

PARTNERING WITH THE NEW DEVELOPMENT BANK

WHAT IMPROVED SERVICES CAN IT OFFER
MIDDLE-INCOME COUNTRIES?

Cyril Prinsloo



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ABSTRACT

Multilateral development banks increasingly struggle to respond effectively to the needs of middle-income countries, influencing not only their potential development impact but also their own financial stability. This challenge has been driven by a changing external environment, including additional competition from other financiers, the changing needs of middle income countries and institutional constraints. Business processes that deter greater borrowing by countries, especially in the presence of other financiers with less strenuous requirements, also contribute to this situation. These include lengthy loan approval processes, limited use of in-country management systems and sensitivities around environmental and social safeguards. There is also a need for greater responsiveness and an emphasis on the importance of knowledge services. This paper highlights some of these challenges and offers some alternative solutions. The New Development Bank, as a new entrant to the development finance milieu, will do well to draw on the experiences of existing multilateral development banks to improve its offerings to countries.

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INTRODUCTION

Ever since the Second World War, multilateral development banks (MDBs) have performed an important role in infrastructure financing, investing in areas where other financiers were reluctant to go. Their interventions have been deemed mostly successful. This success has been attributed partly to the effectiveness of the model they employed: by leveraging paid-in capital from their members through international debt markets, MDBs have been able to secure additional capital relatively cost-effectively, to be extended to borrowers at low interest rates with long maturities. Those attractive borrowing options, combined with decades of development knowledge and understanding, have made MDBs a preferred infrastructure development partner for many countries. The model has changed little over the past six decades.

Instead of ramping up investments to keep pace with the growing need for infrastructure financing on the African continent, however, MDBs increasingly have experienced difficulty in finding an adequate response to the needs of middle-income countries (MICs), which nowadays exist in a global environment markedly different from conditions prevailing during the latter part of the last century. In their insistence on strict loan conditions, placing social and environmental concerns at the centre of those conditions and adding bureaucratic layer upon layer to their operation, traditional MDBs now find themselves with access to large amounts of funding but decreasing calls for borrowing.

The increasingly difficult circumstances in which MDBs are placed result from a changing operating environment in addition to their own institutional limitations. These limitations include such issues as capital restrictions or conservative financial policies, together with inefficient business practices such as excessive bureaucracy and conditionalities. In addition, global debate around climate change and the promotion of social safeguards has influenced the attitudes of MDBs, requiring them to be more responsive to changing world standards. Increased availability of alternative sources of finance such as the private sector or bilateral national donors has sharpened competition. Lastly, the evolving capacities and priorities of potential recipient countries have emboldened their search for more readily accessible financing. All this has happened at the same time as the effectiveness of MDBs has been hamstrung by their own institutional constraints.

This paper identifies five key business processes that hamper the operations of MDBs. Its approach is to present suggestions to new MDB entrants, specifically the New Development Bank (NDB), on how to optimise their operations while

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drawing on best practice examples globally, and on experience in Africa. Given that these challenges are inextricably linked to the changing environment in which MDBs find themselves, the paper first outlines the global parameters within which they operate before homing in on more specific organisational constraints. The African Development Bank (AfDB) has become one of the largest infrastructure financiers in Africa and for that reason is used as a case study. The experience of two MICs, Botswana and Nigeria, serves to illustrate constraints and challenges identified in the literature. The paper concludes by offering recommendations to the NDB on how to avoid some of the self-inflicted limitations faced by other MDBs, and on how to operate within the limits imposed by the present global operating environment.

METHODOLOGY

The authors used a mixed methodology combining desk research, individual interviews and the results of a study group held on 24 August 2016 in Johannesburg, as well as peer review on initial drafts of the paper. The choice of Nigeria and Botswana for the case studies was made on the basis of identifying strong research partners within the GEG Africa network from the first phase of the project; and drawing on the experience of MICs with a background in accessing

non-concessional loans for infrastructure development from the AfDB and other sources, including the private sector and new donors such as China. In addition, Nigeria is one of the largest economies on the continent and is seen as an important factor in West African integration efforts. For its part Botswana has one of the highest per capita incomes on the continent and boasts a long history of stable economic growth and governance.

BACKGROUND AND CONTEXT: CHANGING ENVIRONMENTS

To provide context and background to the ensuing discussion the following sections briefly outline the role of MDBs in infrastructure financing and also explore the importance of MICs to the operations and sustainability of MDBs. Finally, the section discusses the changing landscape within which these organisations must now operate.

THE DEVELOPMENTAL ROLE OF MDBs

MDBs have played a crucial role in economic development ever since the Second World War. The model they use has not changed radically since that time. MDBs leverage paid-in capital from their members to secure additional funding on global debt markets as a means of extending loans to member countries at preferential rates. These loans are used to fund projects geared towards development and poverty alleviation. The model has been successful in terms of leveraging

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shareholder capital to raise additional resources. The World Bank, for example, between 1945 and 2013 raised more than \$580 billion in additional capital from a mere \$13.4 billion of paid-in capital from its members.¹ While MDBs are underpinned by capital from member states, they also enjoy a unique feature in the form of ‘callable’ capital. Callable capital refers to additional guarantees provided

¹ Humphrey C, *Challenges and Opportunities for Multilateral Development Banks in 21st Century Infrastructure Finance*, GGGI (Global Green Growth Institute) & Intergovernmental Group of 24, Special Paper Series. Seoul: GGGI, 2015.

by member states² that allow MDBs to call on additional funds from their members to meet situations of financial distress. The success of this model, coupled with the development knowledge gained over decades of operation, accounts for its continued relevance and explains why new MDBs such as the NDB and the Asian Infrastructure Investment Bank (AIIB) have not discarded the model. Instead, they are learning from it and looking to improve upon it by correcting some of its deficiencies.

Investment in infrastructure carries inherent risks that many commercial financial organisations are unwilling to take. MDBs are better placed to assume these risks, enabling them to provide loans to countries at lower interest rates and with longer maturities and grace periods

MDBs encourage development by financing development projects and providing technical assistance to recipient countries. Judging by the high proportion of loans extended for infrastructure projects, financing infrastructure is a core feature. Infrastructure plays a central role as an enabler of economic growth and poverty reduction by promoting greater productivity, improving access to markets and increasing trade, reducing transaction costs and creating employment. In addition, governments opt for large-scale infrastructure projects because they are often seen as the most effective way to address broad-based development challenges such as poverty and unemployment, with the greatest impact on the largest number of people.³ Some have argued, however, that such projects are not the most efficient way of addressing development challenges as they are typically 'over budget, over time, over and over again'.⁴

Investment in infrastructure carries inherent risks that many commercial financial organisations are unwilling to take. MDBs are better placed to assume these risks, enabling them to provide loans to countries at lower interest rates and with longer maturities and grace periods. Given that MDBs are backed by governments, are not profit-driven and are respected asset managers with privileged information about their borrowers, they are highly rated by credit rating agencies, allowing them to

2 The ratio between paid-up and callable capital has differed in the past. For example, for the African Development Bank's (AfDB) General Capital Increase 5 and 6, paid-up capital represented only 6% (with the balance callable) while for GCI 4, 12.5% of capital was paid up.

3 Bradlow D, 'Southern African governments, multilateral development banks, non-state actors, and sustainable infrastructure: Managing changing relationships', *South African Journal of International Affairs*, 22, 3, 2015, pp. 289–302.

4 Flyvbjerg B, 'What you should know about megaprojects and why: An overview', *Project Management Journal*, 45, 2, 2014, pp. 6–19.

access money on capital markets relatively cheaply.⁵ MDBs extend such funds, raised through a non-concessional window, to MICs; however, they also typically have a ‘concessional window’ (which offers grants, and loans at zero or close to zero interest to low-income countries, or LICs). Concessional windows rely on periodic replenishments from contributions by richer countries.

MDBs can play an important role in increasing private investment in infrastructure by working with client countries to establish sound policy frameworks, leveraging their experience in the technical design and implementation of projects or simply by demonstrating the financial feasibility of a project, which in turn will boost the confidence of private investors.⁶ Equally, MDBs can spur additional participation from public or private sector investors by acting as a conduit between capital providers and development projects or by providing the security needed for these

The MDB model also relies on accumulated development knowledge tested over many years in a wide range of countries and projects, which constitutes a unique value proposition to borrowers that other sources of finance cannot necessarily provide

investors.⁷ For private investors unaccustomed to investing in infrastructure (eg, sovereign wealth or pension funds) the risks involved may be unclear, because the project would differ from other, more familiar classes of asset; or they might lack the in-house expertise required to invest in infrastructure projects, in which case MDBs could act as a bridge.⁸

The MDB model also relies on accumulated development knowledge tested over many years in a wide range of countries and projects, which constitutes a unique value proposition to borrowers that other sources of finance cannot necessarily provide. MDBs such as the World Bank are able to deploy the world’s leading experts in a large variety of sub-sectors that can be called on to structure loans, scope projects and assist governments in implementation. The experience gained from working in a variety of MICs and LICs gives MDBs such as the World Bank a comparative advantage when countries seek knowledge and expertise to implement technically complex projects.

5 Nelson R, ‘Multilateral Development Banks: Overview and Issues for Congress’. Washington DC: Congressional Research Service, 2 December 2015.

6 Humphrey C, 2015, *op. cit.*

7 Bradlow D, *op. cit.*, pp. 289–302.

8 Arezki R & A Sy, *Financing Africa’s Infrastructure Deficit: From Development Banking To Long-Term Investing*. Washington: Brookings Institution, August 2016.

THE IMPORTANCE TO MICs OF NON-CONCESSIONAL LENDING

MICs are of particular importance to MDBs for two reasons.⁹ First, those countries often make up the bulk of the MDB's income-generating business: in most cases they qualify to borrow from non-concessional windows only, unlike LICs, which predominantly rely on concessional loans and grants.¹⁰ In the particular case of the AfDB, a number of LICs are eligible for 'blended' finance, allowing borrowing from both non-concessional and concessional windows. Although MDBs offer better rates than elsewhere, there is a small interest payment in play, from which these institutions fund their own business operations such as staffing, research and data collection.

Second, MDBs do not generate profits for, or pay dividends to their shareholders (ie, the member states); hence income generated from non-concessional operations instead can be used to fund or supplement their concessional window. Concessional operations depend on funding from member countries, including donors and other MICs, to replenish the fund on a regular basis. In the case of the AfDB, any additional income is transferred every three years from the African Development Bank (ADB, concessional window) to the African Development Fund (ADF, non-concessional window), to supplement the assistance provided by contributing countries.

Given the considerable influence the non-concessional window has on funding the concessional window, it is important that the NDB ensures efficient and sustainable operations within its concessional window, should it choose to establish a non-concessional window at a later stage. Most African countries are LICs, hence a non-concessional window could have a notable impact on development in Africa.

A CHANGING GLOBAL ENVIRONMENT

The priority afforded to infrastructure financing by MDBs is shaped by international trends, which have determined the scale of financing available for infrastructure development. After the Second World War and into the 1960s, most international and regional development banks focused on financing the infrastructure needed to rebuild cities following the devastation caused by the war. Towards the 1980s funding increasingly was channelled to social development projects and policy operations (eg, sector transformation plans), driven by the belief that project lending alone would not bring about the requisite development benefits. Infrastructure spending in many MDB portfolios dropped from as high as 70% of total funding during the 1960s to as low as 20% in the 1990s. Through the 2000s,

9 Humphrey C, 'The African Development Bank: Ready to Face the Challenges of a Changing Africa?', E6 July 2016, <https://www.oecd.org/derec/sweden/The-African-Development-Bank.pdf>, accessed 28 October 2016.

10 Some LICs such as Zambia and Cameroon can access both concession and non-concessional loans through the ADF and ADB.

however, infrastructure disbursements increased again, with the infrastructure portfolios of most MDBs now ranging between 30% and 40% of overall lending.¹¹

A trend that exerts significant influence on the operations of MDBs is the present global stress on environmental and social protection. MDB operations have come under increasing pressure not only from governments that provide the paid-in capital (funded by taxpayers), but also from organised civil society. While in the past MDBs have been accountable to civil society indirectly through their governments' shareholding and participation, non-state actors increasingly encourage MDBs not merely to focus on the economic and technical viability of development projects but also to consider their wider implications, which include broader social, political, environmental and cultural dimensions.¹² Equally, growing cognisance of the significant risks posed by large-scale infrastructure projects, such as involuntary or coerced resettlement and environmental destruction, and the potential societal backlash thus caused, has contributed to a shift in the priority accorded to such issues, not only by public financial institutions but equally by sources of private finance. This has put many MDBs in a difficult position: responding to increased pressure from international civil society leads to a belief in some countries that MDBs undermine their sovereignty, while the evaluation criteria demanded by civil society and adopted by MDBs increase both the time and cost of implementing projects, thus reducing the attractiveness of MDB finance to recipient governments.¹³ Others, however, argue that precisely because extensive upfront environmental and social impact assessments will attenuate backlashes down the line, they can prove more cost effective in the long run.¹⁴

The global financial crisis (GFC) that began in 2008 has also influenced MDB operations. MDBs act as counter-cyclical funders, providing financing during difficult economic periods to overcome public sector financing constraints and help reinvigorate economies. Most MDBs experienced increased borrowing between 2007 and 2009. In the case of the AfDB, for example, disbursements rose from UA¹⁵ 884 million (\$1.36 billion) in 2007 to UA 2.35 billion (\$3.7 billion) in 2009 (albeit coinciding with a general capital increase for the bank).¹⁶ After the GFC restrictions were placed on public and private financial institutions: the aim was to improve

11 Humphrey C, 2015, *op. cit.*

12 Bradlow D, *op. cit.*

13 *Ibid.*

14 IISD (International Institute for Sustainable Development), *Value for Money in Infrastructure Procurement: The Costs and Benefits of Environmental and Social Safeguards in India*. Winnipeg: IISD, January 2014, https://www.iisd.org/sites/default/files/publications/value_for_money.pdf, accessed 13 October 2016.

15 The AfDB (African Development Bank) employs 'UA', or 'Unit of Account', as its reporting currency. Conversion rates into all other currencies of member states for each year can be found in AfDB, 'Compendium of Statistics on Bank Group Operations', 2016.

