collaboration with Mrs Joana Bento (CABRI Secretariat) and inputs from the Guinean Sily team, and in particular, Mrs Doré Soua and Mrs Sylla Abdourahmane, Mr Barry Thierno Ibrahim, Mr Diallo Mamadou Mouctar, Mr Camara Soufiane and Mr Diane Ousmane. We would also like to thank Mr Thierno Amadou Bah, Secretary-General of the Ministry of Budget, for his leadership and support for the work of the team.

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AFRICAN DEVELOPMENT BANK GROUP

1. Introduction



Background

The Republic of Guinea, located in West Africa, is rich in diverse resources, particularly mining resources (such as bauxite, gold, diamonds, iron) and oil reserves, all of which have yet to be fully exploited. The country has a population of over 13 million people, characterised by a youthful demographic, with more than 45% under the age of 14 (National Institute of Statistics, 2023). Its economy is primarily based on the secondary and tertiary sectors, which contribute an average of 2.15% and 1.15% , respectively, to the country's growth (MoEFP, 2024).

Guinea's economy has demonstrated a certain degree of resilience despite facing both internal and external setbacks over the past decade. In the post-COVID period, the country achieved notable growth, with an upward trend of 5% between 2020 and 2023 and maintained a moderate and conservative debt level (36.2% of GDP in 2023) (MoEFP, 2024). However, this progress has been undermined by political instability, including a coup d'état in September 2021 and a high turnover of administrative personnel. Additionally, the country experienced a high inflation rate, averaging 10% between 2020 and 2023, along with precarious social conditions. Guinea ranks very low on the Human Development Index, occupying the 182nd spot out of 191 countries in 2021/2022.

Public finances present a mixed picture, with efforts made to improve the mobilisation of domestic resources, which reached 13.7% of GDP in 2023 (MoEFP, 2024). However, this is below the 15% average for sub-Saharan Africa. In terms of expenditure, there was a significant upward trend between 2020 and 2021 (24% growth), but growth has been more moderate between 2021 and 2023 (6%) (MoEFP, 2024). Overall, public finances have been quite restrictive to reduce the budget deficit, which decreased from 4.2% to 0.3% of GDP between 2020 and 2022 (MoEFP, 2024); however, between 2022 and 2023, the deficit widened again to 2.2%.



The problem of payment arrears

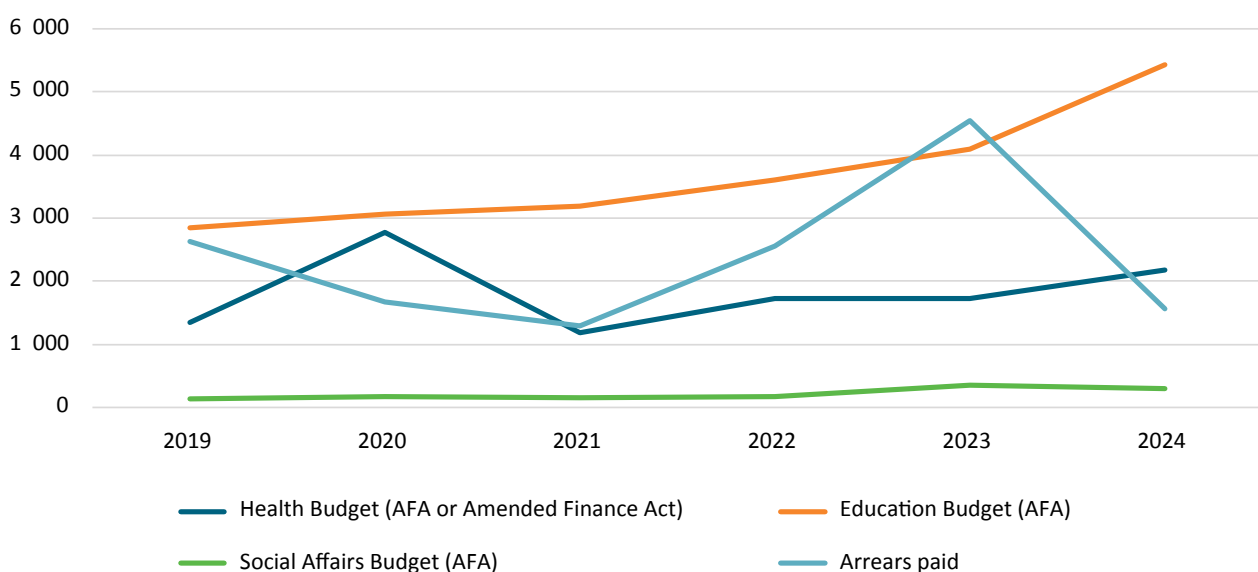
In Guinea, **these arrears refer to the financial obligations of the state for services rendered that have not been paid within a period of 90 days.** Between 2021 and 2023, the stock of arrears, or the total amounts remaining due, came to a total 3,925 billion GNF, equivalent to 14% of public expenditure.