16 *Ibid.*

financial resilience but the measures had the effect of making the institutions more conservative and restricting their lending capacity.¹⁷

POLITICAL ECONOMY CONSTRAINTS

The effectiveness of MDBs is sometimes hamstrung by internal politics. In most traditional MDBs, developed countries have contributed the bulk of the capital hence enjoy the greater share of voting rights. Thus, although they are not borrowing from these organisations they hold significant sway in their decision-making and policy direction. Equally, MDBs are influenced by the very conservative management style of those funders, driven largely by non-borrowers' need to ensure the security of their capital. In order for MDBs to retain their high credit ratings, critical to their securing cheap capital on international markets, they have maintained equity–loan ratios significantly higher than those of private institutions (in some cases even doubling them). While so conservative an approach ensures

Sound macroeconomic principles, together with strengthened legal and institutional capacities, have made MIC economies more predictable and less risk-prone, attracting the attention of a wide range of financial services providers

higher credit ratings, it may be argued that many MDBs could comfortably relax their equity–loan ratios without fear of retribution from ratings agencies.¹⁸ For the AfDB in particular this conservative approach could be a hangover from the 1980s, when a string of bad loans led to the loss of the institution's credibility and, as a result, the loss of its AAA credit rating as well. Given that the organisation has since significantly improved its financial standing and regained a top credit rating, the argument against a conservative approach may have lost some force.

MICs: CHANGING NEEDS AND PRIORITIES

Sound macroeconomic principles, together with strengthened legal and institutional capacities, have made MIC economies more predictable and less risk-prone, attracting the attention of a wide range of financial services providers. Botswana, with its impressive economic growth, good governance record and prudent macroeconomic and fiscal management, has been a notable example of this trend. At the same time, MICs increasingly have developed sophisticated and 'deep' domestic financial markets on which to draw, making MDBs no longer the

17 Humphrey C, 2015, *op. cit.*

18 *Ibid.*

only viable option for MIC infrastructure financing. In Botswana, for example, government bond market capitalisation has grown rapidly over the past 10 years, with domestic market capitalisation increasing from BWP¹⁹ 0.4 billion (\$40 million) in 2005 to BWP 6.4 billion (\$600 million) in 2015.²⁰

Over time, private sector investment and participation in infrastructure development have grown, driven by the prolonged dismal performance of public enterprises in infrastructure financing and service delivery. Some of this success has been achieved as a result of the policies of various governments aimed at incentivising private investment in infrastructure development.

As many MICs move up the development curve, their development needs change. No longer are they challenged by extreme poverty; instead, inequality and unemployment become major concerns. Despite moderate gains in overall economic development, however, there has been a significant rise in inequality as development dividends fail to ‘trickle down’ sufficiently.²¹ Inequality in Botswana,²² measured by the Gini coefficient (where zero represents perfect equality and 100 implies perfect inequality), rose from 54.2 in 1982 to 64.7 in 2002 before dropping back to 60.9 in 2009. Similarly, Nigeria recorded 38.7 in 1985 rising to 51.9 at its peak in 1996, before dropping to 43 in 2009.²³ For these countries, priorities have shifted to a greater focus on ‘inclusive’ growth. MDBs can respond to these challenges by promoting policies aimed at reducing inequality (with a specific focus on marginalised groups such as children, women and the elderly), and putting stress on ‘pro-poor’ infrastructure such as that located in geographically poor areas; and targeting wealth creation, education and health (eg, rural roads, factories, and water and sanitation projects).

MICs also continue to struggle with significant structural challenges, allowing exogenous shocks to severely influence domestic economic positions. For example, the recent global downturn in demand for commodities has severely influenced single commodity-dependent economies such as Nigeria where, until recently, capital expenditure was primarily funded from revenue from crude oil exports, with debt and private sector financing playing a more limited role. This reliance

19 Currency code of the Botswana pula.

20 BSE (Botswana Stock Exchange), ‘Annual Report 2006’, http://www.bse.co.bw/docs/BSE_annual_report2006.pdf, accessed 28 October 2016; BSE, ‘Annual Report 2015’, http://www.bse.co.bw/docs/BSEAnnualReport_2015.pdf, accessed 28 October 2016.

21 Kapoor S, ‘How Can the Multilateral Development Banks Best Adapt to the Changing Development Landscape?’ Norway, Ministry of Foreign Affairs, 2007.

22 Botswana is currently ranked in the top five countries in Africa with the highest gross domestic product (GDP) per capita. In 2015, Botswana’s GDP per capita was \$6,360, compared with a sub-Saharan Africa average of \$1,571 and \$2,640 for Nigeria. Source: World Bank, ‘GDP per capita (current US\$)’, <http://data.worldbank.org/indicator/NY.GDP.PCAP.CD>, accessed 6 September 2016.

23 World Bank, ‘GINI index (World Bank estimate)’, <http://data.worldbank.org/indicator/SI.POV.GINI?locations=NG>, accessed 28 August 2016.

was largely the result of high crude oil prices. Although this boom period was clearly beneficial to Nigeria, price volatility in international crude markets meant that revenue flows were unpredictable and unstable. As a result of this, national and sub-national budgetary allocations to various critical infrastructural sectors such as energy and transportation have fluctuated considerably, indeed sometimes proving unsustainable. Similarly, as a consequence of declining diamond sales revenue arising from plummeting global commodity prices and a slowing global economy following the GFC, financing Botswana's pressing investment infrastructure

As a consequence of declining diamond sales revenue arising from plummeting global commodity prices and a slowing global economy following the GFC, financing Botswana's pressing investment infrastructure requirements through public finances has been a challenge

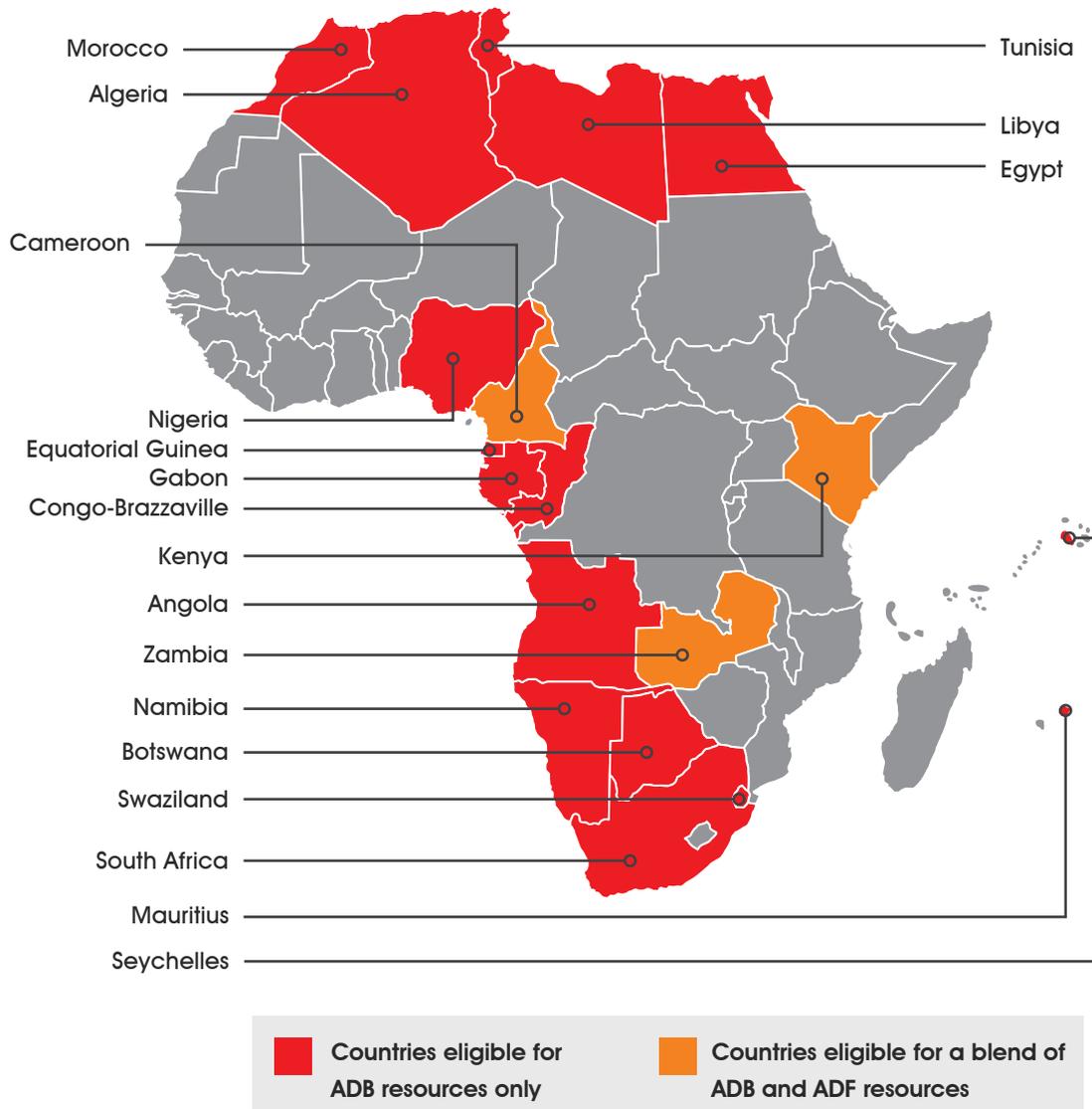
requirements through public finances has been a challenge. At the same time the downturn in commodity prices has exposed an additional struggle for MICs: the volatility of private capital flows. There is no question that Nigeria's and Botswana's ability to step up investment in vital infrastructure over the next few years will be critically dependent on their ability to borrow from MDBs and other sources of infrastructure financing.

Despite these problems MICs today have a wider range of financing options than previously, which in turn requires MDBs to adopt a lending approach more tailored to individual circumstances: fast, innovative and flexible.

THE AfDB AND ALTERNATIVE SOURCES OF FINANCING

Along with the global constraints that affect the lending capacity of MDBs and the changing needs and positioning of MICs there are a number of organisation-specific matters that influence the appetite of countries for borrowing from MDBs. These include factors such as unnecessarily bureaucratic business processes that result in unwarranted delays, and the entry of new sources of finance such as bilateral development partners and private finance providers. MDBs will have to ensure that they respond adequately to the needs of their putative borrowers. New entrants such as the NDB are potential catalysts for further renewal in the approach to infrastructure financing, but the NDB would do well to learn from the experience of other MDBs and financial institutions operating on the African continent. The following section highlights key lessons from the AfDB and other financiers.

FIGURE 1 CLASSIFICATION OF REGIONAL MEMBER COUNTRIES IN BANK GROUP OPERATIONS



Source: AfDB, 2016 Compendium of Statistics on Bank Group Operations

AfDB OPERATIONS

The AfDB was created in 1964 as an African-owned regional development institution. Since its inception the organisation's main lending has been through the ADB, which is its non-concessional lending window for MICs. The African Development Fund (ADF, concessional window) was created in 1973 to support countries ineligible for borrowing from the ADB. The Nigeria Trust Fund (NTF)

was set up in 1976. Like the ADF, the NTF is a concessional fund from which only LICs can draw support. However, unlike the ADF the NTF is allocated to projects rather than countries; and it can also co-finance ADB or ADF schemes as well as fund stand-alone projects.²⁴ While ADB membership remained confined to borrowing African countries for nearly two decades, non-borrowers were invited to contribute to the ADF from the outset.²⁵

The AfDB operated to good effect throughout the 1960s but oil price crises in the early 1970s severely affected member countries' economies, which eventually dented the financial credibility of the institution. In 1982 the ADB opened its membership to participation from non-borrowers (mainly developed countries), to increase the paid-up capital of the organisation and improve its financial stability.²⁶ Its reputation was somewhat tainted throughout the 1990s, mainly due to bad

Female representation at the executive directorate level in the Bank remains low, with only six women among the 27 nominated executive or alternative executive director positions (currently with two vacancies) among regional member states. There are no female representatives among the 13 non-regional members' representatives

lending practices and corruption. It managed to reverse this image, however, through structural reforms such as cost-cutting and refocusing its processes, and has since achieved high credit rating scores.²⁷ Today the AfDB has 54 African members and 27 non-regional members.²⁸ As of 31 March 2016 the three biggest regional members were Nigeria (8.87% of total votes), Egypt (5.43%) and South Africa (4.95%). The three biggest non-regional members were the US (6.54%), Japan (5.47%) and Germany (4.11%). Overall, regional members own 60% equity in the bank with non-member countries holding the balance. Female representation at the executive directorate level in the Bank remains low, with only six women among the 27 nominated executive or alternative executive director positions (currently with two vacancies) among regional member states. There are no female representatives among the 13 non-regional members' representatives (two

24 AfDB, 'Nigeria Trust Fund (NTF)', <http://www.afdb.org/en/about-us/corporate-information/nigeria-trust-fund-ntf/>, accessed 28 October 2016.

25 Nelson R, *op. cit.*

26 Kapoor S, *op. cit.*

27 Adams P, 'Bank to the Future: New Era at the AfDB', ARI (Africa Research Institute) Briefing Note, 1502. London: ARI, May 2015.

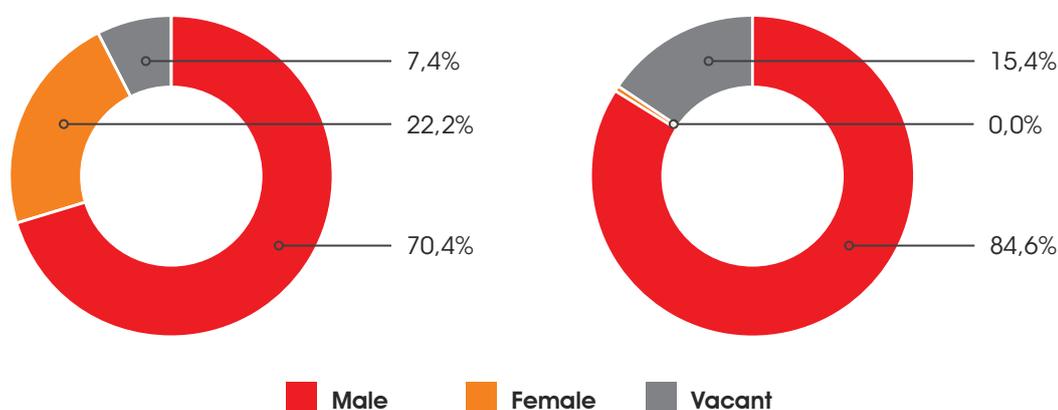
28 AfDB, 'Member countries', <http://www.afdb.org/en/about-us/corporate-information/members/>, accessed 28 October 2016.

positions are vacant).²⁹ Table 1 and Figure 2 illustrate the voting power and gender representation at the executive level within the ADB.