These arrears are predominantly composed of state subsidies (63%), followed by investments (21%), and lastly goods and services provided by service providers (16%). Included in the state subsidies are those to *Électricité de Guinée* (EDG) (Electricity of Guinea), which accounts for 56% of all the arrears. EDG has a special status with the government as the Prime Minister determines the subsidies granted to

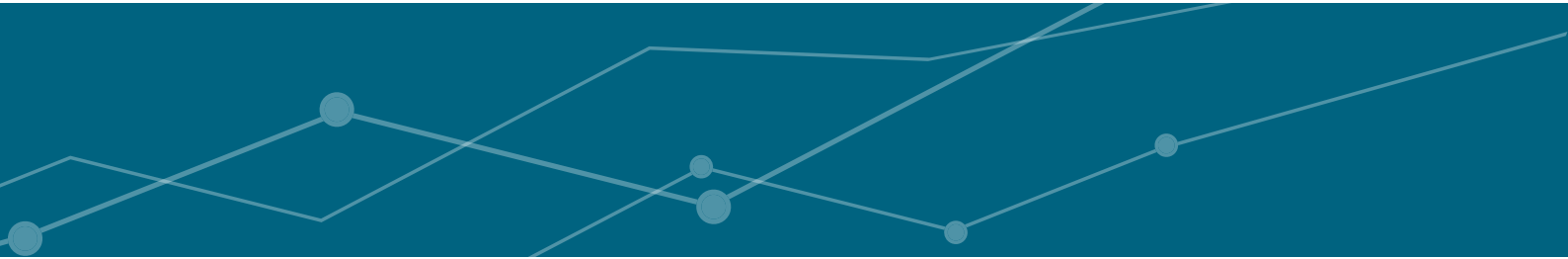
EDG in the guidelines and budget stance. Up to 2024, these arrears represented duly incurred expenses as well as extrabudgetary and political sovereignty expenses.

The stock of arrears outstanding in 2023 slightly exceeds the education budget (11%), amounts to more than double the health budget, and is nearly 12 times that of the social affairs budget. Although this particular year (2023) saw a peak in the amount of arrears paid, the gap between the amounts of arrears paid and the health and social welfare budgets has been growing appreciably wider since 2021. However, only in 2023 did the trend in education start reversing.

Figure 1: Payment of arrears compared to social sector budgets (billions of GNF)



Source: Ministry of Budget



Apart from the budgetary implications caused by the accumulation of arrears, a study by the African Department of the International Monetary Fund (IDA and IMF, 2018) illustrates the effects of internal (or domestic) arrears on key macroeconomic aggregates in sub-Saharan Africa: a decline of 0.33% in growth and 0.2% in tax revenue as percentages of GDP. Moreover, the impact on companies is also significant: turnover dropped by 4.68 percentage points, job creation decreased by 2.54 percentage points and productivity declined by 5.43 percentage points (IMF, 2024).

For Guinea, the impact of arrears is undeniable with regard to growth, the expansion of the private sector and confidence in state institutions. Moreover, the new status of lower middle-income country assigned to Guinea by the World Bank could increase debt-servicing levels, squeeze out the payment of arrears and further worsen the situation. Furthermore, **the absence of an arrears clearance strategy in the national budget, without deprioritising essential social sectors approved by the government, is concerning.**

In this context, a multidisciplinary team (the Syli team) comprising officials within the Ministry of Budget and the Ministry of the Economy, Finance and Planning (MoEFP) – represented by the Directorates of Treasury and Debt and Public Development Aid – have formulated a problem on the accumulation of Guinea’s internal arrears within the context of CABRI’s Building Public Finance Capabilities (BPFC) in Africa programme.

CABRI’s BPFC is a 12-month action-learning programme designed to build local capabilities in solving public finance problems at the local level. The programme recognises that public finance management (PFM) does not lend itself to a one-size-fits-all approach. In addition to technical fixes, sustainable PFM solutions require an in-depth understanding and judicious management of political economy constraints.

Accordingly, the BPFC programme applies the Problem-Driven Iterative Adaptation (PDIA) approach, developed in response to challenges identified in

multiple evaluations of the impact of PFM reforms over the past 30 years. These evaluations revealed certain gaps (Andrews, 2013; Fritz, Verhoeven and Avenia, 2013) related to:

1. Reproducing international best practices that, in some cases, were not appropriate for resolving local problems;
2. Poor adherence and limited commitment by local agents, leading to resistance to change;
3. Excessively rigid approaches to reform that did not allow for adaptation to local context solutions.

In response to these challenges, the PDIA approach and the BPFC programme are based on the following principles:

1. Local solutions to local problems: Problems identified locally draw attention and facilitate the development of solutions appropriate to that context.
2. Local ownership of reforms: Officials within various institutions are best placed to undertake reforms, as they understand their local context and can mobilise the necessary support.
3. Experimentation, learning and adaptation: Reforms require a constant review of what works and what doesn’t, as well as adaptation and iteration over time or as new learnings are uncovered.
4. Positive deviance: the emergence of appropriate local solutions requires the creation of environments across organisations that encourage experimentation and positive deviance.
5. Scaling through diffusion: The crucial involvement of stakeholders from all organisations ensures that reforms are viable, legitimate and relevant.

The BPFC programme is structured in a way that facilitates officials’ practical and experimental learning to solve complex public finance problems.

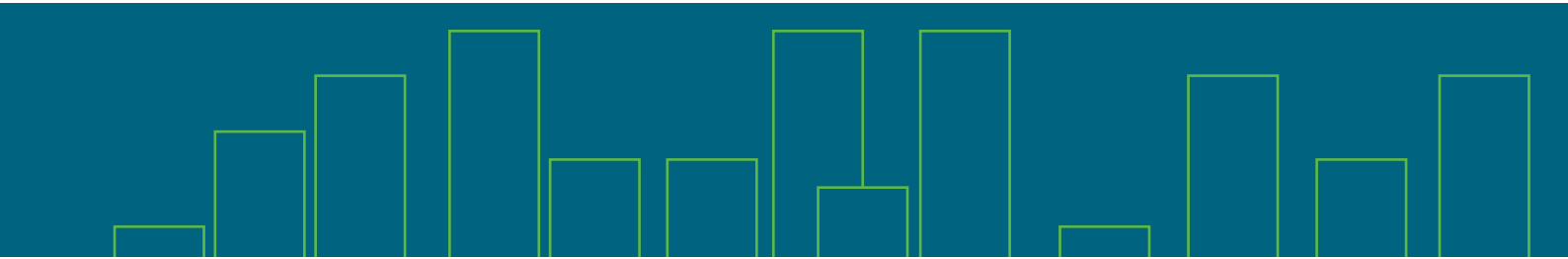
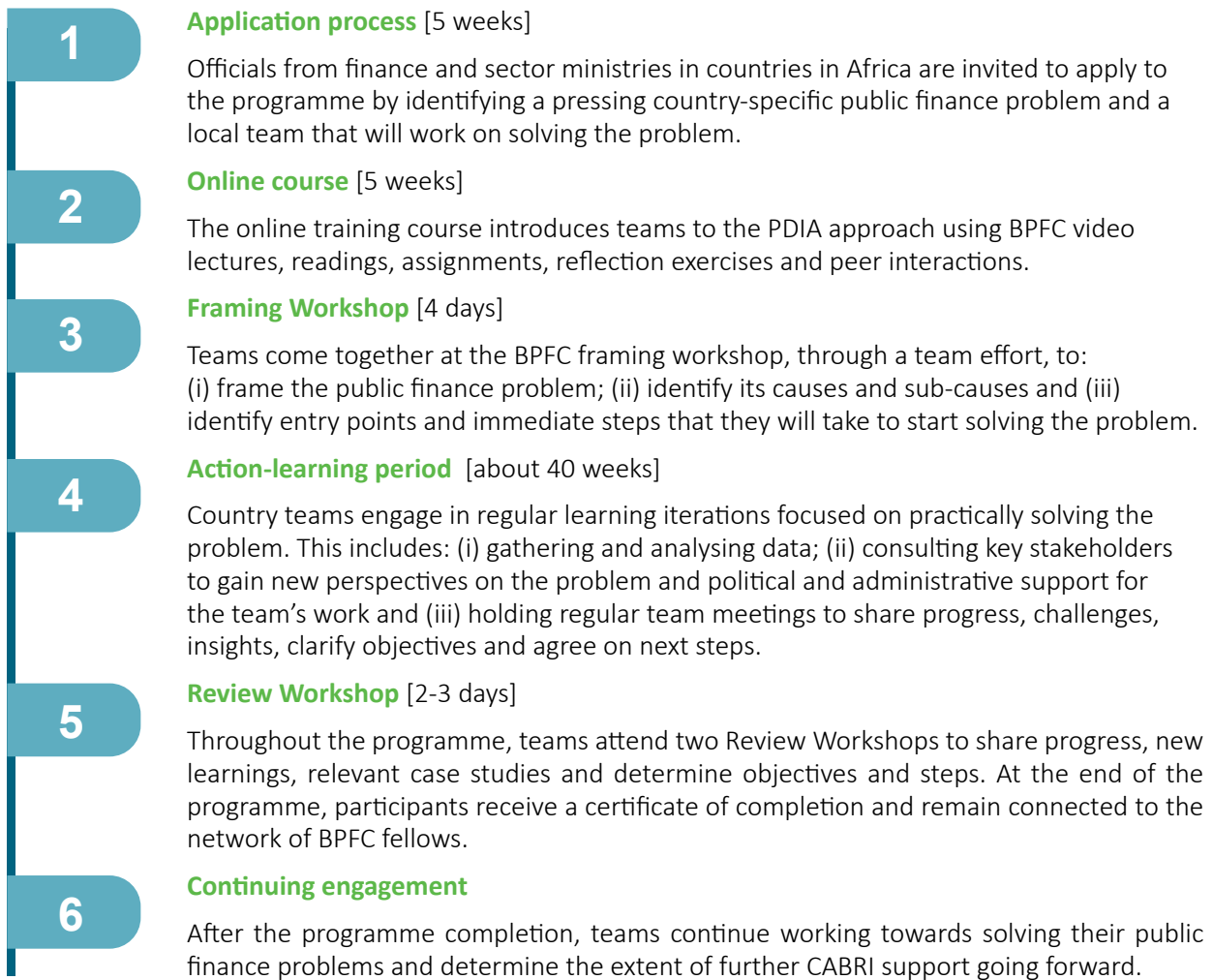