TABLE 1 DISTRIBUTION OF ADB VOTING POWER BETWEEN TOP REGIONAL AND NON-REGIONAL COUNTRIES					
REGIONAL MEMBERS	TOTAL VOTES	VOTING POWERS	NON-REGIONAL MEMBERS	TOTAL VOTES	VOTING POWERS
Nigeria	574 669	8.87%	US	423 487	6.54%
Egypt	351 035	5.42%	Japan	354 493	5.47%
South Africa	320 652	4.95%	Germany	266 265	4.11%
Algeria	273 071	4.22%	Canada	246 629	3.81%
Côte d'Ivoire	240 999	3.72%	France	242 606	3.75%
Other regional	2 089 671	32.26%	Other non-regional	1 095 407	16.91%

Source: AfDB, 'Statement of voting power as at 31 March 2016', <http://www.afdb.org/en/documents/document/afdb-statement-of-voting-power-as-at-31-march-2016-87909/>, accessed 28 October 2016

FIGURE 2 ADB, GENDER REPRESENTATION OF EXECUTIVE/ALTERNATIVE EXECUTIVE DIRECTOR REPRESENTATIVES



Source: AfDB, 'Statement of voting power as at 31 March 2016', <http://www.afdb.org/en/documents/document/afdb-statement-of-voting-power-as-at-31-march-2016-87909/>

²⁹ AfDB, 'Statement of voting power as at 31 March 2016', <http://www.afdb.org/en/documents/document/afdb-statement-of-voting-power-as-at-31-march-2016-87909/>, accessed 28 October 2016.

The NDB's equity structure differs radically from that of the AfDB in that, at present, only the five participating countries have voting rights, although it will look to increase its membership in the near future. Like the AfDB, however, the NDB lacks equitable representation of women within its key decision-making structures, with no female representation on its board of governors, board of directors or its top five senior management positions. A critical step for the NDB, not only in the institution itself but also in the projects it funds, would be to increase female representation. Evidence from the World Bank suggests that realising gender equality in the outcome of projects requires an explicit focus on gender considerations throughout the life cycle of a project and beyond: gender considerations need to be built into institutional policies, country strategy papers, loan approval processes, the design and implementation of projects, and monitoring mechanisms.³⁰ It is encouraging to note that the NDB has released a 'diversity policy', aimed at eliminating any form of discrimination with the organisation.³¹

The AfDB has progressively increased its authorised capital, with the latest general increase (in 2010) raising it to \$100 billion. This puts it on par with other regional development banks, such as the NDB and the AIIB, but short of the Asian Development Bank (\$164 billion) and the World Bank (\$280 billion).³²

TABLE 2 AfDB GENERAL CAPITAL INCREASE

YEAR	1964	1982	1983	1987	1998	2010
Authorised capital	\$250 million	\$2.9 billion	\$6.3 billion	\$22.3 billion	\$30.1 billion	\$100 billion

Source: AfDB, 'Corporate information: History', <http://www.afdb.org/en/about-us/corporate-information/history/>, accessed 28 October 2016

- **AfDB products and mandate**

To assist in development efforts the AfDB offers regional members a range of products that includes loans, guarantees, equity and quasi-equity and risk management products. During the GFC the bank also introduced shorter-term counter-cyclical products, including the Emergency Liquidity Facility

30 Fofack H, 'Overview of Gender Mainstreaming in the World Bank', AfDB, Evaluation Matters, March 2014, http://www.afdb.org/fileadmin/uploads/opev/Documents/Evaluation_Matters_March_2014_-_Gender_inequality_and_You_-_article__14_.pdf, accessed 19 October 2016.

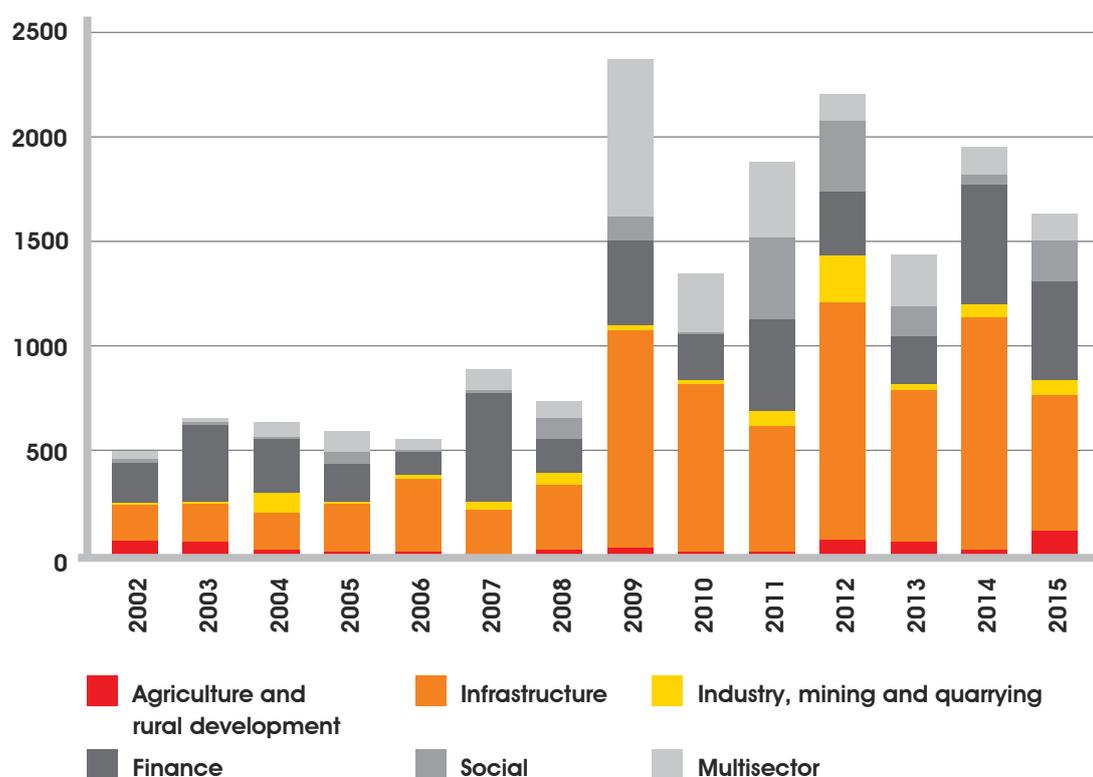
31 NDB (New Development Bank), 'Diversity policy', January 2016.

32 Bertelsmann-Scott T *et al.*, 'The New Development Bank: Moving the BRICS from an Acronym to an Institution', SAIIA (South African Institute of International Affairs) Occasional Paper, 233, June 2016, <http://www.saiia.org.za/occasional-papers/1074-the-new-development-bank-moving-the-brics-from-an-acronym-to-an-institution/file>, accessed 28 October 2016.

(discontinued in 2010) and the Trade Finance Initiative, which provides financing for trade-related activities.

Following the election of a new president in 2015 the AfDB has identified five priorities it considers critical to the development of the continent. These so-called 'high-fives' are respectively: to 'Light up and Power Africa', 'Feed Africa', 'Integrate Africa', 'Industrialise Africa' and 'Improve the quality of life for the people of Africa'.³³

FIGURE 3 ADB DISBURSEMENT BY SECTOR (UA^a MILLION)



a Unit of Account

Source: AfDB, 'Compendium of Statistics on Bank Group Operations', 2016

- **Borrowing trends and challenges**

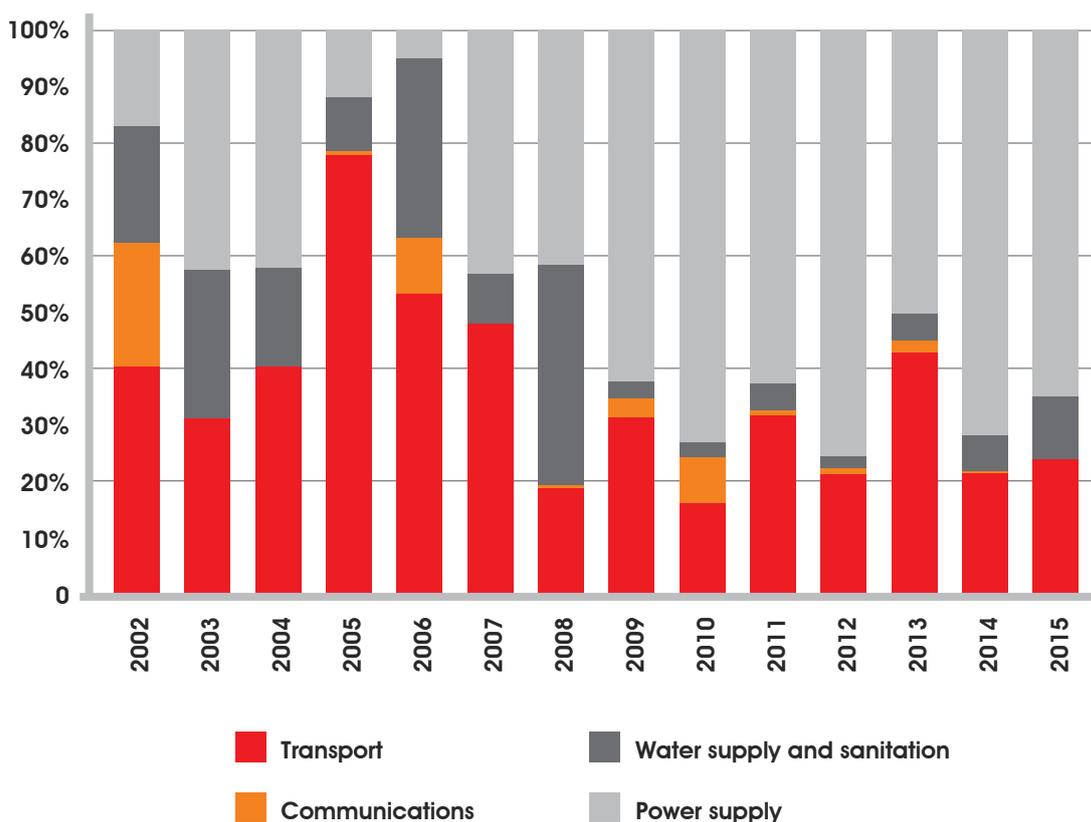
In 2015 the AfDB disbursed more than UA 1.6 billion (\$2.2 billion), down from UA 2.35 billion (\$3.7 billion) in 2009 at the height of the GFC, around the time of the bank's 2010 general capital increase. Infrastructure, finance and social sectors

33 AfDB, 'African Development Bank accelerates pace with "High 5" priorities', 27 June 2016, <http://www.afdb.org/en/news-and-events/article/african-development-bank-accelerates-pace-with-high-5-priorities-15879/>, accessed 27 August 2016.

received the biggest share of disbursements in 2015, representing 40%, 29% and 12% of disbursements respectively.

The bulk of infrastructure disbursements has been to the energy sector, with transport second. There appears to have been a marked shift from 2009 onwards, since when energy disbursements have consistently outranked transport-related payments. Prioritisation of energy projects has been a response to low energy generation capacity being regarded as a major brake on economic growth in Africa, costing the continent between 2% and 4% of GDP annually, according to the AfDB.³⁴ Investment in communications infrastructure has remained low throughout this period although the private sector is particularly active in this sector (see below for more detail).

FIGURE 4 ADB INFRASTRUCTURE DISBURSEMENTS (UA MILLION)

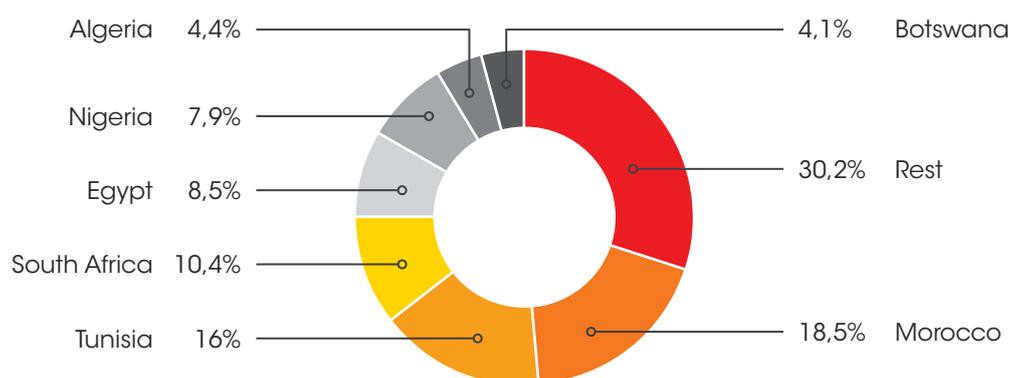


Source: AfDB, 'Compendium of Statistics on Bank Group Operations', 2016

34 AfDB, 'Annual Report 2015', <http://www.afdb.org/en/knowledge/publications/annual-report/annual-report-2015/>, accessed 28 October 2016.

One major challenge faced by the ADB is a high concentration of loans in a limited number of countries. Between 1967 and 2015 disbursements to its top five borrowers (Morocco, Tunisia, South Africa, Egypt and Nigeria) accounted for more than 60% of the total (see Figure 6). So highly concentrated a portfolio increases risk for the bank; serious economic difficulties experienced by only one or two borrowers would have a negative influence on the organisation³⁵ and in turn would have an impact on its credit rating. Standard & Poor's Rating Services, however, 'anticipate[s] that the bank will embark on some innovative portfolio management techniques over the next few years to reduce concentrations'.³⁶ Figure 5 shows how the ADB has already started to address this issue, notably through extending loans to the Southern African region (although this increase has also largely been concentrated in South Africa).