Figure 2: Structure of the BPFC programme



Keeping in mind the importance of identifying a significant and substantial problem that would attract the attention of stakeholders and allow for the identification of underlying causes to propose the most appropriate local solutions, the Sily team has formulated the following problem:



A significant accumulation of internal arrears impacts the implementation of public policies, penalises service providers and taints the credibility of the state.

2. The problem of accumulation of arrears in Guinea

The Syli team made five assumptions to explain the situation regarding the accumulation of arrears. The assumptions are outlined in Figure 3.

The causes and sub-causes initially identified were supported by data obtained from the General Directorate of Budget as well as the experiences of team members in drawing up macroeconomic guidelines, followed by budget guidelines and the steps involved in formulating and executing the general state budget.

The Syli team identified two entry points in which they would focus their investigation, based on an assessment of a more favorable space and ability to effect change.

This assessment was based on whether there was a favourable accepting environment by stakeholders affected (the degree to which stakeholders accept the need for change), authority (high-level support required to carry out the reform) and ability (the available resources in terms of time, skills, funding, etc). These entry points are:

1. Unrealistic budgeting, with an analysis of all the sub-causes related to macroeconomic and budget guidelines.
2. Inefficiency of the cash management system, in particular with the Single Treasury Account (STA) becoming operational.



Figure 3: Causes for the accumulation of arrears in Guinea

Unrealistic budgeting, typified by poor execution rates	Weaknesses in the tools used for macroeconomic guidelines	Macroeconomic data is not updated	Budget forecasts are not reliable
Low level of domestic resources	Disfunctional collection chain	Tax administration revenues are not secured	Narrow tax base
Priorisation of some MDAs at the expense of regular forecasted expenditures for other MDAs	There is an execution rate of over 100% for the Presidency, Defence and Security appropriations	Extra-budgetary expenses are the norm	Limited accountability on the use of public money
Inefficiency of the cash management system, illustrated by the multiplicity of state bank accounts, to manage public finances	Non-compliance with the Single Treasury Account (STA) agreement	Poor supervision of resources to cope with expenditure	Lack of coordination between commitment, procurement and cash flow plans
Non-compliance with processing deadlines in the expenditure circuit/channel	Non-compliance with monitoring time limits for expenditure	Administrative red tape for disbursement of payments	Lack of regulations penalizing failure to make expense payments timeously

3. The underlying causes of accumulation of arrears in Guinea: Findings from an action-learning approach

The Syli team's problem deconstruction process made it possible to collect the necessary data and information to explain institutional, technical and political reasons underlying these causes.

Firstly, it was important to determine the period after which an unpaid expense is considered to have fallen into arrears (90 days). Next, the stock and the evolution of internal arrears had to be evaluated. Such arrears cannot be definitively confirmed as unpaid services rendered, thus creating ambiguity concerning the nature of their clearance. Lastly, joint instructions on the write-off period should be reviewed. This led to the realisation that there have been arrears clearance strategy projects dating back to 2021, but these strategies have not been approved.

With regards to unrealistic budget forecasts, the starting point is the unreliability of the macroeconomic guidelines. Despite the availability of a procedures manual for the macroeconomic guidelines forecast tool (Simulation Model of the Guinean Economy – MSEGUI), a comparison between forecasts and actual results of aggregates reveals significant divergences. These divergences are due to volatile exchange rates, the absence of comprehensive and recent economic data for realistic forecasts, as well as a shortage of competent personnel for macroeconomic modelling and forecasting.

The tool is considered capable of improvement and could be certified by institutions with indisputable expertise in macroeconomics, such as the International Monetary Fund. Indeed, inaccurate forecasts not only impede the mobilisation of resources but also affect the size of the budget and the credibility of its contents.

With regards to the budget, the separation of institutions responsible for planning, programming and budgeting, as well as the failure to comply with budgeting procedures, undermines the alignment of public policies with budgets. This is particularly problematic in a volatile economic context that is vulnerable to various setbacks and highly dependent on natural resources. This misalignment is evident in the delay or indeed absence of decision-making due to the divergences or differences in prioritisation of issues between various institutions. As an example, the fact that no consensus on arrears clearance strategies has been signed jointly by the Minister responsible for the budget and the Minister in charge of the economy over the past two years reveals significant economic policy problems within the government.

Moreover, the lack of synchronisation between the commitment plan and the cash flow plan leads to delays in payments, which gradually turn into arrears. Even though the general state budget for year N includes a budget line item for 'Outstanding arrears' for year N-1, the various ways in which this line item was executed was not always in line with the budget approved by the National Assembly. Either the total arrears in each sectoral Ministry were debited from the overall budget of the Ministry in question, preventing its projects from being implemented as forecast, or an estimate of the total arrears was made and entered into the budget line item 'Outstanding payments' for the year N budget, with the obligation to clear these arrears by the end of the first quarter of year N. However, this does not always materialise due to fiscal constraints.



As a result, given limited revenue and competing priorities, this budget line item, even though it is increased every year, is still underbudgeted. It does not account for all arrears awaiting payment, and is far from being fully cleared by the end of the fiscal year. For example, a sum of 2 200 billion GNF was set aside from the 2024 treasury balance to reduce outstanding payments, even though outstanding payments amounted to 3 925 billion GNF.

Currently, the government is struggling to clear arrears. Without a unanimous political decision on concrete measures to clear them, arrears will continue to be settled in a haphazard manner, undermining budget credibility.

The situation with *Électricité de Guinée (EDG)*, which accounts for the greater share of unpaid arrears, highlights several issues: insufficient data on the volume and stock of arrears payments; a lack of understanding of the process of accumulating these arrears; and the absence of a clearing strategy. During discussions in a workshop that included senior officials from EDG management, it was revealed that this state enterprise was partially financed by the state, which directly settled specific supplier invoices up to a given ceiling specified in the budget.

However, since the EDG cannot mobilise sufficient resources from customer billing, it remains largely subsidised and has to pay for supplies in foreign currency, which leads to additional costs that the state will eventually be forced to cover. Despite a unilateral announcement in the 2024 guidelines that there would be a gradual reduction in state subsidies to EDG to encourage greater self-financing, the management of the enterprise and its perpetual need for state intervention – especially during demonstrations caused by electricity cuts – should be reorganised to achieve the intended results.