FIGURE 5 ADB LOAN DISBURSEMENTS 1967–2015 (% OF TOTAL)



Source: AfDB, 'Compendium of Statistics on Bank Group Operations', 2016

A critical trend related to its operational activities, however, is that total borrowing from the ADB has declined from its peak in 2009. This trend has been in evidence since 2003–2006, shortly before the GFC. The literature offers two explanations for this decline: first, the increased availability of alternative sources of finance for MICs, and second, procedural processes that have made borrowing less attractive – both issues to be explored further in subsequent sections. Not only does this situation pose a challenge to the AfDB financial model (given the importance of

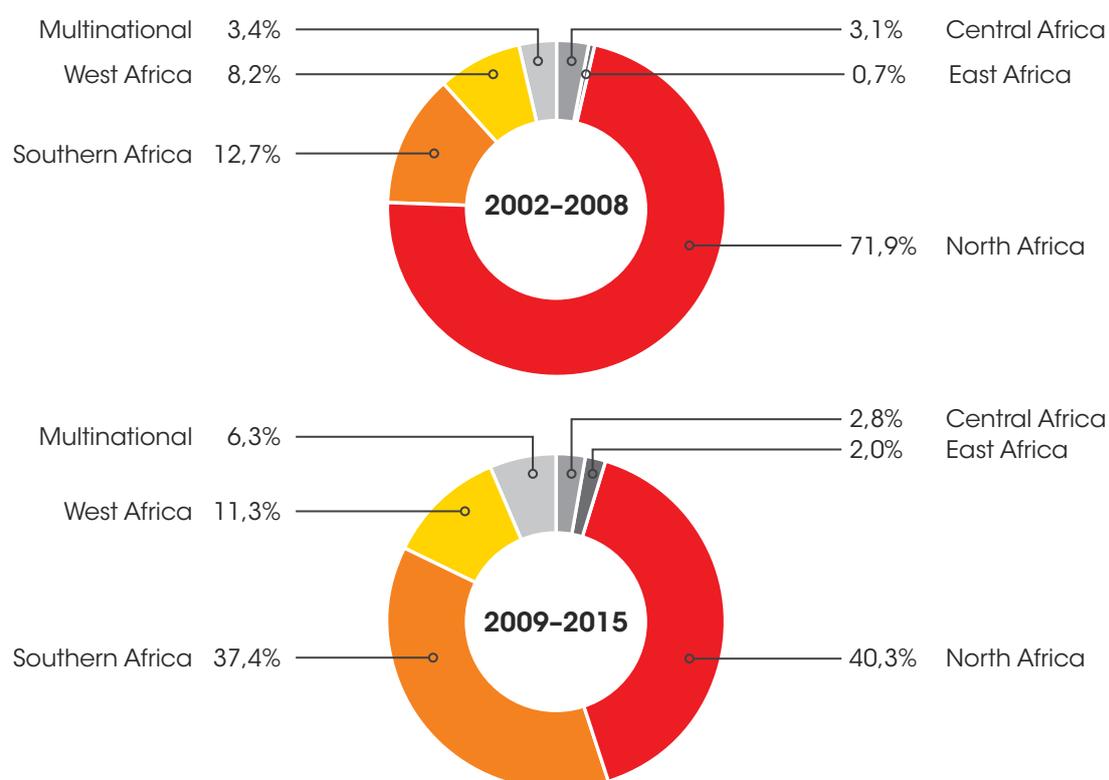
35 Humphrey C, 2016, *op. cit.*

36 Standard & Poor's Rating Services, 'Report on African Development Bank', 14 September 2015.

MICs to its operations); it also means that the bank is not adequately responding to the MICs' needs.³⁷

The case of Nigeria illustrates the trend. The AfDB's involvement with Nigeria remains limited vis-à-vis other MDBs; for them, facilities from the World Bank's concessionary window (the International Development Association, or IDA), significantly eclipse ADB and ADF lending. The IDA alone accounted for 58.69% (\$6.29 billion) of Nigeria's external debt (comprising all financing sources) with borrowing from the AfDB group at about 10% (\$1.07 billion).³⁸ While not necessarily indicative of the AfDB's inability to respond to Nigeria's needs, this does signify significant scope for the bank to increase its engagement with that country. Nigeria is currently graduating from the ADF and by 2018 will be eligible only for ADB resources, so the ADB's share has the potential to increase; but with no sign that Nigeria is likely to graduate from the IDA in the near future, the comparatively cheap loans provided under the World Bank's concessionary arm might remain the more attractive option and hamper such efforts.

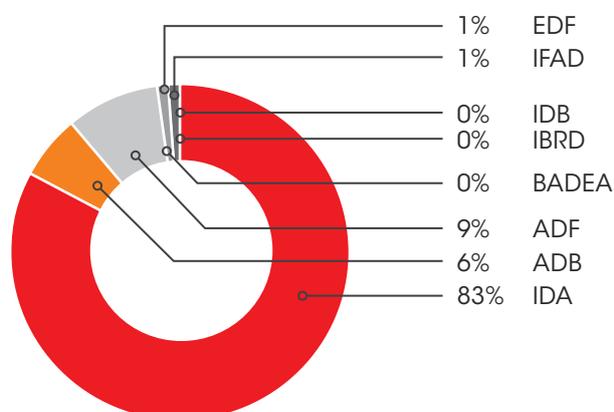
FIGURE 6 ADB DISBURSEMENT BY REGION 2002–2015



Source: AfDB, 'Compendium of Statistics on Bank Group Operations', 2016

37 Humphrey C, 2016, *op. cit.*

38 IDA (International Development Association), 'Financing', <http://ida.worldbank.org/financing/ida-financing>, accessed 28 October 2016.

FIGURE 7 MULTILATERAL SOURCES OF FINANCING FOR NIGERIA

Source: Centre for the Study of the Economies of Africa (CSEA) Analysis, using data from Debt Management Office, 2015, as at December 2015

A further challenge faced by MDBs – which the NDB also would like to address – is the way in which banks could structure loans to MICs in their domestic currencies. For the recipient country the benefits of such a process are high, insofar as the risk of currency fluctuations is eliminated, providing a real buffer against a potential increase in debt without incurring further borrowings or having spent an extra dollar. It is true that borrowing in foreign currency allows recipients to procure goods and services abroad, again limiting currency exchange risks; however, the essential challenge lies in ameliorating the risk of currency fluctuations for MDBs. No MBD can borrow money more cheaply than can governments in their own economies, which in turn tends to negate the participation of a MDB in the first place. Perhaps one option to consider is ‘blended’ loans structured in both domestic and foreign currencies. This method would offer a dual benefit: it would promote efficiency in allocating currencies where they will be most effective while mitigating some of the risks of borrowing solely in one currency.

ALTERNATIVE INFRASTRUCTURE FINANCING SOURCES

There are several reasons why developing countries, especially MICs, increasingly have been able to draw finance from sources other than MDBs. Combinations of strong growth and sound macro-economic policies have made those countries attractive for foreign investors or commercial lenders. Improvements in economic and political management are also occurring at a time where low interest rates are on offer in developed economies and countries and businesses with an excess of savings

seeking higher yields are turning their attention to the African continent.³⁹ Some African MICs have been able to tap into global debt capital markets. The following sections highlight a number of key alternative financing sources in Africa, including private sector financing, official development aid (ODA) and local development finance institutions, and direct engagement from countries such as China.

Private funding

The private sector has become critical to infrastructure financing on the continent, accounting for more than half of total external financing.⁴⁰ Over the past decade or so private investment in infrastructure in sub-Saharan Africa grew by 9.5% annually, whereas during the same period it declined significantly in countries such as Brazil and India (although India has seen a significant renewal of FDI in 2016, with reports of a year-on-year increase of 26%).⁴¹ Sub-Saharan Africa is the fourth largest recipient of private sector funding, with the top 10 recipients being South Africa, Nigeria, Kenya, Tanzania, Ghana, Sudan, Côte d'Ivoire, the Democratic

One option to consider is 'blended' loans structured in both domestic and foreign currencies. This method would offer a dual benefit: it would promote efficiency in allocating currencies where they will be most effective while mitigating some of the risks of borrowing solely in one currency

Republic of the Congo, Benin and Uganda.⁴² In 2013, however, of the \$17 billion in private sector investment in sub-Saharan Africa less than 2% went to countries other than South Africa and Nigeria and to sectors other than telecommunications. The preference of private sector investors for the information and communications technology (ICT) sector has been well observed in Nigeria which, according to the World Bank PPI database, over the past 15 years has attracted \$39.36 billion in private investment in infrastructure for 51 projects across seven economic infrastructure sectors (airports 0.51%, electricity 6.37%, natural gas 1.72%, ports

39 This situation could change when interest rates rise in the developed world or when new national leaders focus attention on infrastructure investment and renewal. Investment in long-term projects in OECD countries will always be seen as less risky than that in the developing world.

40 Gutman J *et al.*, *Financing African Infrastructure: Can the World Deliver?*. Washington DC: Brookings Institution, Global Economy and Development Program, March 2015.

41 *The Hindu*, 'FDI inflows rise 29%', 28 May 2016, <http://www.thehindu.com/business/Economy/fdi-inflows-rise-29/article8656537.ece>, accessed 28 October 2016.

42 Gutman J *et al.*, *op. cit.*

18.22%, railways 0.015% and roads 9.71%); but by far the highest investment has been in ICT infrastructure at 72.2%.⁴³

Whereas the telecoms sector has received the overwhelming portion of private sector investment in sub-Saharan Africa in recent years there seems to have been a definite levelling-off since 2012, with growing interest turning to the energy sector. The government of South Africa, for example, has initiated its highly successful Renewable Energy Independent Power Producers Programme, which has resulted in sharp increases in renewable energy investment. Within the energy sector generally, private sector interest lies almost exclusively in generation capacity with distribution and transmission functions left almost entirely to national governments.

The reasons for the earlier private sector interest in ICT are fourfold: firstly, the clear costs associated with such projects, secondly, the low risk exposure during development and construction, thirdly the easy securitisation of revenue streams and finally the private sector's control over the management of the investment. Given the growing saturation levels in the telecoms sector, investors are now exploring opportunities in land fibre optic technologies, establishing Internet exchange points and connecting sub-Saharan African states to submarine cables.⁴⁴

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According to the Infrastructure Consortium for Africa (ICA) 2014 survey of private sector investors, more than 50% of respondents said that they would continue to invest in those sectors in which they are already active. This implies low prospects for attracting private sector investment into areas outside telecoms and energy. Within the energy sector, 88% of investors indicated that they would be increasing their investments. The most attractive countries were identified as South Africa,⁴⁵

43 World Bank, Private Participation in Infrastructure Database, 'Country snapshots: Nigeria', <http://ppi.worldbank.org/snapshots/country/nigeria>, accessed 28 October 2016.

44 Submarine fibre optic cables already run along Africa's east and west coasts with links planned and in construction to connect South Africa to the Middle East. Linking landlocked countries through terrestrial networks to submarine cables will ensure faster and cheaper Internet connections throughout sub-Saharan Africa.

45 Eskom, South Africa's state-owned energy provider, has indicated that it would no longer off-take independent power producers' contributions to the national grid at a fixed price, a decision that will affect future investment into the South African energy sector. See Dodds C, 'Dismay as Eskom pulls plug on power purchases', *iol*, 5 October 2016, <http://www.iol.co.za/business/news/dismay-as-eskom-pulls-plug-on-power-purchases-2076253>, accessed 28 October 2016.

Kenya and Nigeria, the larger African MICs.⁴⁶ The World Bank reports, however, that investors are increasingly looking beyond traditional recipients because investment opportunities abound in sub-Saharan African countries that have sound macro-economic policies and have remained stable in the face of the commodity price slump.⁴⁷

Investors are increasingly looking beyond traditional recipients because investment opportunities abound in sub-Saharan African countries that have sound macro-economic policies and have remained stable in the face of the commodity price slump

From the ICA and other surveys of the private sector in its choice of investment destination in infrastructure projects, four key elements emerge as critical to the investment commitment: project feasibility, country political risk, profitability and the operative legal and regulatory framework. 'Constraints such as bureaucratic delays, policy uncertainty, lack of transparency and insufficient institutional capacity remain a challenge.'⁴⁸ The problem is compounded in that according to a report by the consultants McKinsey & Co,⁴⁹ three-quarters of sub-Saharan African countries lack the GDP sufficient to support projects larger than \$100 million.

Project feasibility and the project preparation phase repeatedly arise as key factors inhibiting investment, because their associated costs are high but there is no guarantee of eventual profit. 'The shortage of adequately prepared or bankable projects was a much bigger challenge than finding project finance.'⁵⁰ If national governments or MDBs do not facilitate investment by completing the project preparation phase, it is very rare for a private sector investor to take on this responsibility.

In the case of Botswana, the government formulated the Public Private Partnership (PPP) Policy and Framework in 2009 to create a solid environment aimed at encouraging and attracting private sector finance for infrastructure and service

46 ICA (Infrastructure Consortium Africa), *Infrastructure Financing Trends in Africa 2014*, ICA Report, 2014.

47 Diop M *et al.*, 'Africa still poised to become the next great investment destination,' *China Daily*, 30 June 2015, <http://www.worldbank.org/en/news/opinion/2015/06/30/africa-still-poised-to-become-the-next-great-investment-destination>, accessed 28 October 2016.

48 ICA, *op. cit.*

49 Cloete R *et al.*, 'Infrastructure: A long road ahead', in McKinsey & Co., *Africa's Path to Growth: Sector by Sector*, Report, June 2010, <http://www.mckinsey.com/global-themes/middle-east-and-africa/africas-path-to-growth-sector-by-sector>, accessed 28 October 2016.