Lastly, in terms of cash flow management, a review of the agreement on the management and functioning of the Single Treasury Account (STA) highlights the state's non-compliance with the principle of a single bank account for all financial operations. This non-compliance may be explained by a poor understanding of the STA on one hand, and by the erosion of confidence of officials of various institutions regarding the management of public funds by their predecessors on the other. Consequently, these institutions operate with dedicated bank accounts.

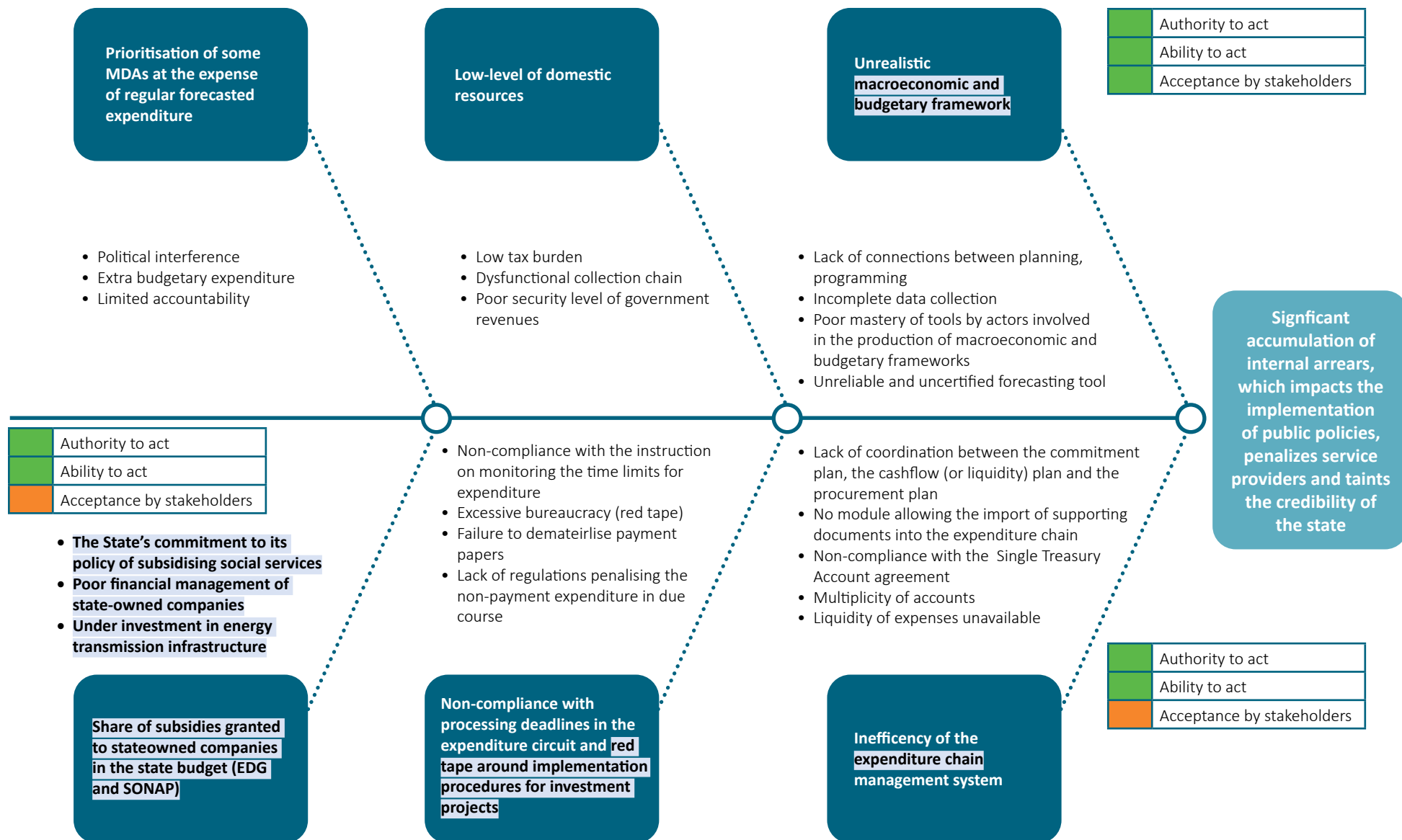
Thus, whether it is sub-accounts linked to the STA or other independent accounts, the Central Bank of the Republic of Guinea (BCRG) is not in a position to provide the government's net flow position in real time. This lack of information disrupts the public expenditure chain and also partially contributes to the accumulation of arrears.