50 ICA, *op. cit.*

delivery. The government anticipated that PPPs would be used extensively as a form of procuring and financing infrastructure projects in the public sector with the goal of ensuring sustainable investment in infrastructure and restoring sound public finances.⁵¹ Expected benefits from a solid PPP policy included the acceleration of infrastructure provision and access to private sector financial resources as well as expertise, while the government would focus on providing the required regulatory oversight.⁵² The intention was to ease implementation constraints on the government and yield sustained efficiency benefits in infrastructure service delivery.⁵³ As of 2015, however, PPP activity in Botswana has been rather limited: since the adoption of the PPP policy only two minor undertakings have been carried out under its framework. The country has signed one PPP (with the independent power producer Karoo Sustainable Energy) for a 90 MWe emergency power plant at Orapa, and initiated plans to build a new science and technology university through a PPP.

Reasons suggested for low PPP activity in Botswana include weak institutions (ie, the PPP unit is short-staffed), limited capacity for PPPs in the public and private sector and weak delivery processes within the PPP framework.⁵⁴ Continued government efforts to increase PPP activity include a review of draft legislation and the establishment of a committee to complete the implementation of an enabling environment for the PPP framework. The main lesson to be drawn from Botswana's experience with the implementation of PPPs is that traditional forms of financing infrastructure and development⁵⁵ cannot be replaced by PPP activities in the near term, given the amount of preparatory work still to be done for creating an enabling environment for PPP activities. For this reason Botswana's interactions with MDBs remain relevant.

Under the AU's New Partnership for Africa's Development (NEPAD), the NEPAD Business Foundation (NBF) operates actively to attract private sector investment in infrastructure projects. Basing its work on the 2012 Programme for Infrastructure Development in Africa (PIDA) that identified gaps in infrastructure financing on the continent, the NBF launched the Africa Infrastructure Desk (Afri-ID)⁵⁶

51 Republic of Botswana, 'Transforming Our Economy after the Crisis: 2010 and Beyond', Budget Speech, Minister of Finance and Development Planning OK Matambo, 2010, p. 12.

52 World Bank, PPP Knowledge Lab, 'Botswana', <https://pppknowledgelab.org/countries/botswana>, accessed 21 August 2016.

53 Kaboyakgosi G & K Marata, 'An analysis of Botswana's implementation challenges', PULA: *Botswana Journal of African Studies*, 27, 2, 2013.

54 PPP Country paper, Botswana, Submitted to SADC-DFRC 3P Network Public-Private-Partnership Working Group, 2015.

55 This excludes the use of public funds.

56 NBF (NEPAD Business Foundation), *NBF 2015 Integrated Report: Turning the Gears of Africa's Transformation*. Sandton: NBF, 2015.

to support the efforts of PIDA by coordinating the private sector and mobilising their resources to implement infrastructure projects that present commercial opportunities for members of the desk. The Afri-ID is therefore a multi-stakeholder platform bringing together the private and public sectors, multilateral finance/development agencies and other stakeholders with the common purpose of accelerating regional infrastructure development in Africa.

Afri-ID has managed to attract private sector investment to five port and rail projects on the continent – predominantly in Southern and Eastern Africa – but is actively seeking additional projects for PPPs. The real success factor lies in the fact that the private sector was attracted to projects outside of telecoms and energy, indicating that multi-stakeholder collaboration under a strong co-ordinating body can make almost any sector attractive to private investment. Regional projects, however, rarely involve private sector investors, which tend to find the process of working with a diverse range of governments and project directors too uncertain.

ODA

This section discusses the role played by ODA from the OECD countries in Africa's infrastructure development. For the most part OECD countries have given infrastructure investment assistance indirectly through their contributions either to the World Bank or the AfDB. Bilateral assistance on a country-by-country basis has continued but its focus has generally been away from the traditional

OECD countries have given infrastructure investment assistance indirectly through their contributions either to the World Bank or the AfDB. Bilateral assistance on a country-by-country basis has continued but its focus has generally been away from the traditional infrastructure sectors

infrastructure sectors of ICT, transport, energy, water and sanitation. A recent Overseas Development Institute (ODI) report found that ODA remains the largest single source of external development finance at country level and its flows are growing, even to MICs.⁵⁷ It is estimated that just under half of this funding goes to infrastructure spend.⁵⁸

Through the World Bank and the AfDB, support for large-scale infrastructure investment projects remains an important contribution from OECD countries.⁵⁹

57 Prizzon A *et al.*, *An Age of Choice for Development Finance: Evidence from Country Case Studies*. London: ODI (Overseas Development Institute), 2016.

58 Addison T & P Anand, *Aid and Infrastructure Financing – Emerging Challenges with a Focus on Africa*, Unu-Wider Working Paper 2012/56. Helsinki: UN University, 2012.

59 Gutman J *et al.*, *op. cit.*

At the World Bank, infrastructure lending represented 47% of all global lending in 1980. Over time, however, infrastructure as a target sector for such aid has varied. During the late 1990s and early 2000s, the Bank's emphasis on policy lending and human development funding left infrastructure to the regional banks and the private sector, which lowered infrastructure as a share of [total] lending to below 30%. That downward trend ended around 2005, as infrastructure's importance to growth and poverty alleviation received greater recognition, and the role of multilateral assistance, in particular, began to be considered essential.

Transport lending now accounts for 21% of the World Bank total active portfolio and three-quarters of the bank's projects include an ICT component.⁶⁰ In total, World Bank infrastructure spend currently hovers at the 40% mark, lower than the pre-1980 level but showing signs of increasing year-on-year.

The clear advantage of ODA, World Bank and AfDB funding is that the loans and grants go to areas where private sector interest is limited. Whereas the private sector tends to stick to countries where perceived risk is low, governance strong

Whereas the private sector tends to stick to countries where perceived risk is low, governance strong and ease of doing business high, ODA is spread more evenly among sub-Saharan African countries

and ease of doing business high, ODA is spread more evenly among sub-Saharan African countries. On the other hand, the ODA community can operate easier in fragile states. The preferred sectors for ODA are in transport, water and sanitation – again, areas within which private sector participation is low.

The Brookings Institution reports⁶¹ that the World Bank and AfDB models are not sufficiently adapted to sub-Saharan Africa's infrastructure needs. Questions raised include whether the classification of countries into concessional and non-concessional loan recipients is still valid, given new models introduced by China (see below). The report suggests that a mix of the two could be more effective depending on the sector and type of investment, and these issues should be discussed at upcoming replenishment meetings of the ADF.⁶²

Some ODA donors have seen the need to leverage private sector funds and a few initiatives along these lines have been developed (see Table 3). Schemes of this kind could provide pointers on the best way forward.

60 World Bank, 'Annual Report 2015', *op. cit.*

61 *Ibid.*

62 The fund's resources are replenished every three years by its donor countries. The next replenishment is due end-2016.

TABLE 3 ODA AND PRIVATE SECTOR COLLABORATION

PROJECT	DONORS INVOLVED	HOW IT WORKS
Private Infrastructure Development Group (PIDG)^a		
PIDG was established in 2002 as a donor-financed group to help overcome the obstacles to private sector involvement in infrastructure development in developing countries. It was founded on the belief that promoting growth and fighting poverty in developing countries demands serious investment in infrastructure and that the private sector has a crucial role to play in helping achieve the requisite level of funding in poorer developing countries. Attracting private sector investment in infrastructure projects in these countries will need expert and reliable encouragement and support	<ul style="list-style-type: none"> • AusAid • DfID • Swiss Federal Department of Economic Affairs • International Finance Corporation • KfW Entwicklungsbank (Germany) • Netherlands Ministry of Foreign Affairs • Norwegian Ministry of Foreign Affairs • SIDA (Sweden) 	PIDG is a PPP. PIDG members set the rules by which the companies operate. This aims to ensure that funding is channelled towards development priorities, and that every project is rigorously assessed against economic, social and environmental criteria. At the same time, companies harness their private sector expertise to take forward deals with private investors. PIDG is accountable to its members' governments, their taxpayers and the developing countries within which it works
Global Infrastructure Facility (GIF)^b		
The Global Infrastructure Facility is an open platform to help prepare and structure complex infrastructure PPPs, enabling mobilisation of the private sector and institutional investor capital	World Bank	The GIF co-ordinates and integrates the efforts of MDBs, the private sector and governments interested in infrastructure investment in emerging markets and developing economies. It fosters collaboration and collective action on complex projects that no single institution could achieve alone. GIF private sector partners alone represent about \$12 trillion in assets under management seeking productive investments with risk-reflective returns

a PIDG (Private Infrastructure Development Group), www.pidg.org, accessed 28 October 2016.

b World Bank, 'Global Infrastructure Facility', <http://www.worldbank.org/en/programs/global-infrastructure-facility>, accessed 28 October 2016.

Source: Compiled from Private Infrastructure Development Group and Global Infrastructure Facility websites⁶³

63 www.pidg.org and www.worldbank.org/en/programs/global-infrastructure-facility

Local development finance institutions

It is estimated that Africa contains more than 140 development finance institutions (DFIs), comprising national and multinational institutions as well as those with specific mandates (eg, universal, sectoral, import–export).⁶⁴ Almost two-thirds of the national development finance institutes (NDFIs) on the African continent, however, do not participate in infrastructure financing, instead concentrating on areas such as agriculture, housing, commerce and manufacturing.⁶⁵ Reasons for non-participation include capacity constraints during the project preparation phase, high risks associated with large infrastructure projects, the lack of upfront capital and the relative safety of investing in smaller projects spread across different sectors.⁶⁶

Nevertheless, a handful of NDFIs are active in Africa's infrastructure projects, most notably the Development Bank of Southern Africa (DBSA) and the Industrial Development Corporation (IDC) of South Africa. Algerian, Liberian, Namibian, Zimbabwean and Mozambique NDFIs are also active. NDFIs can play an important role not only in domestic resource mobilisation but also in building partnerships

NDFIs can play an important role not only in domestic resource mobilisation but also in building partnerships towards more effective onward lending from MDBs. They often have particular niches that MDBs can leverage

towards more effective onward lending from MDBs. They often have particular niches that MDBs can leverage; for example the DBSA has a special interest in the requisite technical skills, procedures and protocols for undertaking project preparation and has also established a niche in renewable energy. In early pronouncements from the NDB on areas where it sees the bank improving on existing services provided by MDBs, renewable energies and a more efficient project preparation phase were mentioned as targets. This approach clearly aligns neatly with the DBSA and although it might introduce an element of competition into the local financing landscape, there is ample potential for collaboration and for the DBSA to scale up with NDB support. The DBSA's total assets in 2014 were roughly \$2.7 billion for national projects and just under \$1.1 billion for international

64 Calice P, 'African Development Finance Institutions: Unlocking the Potential', AfDB Working Paper, 174. Abidjan: AfDB, May 2013.

65 Bradlow D & C Humphrey, *Sustainability and Infrastructure Investment: National Development Banks in Africa*, GEGI (Global Economic Governance Initiative) Working Paper, 4, July 2016, https://www.bu.edu/pardeeschool/files/2016/07/Bradlow.Final_.pdf, accessed 28 October 2016.

66 *Ibid.*

operations, bringing its total assets close to \$4 billion;⁶⁷ on this basis the DBSA stands as a minnow against the NDB, which is an estimated 60 times larger, and is significantly smaller than traditional MDBs. Hence the likelihood of head-to-head competition for funding similar projects is lower. Similarly, with regard to the IDC in South Africa there appears to be a divergence in the types of activities undertaken and projects likely to receive funding from the NDB. The IDC's particular area of expertise has been in financing manufacture. In 2015, 45% of funding approvals were to the manufacturing sector.⁶⁸

Generally speaking, given their home-base advantage NDFIs ought to understand the operating environment within which a project is planned better than outsiders, which should allow for improved risk assessment. When an NDFI is involved it can share the project oversight role with the MDB concerned, although this does not always seem to work well. In Botswana the AfDB has provided the national development finance banks with lines of credit (LOC) and technical assistance for capacity building for on-lending to the private sector. These national development finance institutions include the Botswana Development Corporation (BDC) and National Development Bank, which specialise in commercial and industrial development, among other activities. More recently, the AfDB has also extended LOC to the private sector through Bank ABC, a commercial bank operating in Botswana. One of the key products offered by Bank ABC is trade financing, especially to small, medium and micro enterprises.

One LOC from the AfDB includes a \$5 million loan to the National Development Bank for 365 sub-projects. An evaluation report, which assessed the AfDB–Botswana country strategy for 2004–2013, estimated that the LOC created 2 160 jobs, about 72% of the minimum target.⁶⁹ Support for the private sector was, however, characterised by considerable under-delivery and delays, and \$2.5 million of the LOC allocated for technical assistance was cancelled due to a lack of demand. About half of the grants were not disbursed, even after four time extensions. The evaluation team reviewed 41 projects under the LOC and found that about 67% of respondents were unhappy with the services under this arrangement, especially in terms of follow-up, monitoring and evaluation (M&E) and furnishing of appropriate lessons and experience. More than one-third of those interviewed for the report had repaid their LOCs in full, finding it easier to deal with other domestic banks, especially when requiring further financing.

67 Development Bank of Southern Africa, 'Integrated Annual Report 2014', <http://www.dbsa.org/EN/About-Us/Publications/Annual%20Reports/DBSA%20Integrated%20Annual%20Report%202013-14.pdf>, accessed 28 October 2016.

68 Industrial Development Corporation, South Africa, 'Annual Report 2015', http://www.idc.co.za/ir2015/images/pdfs/IDC_AR2015_Final.pdf, accessed 28 October 2016.

69 AfDB, 'Independent Development Evaluation: Botswana Country Assistance Evaluation 2004 – 2013', <http://www.idev.afdb.org/sites/default/files/documents/files/Botswana-%20Country%20Assesment%20Evaluation%20-%202004-2023.pdf>, accessed 1 November 2016.

Important lessons from the Botswana experience are that the LOC should make a significant contribution to private sector development and that there is a need for stronger oversight by the NDC and AfDB. It is clear from this experience that the NDB must caution against its becoming a mere conduit for funding from bank headquarters to NDFIs, and will have to be deeply involved in oversight of the project while further improving national capacities. If Botswana, a country with a democratic government and well-established processes, has experienced such difficulty in disbursing LOC, the challenges involved in doing so would be much higher in other, less well administered MICs or LICs. This might lead to the conclusion that access to finance is not the biggest challenge; it is rather the effective and efficient use of funds that presents the problem.

In March 2015 under President Goodluck Jonathan in Nigeria, the Development Bank of Nigeria was launched (the Nigerian Bank of Industry was already in place, with a sizeable portfolio of \$3.4 billion in 2014). This bank, as opposed to most other NDFIs, is a private sector-driven institution aimed at easing the financial constraints faced by small businesses. Unfortunately, not much has been done since the launch of the bank following a leadership change that took effect in November 2015, diverting attention to other concerns.

Nonetheless, there are significant precedents for MDBs to leverage NDFI expertise. For example, the AfDB over the years has extended numerous LOCs to the DBSA, which the latter in turn used to fund infrastructure projects.⁷⁰ Equally, one of the first loans extended by the NDB to Brazil was an LOC for its NDFI, the Brazilian Development Bank (BNDES), to fund renewable energy projects. It would seem therefore that involvement with local DFIs in future will require attention from traditional and new MDBs alike.

China as bilateral donor

China has a strong and visible presence in infrastructure financing on the African continent. Determining the precise scale of its commitment and projects in progress remains difficult, however, as unlike other OECD donors operating under development assistance criteria China does not participate in any formal data-recording processes. It is also clear that there has been a marked fall in Chinese investment in Africa, partly due to the slowdown of the Chinese economy, but the ICA in 2014 also reported a slowdown in financing for road and rail projects that previously would have attracted Chinese investment.⁷¹ In 2014 China invested \$3.9 billion, a substantial drop from an annual average of \$13 billion over the previous three years. Projects of choice remain road and rail, although the two largest investments in 2014 were port and airport developments, which could indicate

70 AfDB, 'AfDB approves 5th line of credit to DBSA', 8 February 2011, <http://www.afdb.org/en/news-and-events/article/afdb-approves-5th-line-of-credit-to-dbsa-7707/>, accessed 28 October 2016.

71 ICA, *op. cit.*

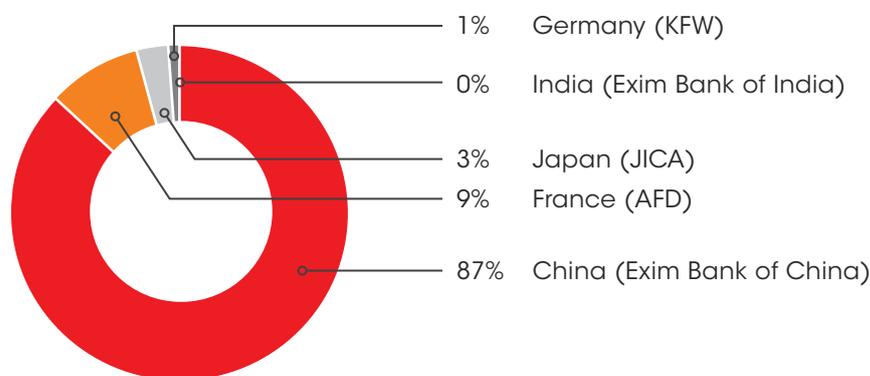
a change in China's sector choice. It is clear, however, that China is involved wherever investment serves its interest – and where the private sector fears to tread.

Ghana and Ethiopia have emerged as the biggest recipients of recent Chinese infrastructure finance, followed by Nigeria, Cameroon and Zambia. It has come to be generally understood that Chinese funding follows resource extraction, a view confirmed in reports by the ICA and the World Bank. The Brookings Institution, however, found that although⁷²

Chinese financing in resource-rich countries is still double the average volume of those flowing to non-resource-rich countries, this gap has sharply diminished over time. The cumulative average of Chinese financing to resource-rich countries doubled from \$300 million to over \$622 million between 2005-2008 and 2009–2012. But over the same period, Chinese commitments to the non-resource-rich countries leapt from \$43 million to \$285 million—a 550 percent increase!

Nigeria's borrowings through bilateral arrangements have increased as a proportion of total outstanding external debt from 8.01% in 2011 to 15.47% in 2015, with China accounting for 87.13% of all bilateral debt (which accounts for 13.48% of Nigeria's \$1.4 billion total external debt).⁷³

FIGURE 8 BILATERAL SOURCES OF FINANCING FOR NIGERIA



Source: CSEA analysis, using data from Debt Management Office, 2015

A trend that has emerged from Chinese lending to African countries is that it does not centre on financing alone but also includes technical assistance to go along with the funding, particularly for infrastructure loans. Understanding the nature,

72 Gutman, J.; Say, S. and Chattopadhyay, S. 2015. *Financing African Infrastructure: Can the world deliver?* Brookings. Global Economy and Development at Brookings.

73 CSEA analysis, using data from Debt Management Office, 2015

quality and depth of Chinese technical assistance, however, is difficult given that reporting remains weak. In planning documents such as the Chinese government's Aid Policy White Paper, technical assistance is not defined by content but simply refers to the time period over which Chinese aid could include technical assistance (up to two years).⁷⁴

Anecdotally it has been reported that Chinese technical assistance would entail training workers to use equipment for a specific task, rather than offering broader training to acquire the technical expertise required to master such projects or equipment as a whole. It therefore remains unclear whether the Chinese government constitutes a real competitor to traditional MDBs in knowledge transfer and technical assistance. Beijing is, however, beginning to engage more closely with the OECD and in 2015 announced a joint programme of work, along with membership of the OECD Development Centre.⁷⁵ China has been using the opportunity presented by its term as chair of the G20 to reach out to a variety of partners, including the OECD, to collaborate under the latter's theme, 'Innovative, Invigorated, Interconnected and Inclusive World Economy'. A special programme has been set up at the OECD specifically to draw views from China on possible revision of OECD instruments. Such closer collaboration will pave the way for better understanding Chinese aid and technical assistance in coming years. Thus while in part China's moves might indicate that the entry of new actors could be eroding one of the main competitive advantages of MDBs – providing technical knowledge to recipient countries – it may also indicate that in certain respects China's approach could be converging with that of OECD members.

One positive outcome has been a co-operation agreement between the AfDB and China to establish a 'Growing Africa Together Fund', which has resulted in a joint financing project for Tanzania's Bus Rapid Transport System. The direction and volume of Chinese investment will have to be followed with interest in coming months and years as the economic slow-down reveals Chinese priorities during times of limited resource availability.

CRITICAL CHALLENGES IN LENDING: BUSINESS PRACTICES

Although admittedly MDBs – and the AfDB in particular – face external and organisational issues that limit their lending, recipient countries have also been disinclined to deal with them on the grounds that their business processes slow down projects while adding additional cost. The processes at issue include unduly extended loan approval procedures; onerous procurement protocols; restrictive environmental and social safeguards and conditionalities tied to loans; and a lack of responsiveness to the needs of recipient countries.

74 Grimm S, *Transparency of Chinese Aid: An Analysis of the Published Information on Chinese External Financial Flows*. Stellenbosch: Centre for Chinese Studies, 2011.

75 OECD, *China and the OECD: A Mutually Beneficial Partnership*. Paris: OECD, 2016.

A concomitant problem is that MDBs employ uniform policies for differing countries without taking into account the latter's different and individual legal, development and institutional circumstances. In practice this means that MICs, which are typically more developed than LICs, must nevertheless comply with the same protocols.⁷⁶ That this is an issue is clearly evident from the two case studies: in Nigeria limited technical capacity exacerbated the challenges arising from difficult bank processes, but it appears to be less of a problem in Botswana.

LOAN APPROVAL PROCESS

One of the biggest complaints from MICs in their dealings with the AfDB is the onerous loan approval process. Considered both inflexible and overly bureaucratic, it results in lengthy and costly delays. The AfDB's loan approval process involves more than 20 formal review and approval steps that include 'an initial screening

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by the country economist; writing and approving the project brief; writing and approving the project identification report (two approvals); writing and approving the project preparation report; writing and approving the project concept note (seven approvals needed); and writing and approving the project appraisal report (nine approvals including board), requiring as many as four or five country visits for a single project.⁷⁷ As noted by Humphrey:⁷⁸

Over the decades, the AfDB has accumulated a bewildering array of policies, procedures and requirements that borrowers must grapple with to access bank services. Shareholders understandably wish to ensure project quality, but the levels of control and oversight have left staff risk-averse and process-obsessed. While each individual element may have been put in place for a valid reason, the cumulative effect has left the AfDB extremely slow.

Part of the problem is also the centralised structure of the bank itself, under which country or regional offices must refer decisions back to headquarters, which entails further delay. (In June 2016 the AfDB board approved a proposal towards greater

76 Humphrey C, 2015, *op. cit.*

77 *Ibid.*

78 Humphrey C, 2016, *op. cit.*

decentralisation of procedures to address exactly this constraint.)⁷⁹ In addition many MDBs, including the AfDB, are under-staffed, with individuals over-stretched over a number of projects; this also contributes to a slowdown in the approval process. Already the NDB, in its attempts to maintain a lean organisation, has faced similar capacity constraints.

Enquiries of key stakeholders in Nigeria, including the Debt Management Office, Federal Ministry of Finance and the Infrastructure Bank, revealed that the main challenges in infrastructure financing from MDBs in Nigeria are exacerbated by demand-side issues: the efficient processing of loans from MDBs for infrastructure financing is critically dependent on Nigeria's ability to follow required procedures diligently and quickly. MDBs have differing mandates and standard procedures that must be strictly followed. Consultations with stakeholders and experts in Nigeria reveal that the loan approval process for the AfDB takes on average six to 12 months and could extend to three years or more in some cases. For external borrowing at the sub-national (ie, state) level the Nigerian Fiscal Responsibility Act of 2007 requires that such loans must be secured and fully guaranteed by the federal government; this after sub-national level consultations, feasibility studies and legislative approvals, among other processes, have been completed. Hence the loan procurement process could be even more cumbersome for a borrowing country such as Nigeria in which the financial and human capacity required for adequate project preparation is generally low, even at the federal level. Clearly, business processes need to be better tailored to specific country capacity, and additional capacity building and assistance is needed for countries that experience difficulties in this respect.

For its part the Infrastructure Bank of Nigeria stresses demand-side constraints occasioned by the government's capacity shortage and low commitment to financing project feasibility studies, urging MDBs to be more accommodating in this regard and, where possible, to offer more help with project preparation. Government officials do not possess the skills adequate to deal with MDBs in the loan procurement process. To this extent the pace of loan procurement and disbursement depends upon and is limited by the level of responsiveness of beneficiary countries in meeting the lender's requirements at each stage of the process. Although the AfDB offers technical assistance to facilitate its dealings with borrowers there remains a knowledge gap on the part of borrowing countries (in this case Nigeria). Further complicating the loan process in Nigeria are instances of undue political interference with some of the more technical components of projects at both national and sub-national levels, which in turn causes disbursements to be put on hold.

Botswana's experience with the AfDB in this regard is similar to that of Nigeria. Loan preparation requires a considerable commitment by the national government

79 AfDB, 'AfDB to improve performance, development impact under new Development and Business Delivery Model', 27 June 2016, <http://www.afdb.org/en/news-and-events/article/afdb-to-improve-performance-development-impact-under-new-development-and-business-delivery-model-15888/>, accessed 13 October 2016.

to discussing project details with MDB staff. Procedures and times vary according to the type of loan, with those for long-term investments typically taking longer due to more stringent procurement procedures than apply to adjustment lending. The time lag between processing and disbursing an investment loan to Botswana by the AfDB is estimated at a maximum of five years, notwithstanding the economic and general development impacts of delay in such projects. In sharp contrast to the months or years that such a procedure might take, private financing is recognised for its speed in loan approval, reporting turnaround times of a few weeks or months.⁸⁰

Along with the time taken for loan approvals, the disbursement of funds from the AfDB is an equally lengthy process.⁸¹ Nevertheless, it is noteworthy that the time and care taken on ensuring positive development outcomes in the end contributes to development banks' competitive advantage over other sources of finance.⁸² Here the NDB would do well to draw on the experience of the Development Bank of Latin America (CAF), which typically takes only three months from loan application to approval, involving only two review levels. The CAF vice president can directly approve loans under \$20 million, while the president can approve loans under \$75 million, both without board approval; this can speed up the process considerably.⁸³ The shorter loan approval time and disbursement periods have not threatened the CAF's credit ratings and completed projects still report positive developmental outcomes.

PUBLIC FINANCIAL MANAGEMENT

MDBs, including the AfDB, have unique financial management and procurement requirements that often differ from each other and from applicants' domestic processes.⁸⁴ This could partly explain why there is such a high concentration of repeat borrowers in the AfDB's client profile: those who have become accustomed to the system tend to rely on it more. For new potential clients, barriers to entry are simply too high to scale in an environment where there are easier financial options. Borrowers such as Nigeria experience further delays because of the necessity of meeting the MDB's stringent procurement requirements. Introducing in this way another layer of control over and above existing national policies, guidelines and practices leads to further delay in implementation.⁸⁵ While such rigorous business practices are aimed at improving project quality, available evidence suggests that

80 Humphrey C, 2015, *op. cit.*

81 Woods N & M Martin, 'The preferred partner? A Client Assessment of the African Development Bank'. Abidjan: AfDB, 2012.

82 Humphrey C, 2015, *op. cit.*

83 Park A & J Strand (eds), *Global Economic Governance and the Development Practices of the Multilateral Development Banks*. London: Routledge, 2015.

84 Humphrey C, 2015, *op. cit.*

85 World Bank, 'World Bank Group/World Bank Corporate Scorecard', 2013.

they are a major deterrent to external financing for borrowing countries,⁸⁶ in sharp contrast to the use of domestic and private financing.