Additionally, greater importance was given to the policy of subsidising state-owned enterprises, particularly the EDG, which is both costly and counterproductive.

These lessons, learnt over a period of ten months through the collection of conclusive evidence and various interactions with the relevant parties, enabled the team to gain a better understanding of the problem and context of the accumulation of domestic arrears in Guinea. This understanding is illustrated in the form of a fishbone diagram in Figure 4.

Figure 4: Fishbone diagram explaining the accumulation of domestic arrears in Guinea

LEGEND | Amended/additional information on the causes of arrears in Guinea after the action-learning phase



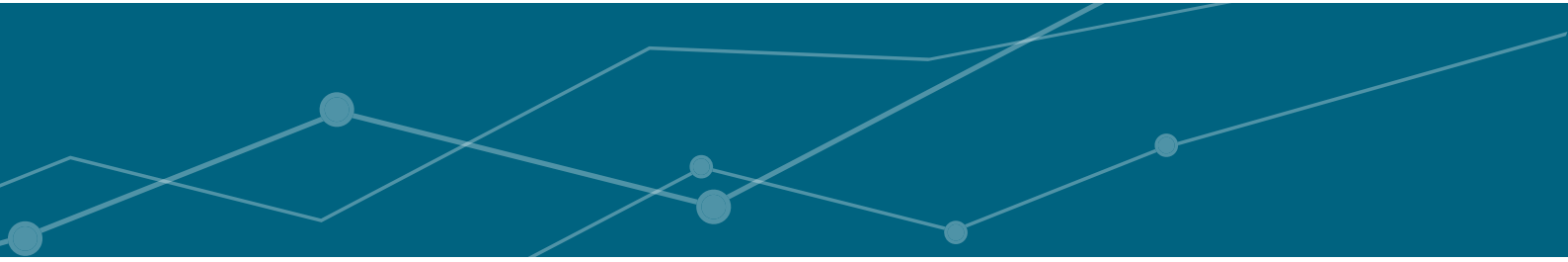
4. Identifying context-appropriate solutions to the accumulation of arrears in Guinea

While paying close attention to the broader political economy constraints and considering their space for change, two types of solutions were identified: (i) short-term solutions that do not require long approval processes and for which support is self-evident; and (ii) long-term solutions that involve several stages of the budgeting process and need to

be pursued continuously over an extended period. A key aspect of these solutions is rebuilding trust between institutions, based on a common vision and improved management focused on achieving results. These solutions are unpacked in more detail in Table 1.

Table 1: Short- and long-term solutions

	Entry point	Solution	Justification	Results to be achieved	Stakeholders involved
Long-term	Unrealistic budgeting with an analysis of all the sub-causes relating to macroeconomic and budget guidelines	Improve forecasting tools and build/strengthen technical and operational capabilities of supervisory staff to make a realistic and comprehensive evaluation of the state's revenues and expenses	<p>Because macroeconomic management tools have revealed certain inadequacies in generating forecasts that reflect the real state of the Guinean economy, it is important to ensure that the model is reliable, allows adjustments to underlying assumptions, processes up-to-date and reliable data and produces credible results.</p> <p>A peer review should be done on the reliability of the tool. Additionally, personnel should receive continuous specialised training to develop a good grasp of the tool and to make necessary adjustments in line with the evolving economy.</p>	<p>Improve the forecasting tools;</p> <p>Build capabilities of supervisory staff in charge of forecasting;</p> <p>Evaluate the state's revenues and expenses realistically.</p>	Directorate of Economic Forecasting and Economic Environment