In an effort to overcome delays caused by MDB procurement practices there has been a concerted effort by the World Bank and the AfDB to adopt the ‘use of country systems’ (UCS) approach to facilitate development financing. The advantages of this approach could be threefold: first, its effect on speed of project implementation; second, the strengthening of country systems by MDB experts using and commenting on them; and third, reductions in transaction costs through employing human resources more efficiently between partners, ensuring greater buy-in from host countries and, ultimately, better project sustainability. Aligning lending procedures with country processes has the additional benefit of falling in with recipient governments’ respective financial cycles, which makes reporting (eg, the delivery of audited accounts) easier. At the same time, where counterpart funding is required, falling in line with government planning and budgeting processes will be made more efficient. Nevertheless, greater UCS also often faces a number of political and economic challenges – for example corruption or weak institutional capacity – and is not necessarily a panacea for all financial management ills.⁸⁷

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Institution-specific processes often require the establishment of project implementation units or recruitment of dedicated technical assistants. Typically these are drawn from experienced government officials (induced to move by the higher salaries paid by such institutions) and once projects are finished the technical expertise departs, having made little sustainable capacity-building impact. Critics also argue that using supranational domestic procurement processes puts domestic firms at a disadvantage compared with international companies that regularly work with these systems, effectively locking the former out of procurement processes. Despite various commitments made by development partners towards UCS (including global declarations on aid effectiveness since 2003 at OECD forums in Rome, Paris, Accra and Busan), uptake remains low. Although the AfDB has increased its adoption of country systems in its operations, a survey

86 Greenhill R *et al.*, *The Age of Choice for Development Finance: Evidence from Country Case Studies*. London: ODI, 2016.

87 Hart T *et al.*, ‘Use of Country Systems in Fragile States’, ODI, December 2015, <https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/10153.pdf>, accessed 13 October 2016.

of stakeholders involved with the bank ‘view progress as too slow, especially on procurement systems’.⁸⁸ In early pronouncements the NDB recognised the value of UCS and has undertaken an analysis of procurement processes in each of the BRIC countries. The NDB’s procurement policy notes that country procurement systems will be employed, but that⁸⁹

the type and size of project, the complexity of procurement, and the capabilities of the executing agency [will] determine the level of supervision. On a case-by-case basis, and as appropriate, [the] NDB may require clients to include specific provisions that may be at variance with the country procurement system in particular to ensure procurement meets the requirements of the Articles of Agreement.

Nigeria’s planning and financial management and procurement systems are not fully aligned with those stipulated by AfDB rules and procedures, which results in further delays in the engagement process. An assessment by the AfDB of Nigeria’s national procurement system for the use of national competitive bidding procedure (NFB) in routine procurement of works and goods under nationally financed projects, indicated that the system complies with basic principles of fairness, transparency, competitiveness and cost-effectiveness. The report also noted, however, that there were some areas of material deviation from acceptable practices: these included the absence of conditions to allow parastatals to bid for and receive contracts; the application of ‘margin of domestic preference’, that applies also to bank-financed projects; and the absence in the procurement process of an independent mechanism for complaints and appeals. To this extent UCS has not been fully implemented in Nigeria for AfDB-financed projects; a problem that needs to be addressed in order to bring national procurement protocols into line with AfDB rules and procedures.⁹⁰

In Botswana, even though the AfDB has made progress in adopting the national system for operations procurement, processes are still seen as out of full alignment with Botswana’s system and very slow. There should not be delays in reconciling the two systems, given that Botswana has sound auditing and procurement processes that conform to international standards. In 2007 the AfDB ascertained that Botswana’s Public Procurement Asset Disposal Board adheres to strict accounting, auditing and control systems, as well as a sound public procurement and asset disposal system; and the board has been found effective and accountable in the utilisation of public resources. The due diligence process for selecting contractors, coupled with the necessary paperwork is, however, considered cumbersome and the complexity of procurement systems has been associated with the lower responsiveness of the AfDB to the capacity available in Botswana.⁹¹

88 Woods N & M Martin, *op. cit.*

89 NDB, ‘Procurement Policy’, 30 March 2016.

90 AfDB, ‘Nigeria Country Strategy Paper 2012–2016’. Abidjan: AfDB, 2012.

91 AfDB, ‘Botswana: Country Assistance Evaluation 2004–2013 Summary Report’. Abidjan: AfDB, 2015.

ENVIRONMENTAL AND SOCIAL SAFEGUARDS

As noted earlier, MDBs have been influenced by the changing international dialogue around the protection of environmental and social rights. Discourse has been driven especially through international forums such as the UN Framework Convention on Climate Change, which came to its latest agreement (the so-called Paris Agreement) in 2015. This in turn has had a significant influence on the operations of MDBs, notably in financing energy generation projects. Major MDBs and DFIs such as the US Import-Export Bank, the World Bank and the European Investment Bank have already started cutting funding for coal-fired energy-generating projects (considered a significant contributor to global warming).⁹² Equally, social safeguards in relation to infrastructure development have gained increasing attention, not least because problems caused by the impact of new infrastructure on human relocation, or the destruction of cultural heritage sites, have drawn severe criticism.

Far from having been insulated from these international debates, African non-state actors (NSAs) in many cases have contributed to lobbying for greater environmental and social safeguards. A recent joint publication from the South African Institute of International Affairs and Oxfam South Africa⁹³ solicited views from a broad range of civil society organisations, think tanks, academia and policymakers on how the NDB should align itself with international best practice related to promoting environmental and social safeguards. Recommendations included giving priority to continued discussion with civil society on operations and observing the principle of ‘free, prior, informed consent’; and a move away from coal and extractive industries.

In response to current global discussions MDBs have developed safeguards aimed at protecting both the environment and communities affected by development projects. The need for such conditions and safeguards is gaining acceptance among stakeholders: for example, an environmental and social assessment by the AfDB of the proposed Lekki deep-sea port project in Lagos indicated that the anticipated impact on the physical and biological environment of the construction and operation of the port and its associated captive power plant would be adverse. The assessment proposed that this would be managed and mitigated through the implementation of a comprehensive environmental and social management plan

92 An earlier Oxfam report, however, noted that direct financing of such activities could be avoided by channelling funds to intermediaries, which in turn undertake such investments. For more information, see Oxfam, ‘Risky Business: Intermediary Lending and Development Finance’, 18 April 2012, <https://www.oxfam.org/sites/www.oxfam.org/files/ib-intermediary-lending-and-development-finance-180412-en.pdf>, accessed 13 October 2016.

93 Bertelsmann-Scott T, Friis C & C Prinsloo, ‘Making Sustainable Development the Key Focus of the BRICS New Development Bank’, SAIIA Occasional Paper, 230, May 2016, <http://www.saiia.org.za/occasional-papers/1033-making-sustainable-development-the-key-focus-of-the-brics-new-development-bank/file>, accessed 6 September 2016.

(ESMP) that would comply with the requirements of AfDB and other lenders.⁹⁴ Meanwhile the execution of the project, for which the AfDB is supposed to be a key lender, continues to stall. The real challenge in this area for several developing borrower countries, including Nigeria is the shortage of experts with the capacity to carry out extensive, timely and cost-effective environmental assessments of projects. This makes loan procurement from MDBs more cumbersome and prolonged.

The World Bank is often viewed as the global leader in the promotion of safeguards, employing the most progressive environmental and social framework (ESF); other MDBs follow its precedent. Even so, the World Bank undertook a review of its ESF over the past four years, adopting a new version in August 2016 aimed at relying more on the recipient country's own environmental regulatory safeguards. This approach has, however, attracted intense criticism from NSAs, which believe that it will weaken those safeguards in many countries.⁹⁵

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Such regulations apply to all development projects but are especially rigorous in infrastructure, energy and urban projects. When safeguards are found to be violated, the review process is usually extremely long and costly, requiring specialised studies and lengthy consultations with affected communities – usually at the expense of the borrowing government, which in consequence may discourage dealings with MDBs. As a result, some projects such as dams, power generation, slum upgrading and transportation may be specifically excluded from MDB funding. This could result in alternative lenders being used with a more cavalier approach to social and environmental concerns, potentially leading to more damage. An assessment of clients of the World Bank's non-concessional lending window (the International Bank for Reconstruction and Development) indicated that in order to avoid the costs and inconvenience that safeguarding processes place on lending, countries would rather opt for alternative sources of finance. Their order of preference for alternatives puts domestic sources first, followed by bilateral donors, regional banks

94 AfDB, 'Summary of the environmental and social assessment (ESIA). Project: Lekki Tolaram Port project. Country: Nigeria'. Abidjan: AfDB, 2014.

95 Bretton Woods Project, 'World Bank approves new "diluted" safeguards', 23 September 2016, <http://www.brettonwoodsproject.org/2016/09/world-bank-approves-new-diluted-safeguards/>, accessed 13 October 2016.

and lastly, MDBs.⁹⁶ In sum, although MDBs are more transparent and accountable than alternative financing sources, countries may reject MDBs because of additional delays or costs.⁹⁷

Botswana has partnered the AfDB in projects and communicated effectively with the bank on balancing the benefits of development with efforts to adhere to environmental safeguards. There are lessons to be drawn from that experience, including the need for clear communications and for training in the benefits of meeting best practice in environmental safeguards. MDBs are well equipped to facilitate capacity building in this area, given their technical expertise compared with that of most financiers.

The NDB has evaluated domestic ESF policies in all five of its members and will employ these as far as is feasible, providing assistance to countries where processes are deemed inadequate. This training imperative is captured in the NDB's ESF and highlighted as a primary principle for the organisation, along with the conservation of natural resources, promotion of gender equality and inclusive and sustainable development, among others. In respect of climate change the ESF notes that the 'NDB seeks to promote mitigation and adaptation measures to address climate change ... [the] NDB also encourages climate proofing of its infrastructure financing and investments to build resilience to climate change'.⁹⁸ Equally important to this discussion, however, is the recognition that it is not necessarily weak legislation that is of major concern – most countries have environmental and social protection legislation on par with internationally accepted norms – but rather failure in implementation of the laws.⁹⁹

RESPONSIVENESS

The AfDB has drawn both praise and criticism for the way in which it has dealt with countries facing rapid exogenous shocks or domestic crises. Praise has been given specifically for the promptness of the AfDB's intervention in crisis situations, especially when high-level political leadership has become involved. Criticism, however, has been directed at the manner of the response, for example when the approval and disbursement of 'emergency' funds take more than a year.¹⁰⁰

Stakeholders in Nigeria suggested that it is this aspect of the AfDB development financing mandate that needs most attention. Consultations revealed that in AfDB operations there are no procurement processes for securing emergency loans for infrastructure. However pressing the circumstances, loan cycle procedures must be

96 Humphrey C, 2015, *op. cit.*

97 Bradlow D, *op. cit.*

98 NDB, 'Environmental and Social Framework', March 2016.

99 Interview, New Development Bank, 26 August 2016.

100 Woods N & M Martin, *op. cit.*

followed to the letter and there is no option for fast-tracking the process. Although grants have been offered to the Nigerian government by the AfDB in the past to address human development concerns, all of them were subject to the stipulated 'rigorous and cumbersome' procurement process.

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The AfDB is perceived as unduly responsive to short- to medium-term changes in domestic circumstances (eg, as a result of a new government or changed sector strategy). Funding from the AfDB is also too closely tied to the bank's Country Strategy Papers (CSP). CSPs, drafted every three to four years in consultation with the host country and in line with its crucial national policies, are intended to bring the bank's strategy in line with that of respective member states. If a proposed activity is not in the CSP, however, the process of obtaining AfDB finance is difficult. Reviewing CSPs every 12–18 months, or whenever significant strategic or policy changes take place, would help alleviate this problem.

In Botswana the AfDB has been criticised for its low response to development needs that fall outside the scope of the CSP. This experience indicates a need to further intensify consultations, especially with the private sector, during consultations in the process of drafting the CSP. The AfDB needs to strengthen its co-operation with the private sector because, although weak at present, that sector is expected to contribute significantly to Botswana's future economic development.

KNOWLEDGE SERVICES

As noted earlier, knowledge services are extremely important for MDBs. They allow them to offer timely and relevant policy advice and, in the case of the AfDB, provide policy guidance appropriate to the African environment.¹⁰¹ MDBs in general have a unique advantage in their benefiting from past experience to improve their approaches and practices in developing countries. The AfDB has a suite of knowledge products (including books, journals, working papers and data banks), as well as statistical compilations and capacity-building activities for which there is a significant demand.¹⁰²

Regrettably, dissemination of this information has been less than optimal. A survey of governments involved with the AfDB indicated that 90% of respondents use the

101 *Ibid.*

102 AfDB, 'Annual Report 2015', *op. cit.*

AfDB's knowledge services 'only occasionally' or even 'never'.¹⁰³ Data are not always accessible online, or are not always up to date; many stakeholders are unaware of the services offered and sometimes the research provided is not detailed enough to allow for effective use.¹⁰⁴ In addition, whereas the World Bank Group is known for its high-quality knowledge services, the AfDB is seen to be less capable of providing them. Some observers in Nigeria believe this perception limits demand for AfDB services, although others consider that this perceived weakness is offset by the AfDB's pro-Africa orientation. On the whole, however, there is room for improvement in its offerings.

In Botswana, AfDB knowledge services have been received more positively. The bank's non-lending activities, including analytical and diagnostic work deriving from the policy of enhancing operations in MICs, have strengthened its partnership with the government and made the bank one of Botswana's preferred MDBs. The AfDB's strong engagement in non-lending services in Botswana has also helped the bank to gain funding for further infrastructure projects, including an LOC to the National Development Bank, an agricultural project in Pandamatenga and a 600MWe electrical generation scheme in Mmamabula.

In considering knowledge services a distinction must be drawn between 'soft' services such as reports, databanks and other knowledge products, and technical and policy advice offered by institutional advisors. The latter aspect is significantly the more important of the two. Often countries reach out to MDBs to access their financing but equally to acquire their expertise.¹⁰⁵ For example, recipient countries' decisions to opt for borrowing from the IBRD or IDA are influenced by the highly specialised technical, knowledge and policy design services that accompany lending from the World Bank. The IDA conducts analytical studies for recipient countries to help build the knowledge base that fosters intelligent design of projects and policies; in this regard the World Bank institutions are seen as superior. Nonetheless, despite inefficient knowledge dissemination and the widespread view of the World Bank as being the superior institution, extensive interaction on the continent and a clear understanding of the African operating environment and its challenges presents the AfDB with a unique opportunity to increase its development impact.