	Entry point	Solution	Justification	Results to be achieved	Stakeholders involved
Short-term	Unrealistic budgeting with an analysis of all the sub-causes relating to macroeconomic and budget guidelines	Establish a platform for information exchanges between the stakeholders involved in the macro-economic and budgetary frameworks (guidelines) chain	<p>Data and information do not circulate adequately between the principal stakeholders involved in the macroeconomic and budget guidelines, from budget preparation to execution.</p> <p>Establishing a repository of data accessible to these stakeholders would improve the reliability of forecasts and estimates on both side sand would consolidate databases. While such tools have not yet been introduced, they would strengthen collaboration and promote transparency between stakeholders.</p>	Ensure that the platform for information exchanges between the stakeholders involved in the macro-economic and budgetary frameworks (guidelines) chain is operational and functioning effectively.	Directorate General of Planning, Directorate General of Budget and Directorate General of Treasury
	Inefficiency of the cash management system, particularly the Single Treasury Account (STA) becoming operational	Establish a committee responsible for monitoring arrears clearance strategies and limiting the accumulation of arrears	<p>In light of the failure to sign off on the arrears clearance strategies over the past two years, it is important to reprioritise the issue by formalising the existing Committee. This Committee should be responsible for drafting a clearance strategy to be approved for year N and for monitoring disbursements related to this clearance.</p> <p>It is proposed that the Secretaries General of the Ministries of Budget and of Finance be designated to approve this strategy and to see to its implementation. The reason for designating the Secretaries General is their stable positions and the leadership role of the Secretary General of Budget in the BPFC programme and the PDIA approach.</p>	<p>Approve and implement the strategy for clearing arrears;</p> <p>Reduce the level of domestic arrears;</p> <p>Reduce payment periods for built-up expenses and arrears.</p>	Directorate General of Treasury, the Central Bank of Guinea



	Entry point	Solution	Justification	Results to be achieved	Stakeholders involved
Short-term	Inefficiency of the cash management system, particularly the Single Treasury Account (STA) becoming operational	Introduce innovations to the financial information system, such as a tab for supporting documents and alerts for delays in the expenditure chain	<p>The execution of the various stages of the budget occurs through the public expenditure chain. However, from the initial phase of commitment by the MDAs, it is currently not possible to guarantee that the expense incurred constitutes a service duly rendered or being rendered at the time.</p> <p>To avoid excessive simultaneous demand for settling unverified expenses, it is suggested that a module can be programmed to make the digitalisation of supporting documentation (contracts, invoices, etc.) compulsory before the expense is approved by the financial auditors.</p> <p>At the payment stage by Treasury, implementing a warning system to highlight delays in payment would motivate the staff to speed up procedures and monitor the availability of domestic revenue during budget execution. Such innovations have not been tested in the past and would be particularly opportune in the digital era. Moreover, officials responsible for the expenditure chain have confirmed that such innovations could be introduced within a short period of time.</p>	<p>Expenses incurred should correspond to services rendered;</p> <p>Familiarisation with the stock of arrears, preventing auditing;</p> <p>Regulation of the budget should be easier.</p>	General Directorate for Budget and National Directorate for Information Technology Systems

5. Conclusions

Ultimately, the Syli team considers that they have experimented with an approach distinct from the usual type of technical assistance, enabling officials to implement PFM reforms focused on identifying appropriate solutions tailored to the specificities and context of the country. According to the team, the PDIA approach is based on addressing local problems, starting with actions within their capabilities and learning lessons from failures to understand how and why they occurred. Their participation in designing solutions enhances their capability to implement them.

One of the advantages the Syli team has is the familiarity among its members, who already work closely together during budget execution. Through numerous consultations with various institutions, the team has gained a better understanding of the processes and modus operandi of these institutions, including the different directorates within the team. Despite differences of opinion and tensions, the team members have managed to overcome them and have remained committed throughout the programme.

The Secretary General of the Ministry of Budget, in his role as authoriser, has been a determining factor in providing guidance, motivation and facilitating access to certain institutions. His understanding of the PDIA approach, along with his experience in putting it into practice in his current position, has made him a role model for the team, demonstrating the feasibility of the approach. The good performance of previous teams who participated in the programme for implementing the PDIA approach has inspired the Syli team, which aims to uphold Guinea's reputation.

Even though the accumulation of arrears hampers the budget process and diverts important resources that could contribute to financing key social sectors, it does not make an appearance in the government's list of priorities. In the absence of any progressive and effective strategy for clearing these arrears and the continued policy of heavily subsidising state-owned enterprises, the situation is unlikely to improve. Governance will be undermined, and the confidence of the private sector will be eroded. The solution proposed is a first step towards resolving this financial and governance problem.

In the coming months, the Syli team will take charge of implementing and monitoring the proposed solutions.¹ New cooperation programmes with technical and financial partners will provide additional means to exercise pressure, beyond the proposed solutions, to completely clear all arrears of the past three years.

¹ Furthermore, the government of Guinea, through the Ministry of Budget, has nominated another team that will be working on cash management frictions and control over cash balances in the BPFC programme 2024/2025.



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