The NDB has stated that it will not develop 'soft' knowledge services, but it certainly intends to address knowledge problems attending the project preparation phase. In the Articles of Agreement establishing the NDB, provision is made for special funds, the first of which will be a dedicated project preparation facility. This will not be a 'desk' but rather a 'fund' from which money can be drawn to pay for expertise to assist countries with project preparation. There is a strong indication from African stakeholders that development of local capacity is more important

103 Woods N & M Martin, *op. cit.*

104 *Ibid.*

105 Humphrey C, 'Scoping workshop: Development Finance in Africa' conference, 24 August 2016.

than technical assistance.¹⁰⁶ This is especially pertinent for project preparation, in which borrowers often lack the necessary competence. For a lasting impact in this area, therefore, instead of merely recruiting outside consultants to handle the job the NDB should focus on longer-term capacity building with the aim of ensuring that the requisite skills are developed locally.

Although the NDB lacks the comparative knowledge advantage of other MDBs with decades of experience of development projects in different countries, it will look to carve a niche for itself in sustainable infrastructure. This will include not only renewable energy but also other infrastructure areas such as wastewater and sewerage treatment and sustainable water usage, and methods of freight transportation and public transport that reduce CO₂ emissions.¹⁰⁷ The NDB should aim to become the leading global institution for 'green' infrastructure project finance and implementation; success in this would allow it to focus its nascent knowledge in one critical area that might be neglected by other MDBs (although now of increasing importance for most MDBs, this is not necessarily their area of expertise). Different development finance institutions acquire specialities over

There is a strong indication from African stakeholders that development of local capacity is more important than technical assistance

the years in response to the weightiest needs of their clients. For example, the AfDB developed specialist skills in infrastructure financing; the DBSA found for itself a niche in project preparation. Sustainable infrastructure (eg, project design and implementation, financing modalities) is an area in which the NDB might develop its own specialisation. It should try to attract the best global expertise in 'green' financing and interact with innovators in that field: new approaches are being developed around 'green' bonds with the aim of enticing pension funds to invest in such endeavours and the NDB would do well to become a home for such innovations.¹⁰⁸

One way in which it could supplement its technical knowledge with 'softer' research issues is by funding research in line with its strategic priorities. This would limit the staffing requirement and help maintain the nimble structure the bank is pursuing while also contributing to policy debate. Such a policy could also be coupled with dedicated efforts to increase research capacity in member countries and develop and draw on the capacity of their local DFIs.¹⁰⁹

106 Woods N & M Martin, *op. cit.*

107 Interview, New Development Bank, 26 August 2016.

108 Humphrey C, 'Scoping workshop' 2016, *op. cit.*

109 Kapoor S, *op. cit.*

KEY SUCCESSES IN LENDING: BUSINESS PRACTICES

Despite the critical challenges outlined above the AfDB has managed to retain its influence among African countries through a number of interventions. Its lending, even from the non-concessional window, remains attractive to MICs. Its development knowledge and know-how has given it a key competitive advantage over other financing sources, and it has leveraged this asset to ensure relevance to member countries. The AfDB has also maintained its image as an African bank serving African interests, a positioning that contributes to its credibility on the continent and elsewhere.

ATTRACTIVE FINANCIAL TERMS

One of the main competitive advantages enjoyed by MDBs over private sector finance in particular is the preferential interest rates, long maturity rates and grace periods offered member countries.¹¹⁰ Low rates are achieved through sound financial management of the institution, which ensures a positive rating from rating agencies. This in turn allows for better lending terms on global bond markets, the benefits of which are eventually passed on to borrowers. In addition most MDBs, unlike private institutions, are not profit driven,¹¹¹ which allows them to offer low interest rates given that they have only to cover their operating costs. Rates offered by the AfDB are comparable to or better than those of other regional banks such as the Inter-American Development Bank. This is certainly the experience in Botswana, where stakeholders suggest that competitive loan terms have constituted the main strength of the AfDB in its Botswana lending operations. AfDB funding is also seen as competitive when matched with that of other IFIs operating in Botswana. Table 4 illustrates the highly competitive terms offered by the AfDB.

TABLE 4 FINANCIAL TERMS FOR VARIABLE LENDING RATE NON-CONCESSIONAL LOANS, 2014		
	MAXIMUM MATURITY (YEARS)	ALL-IN INTEREST RATE
AfDB	20	0.994%
IADB	25	1.220%
AsDB	19	0.570%
IBRD	18	0.830%

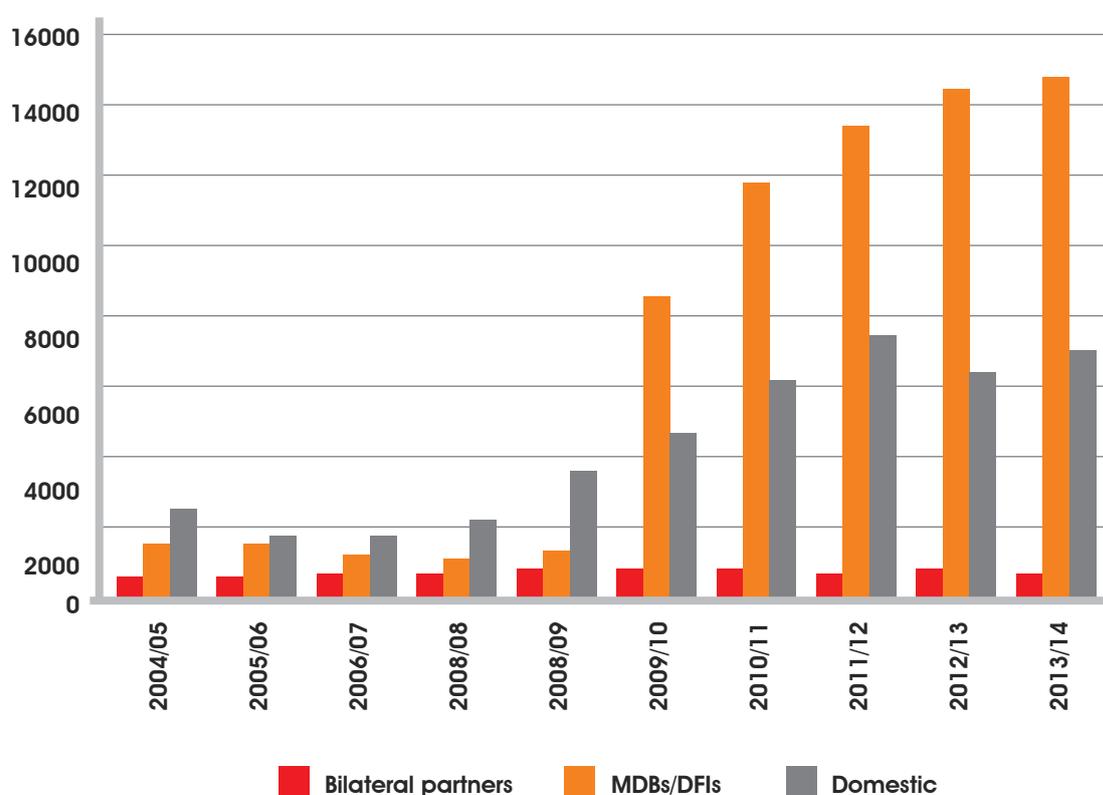
Source: Humphrey C, 'The African Development Bank: Ready to Face the Challenges of a Changing Africa?', Expertgruppen för Biståndsanalys, 6 July 2016, <https://www.oecd.org/derec/sweden/The-African-Development-Bank.pdf>

110 AfDB, 'Financial Products Offered by the African Development Bank', Abidjan: AfDB, 2011.

111 Although some MDBs (eg, the IBRD) make additional income from loans granted to countries, this is used to fund operations rather than pay out dividends to member states. MDBs typically do not maximise profit; additional income goes to ensure the institution's financial stability.

From Figure 9 it is evident that MDBs and IFIs are the largest source of external financing in Botswana, which enjoys a higher level of satisfaction with MDBs than with bilateral organisations and prefers to use such institutions. In seeking finance for infrastructure projects the Botswana authorities consider factors such as loan pricing, longer maturity and grace period, and technical expertise in project preparation and M&E. This generally puts MDBs in a better position than their counterparts in financing projects in Botswana.

FIGURE 9 GROSS OUTSTANDING GOVERNMENT LOANS (BWP MILLION): 2005–2014



Source: Author's calculations, using Bank of Botswana, 'Botswana Financial Statistics', <http://www.bankofbotswana.bw/content/2011062816053-botswana-financial-statistics-past-issues>, accessed 25 August 2016

At the same time the AfDB manages to raise capital on global markets at better rates than those available to sovereign African countries. Between 2007 and 2013 a selection of countries raised \$8.1 billion on global capital markets at an average interest rate of 6.1% and an average maturity of 11.2 years; the AfDB achieved the same but at 1% interest and 20 years' maturity. Although other national

development banks (such as those of China and India) have offered better rates than commercial institutions, these are still less attractive than those of the AfDB.¹¹²

AN AFRICAN PARTNER REPRESENTING AFRICAN INTERESTS

A survey of nearly 220 African stakeholders involved with the AfDB shows that 84% of respondents considered it a 'preferred partner'. This may be partly attributed to the AfDB's advocacy of African positions in important international forums and initiatives such as the G20 and the UN climate change conferences, and the development and adoption of the Sustainable Development Goals (SDGs), as well as the fact that it is led, managed and staffed by Africans.¹¹³ Its reputation in the region is further enhanced by its support for African initiatives such as Heavily Indebted Poor Countries (HIPC), the Multilateral Debt Relief Initiative (MDRI) and NEPAD, and its championing of important African issues such as food security, sustainable growth, financial inclusion and managing epidemics (eg, HIV/Aids, polio and Ebola).¹¹⁴

African countries also appreciate the manner in which the AfDB aligns its disbursement priorities with their needs: it stresses infrastructure lending rather than following a catch-all strategy that tries to fund everything

These characteristics, together with the notion that the AfDB understands the real needs of the African continent, lend legitimacy to the organisation and mean that African governments more readily accept its advice.¹¹⁵ Its appreciation of Africa's needs and priorities is perhaps best reflected in the bank's 10-year strategy (2013–2022), which highlights the continent's main challenges and sets out its response to them. The operational priorities of this strategy include infrastructure development, regional economic integration, private sector development, improved governance and accountability and increasing skills and technology.¹¹⁶

African countries also appreciate the manner in which the AfDB aligns its disbursement priorities with their needs: it stresses infrastructure lending rather

112 Humphrey C, 2016, *op. cit.*

113 Woods N & M Martin, *op. cit.*

114 Ojah K, 'African Development Bank must gear up for a more proactive role', *The Conversation* (online), 18 June 2015, <https://theconversation.com/african-development-bank-must-gear-up-for-a-more-proactive-role-43085>, accessed 5 September 2016.

115 Weiss M, 'The African Development Bank Group', Washington DC: Congressional Research Service, 30 January 2009.

116 AfDB, 'AfDB's Strategy for 2013–2022', Abidjan: AfDB, <http://www.afdb.org/en/about-us/mission-strategy/afdb-strategy/>, accessed 27 August 2016.

than following a catch-all strategy that tries to fund everything.¹¹⁷ This focus is reflected in the fact that in 2015, 40% of total disbursements targeted infrastructure.

Table 5 sets out the priorities identified by different bank stakeholders.

TABLE 5 PRIORITIES OF DIFFERENT STAKEHOLDERS				
CLIENT GROUP	PRIORITY 1 ^a	PRIORITY 2	PRIORITY 3	PRIORITY 4
Polymakers	Infrastructure	Higher education	Private sector	Governance
Parliamentarians	Infrastructure	Higher education	Governance	Private sector
Private sector	Infrastructure	Private sector	Governance	Higher education
CSOs	Infrastructure	Governance	Higher education	Private sector

a AfDB, 'AfDB's Strategy for 2013–2022', Abidjan: AfDB, <http://www.afdb.org/en/about-us/mission-strategy/afdb-strategy/>, accessed 27 August 2016.

Source: Woods N & M Martin, 'The preferred partner? A Client Assessment of the African Development Bank'. Abidjan: African Development Bank, 2012

In fact, many stakeholders feel that the bank has scope for reducing its range of activities to concentrate more on infrastructure financing, allowing other development institutions to operate in other sectors and in that way create a clear distinction between the activities of different partners.¹¹⁸

The AfDB operates in a unique environment. Among the defining characteristics of Africa are widespread and extreme poverty; low human development indicators; many small and disparate economies with relatively low levels of integration; high levels of conflict and endemic disease; poor infrastructure; widespread corruption; and volatile economic growth.¹¹⁹ Against this complex background and with its unquestioned African 'authenticity', the AfDB is ideally placed to help meet the challenges facing its member countries and to understand and address their problems. The NDB should take note of this important factor: already the BRICS grouping is viewed by many African countries as an advocate of developing and emerging country interests, and the NDB should move to capitalise on this view through, for example, using the BRICS's privileged position to further champion the interests of developing countries in global forums such as the G20.

117 Woods N & M Martin, *op. cit.*

118 Woods N & M Martin, *op. cit.*

119 Kapoor S, *op. cit.*

CONCLUSION AND RECOMMENDATIONS FOR THE NDB

As the NDB begins to operate in Africa it is important for the institution to consider the accumulated knowledge of other MDBs with more extensive experience on the continent. This paper highlights a number of overarching changes that the NDB must take into account ahead of its involvement in Africa, as well as giving thought to specific business processes that have hindered lending to African countries.

At a macro level, the following emerge as key issues:

- Large-scale infrastructure developments have often been criticised as frequently exceeding both their estimated cost and deadline. Given the NDB's limited knowledge and experience in implementing very large infrastructure projects, it should make a serious effort to learn from other more experienced institutions (perhaps through means such as project co-financing). This will ensure optimal development outcomes and value for money.
- The NDB cannot divorce itself from global discourse related to environmental and social safeguards; equally it cannot escape the pressure from NSAs to adhere to international best practice. It should therefore institute mechanisms aimed at frequent and timely communication with such groups to address their concerns. Transparency could be enhanced, possibly by setting up an independent accountability mechanism.
- The bank should prioritise key sectors and not necessarily 'be everything for everyone.' The NDB's stated mission is to fund infrastructure and sustainable development projects. By focusing on strategic areas such as sustainable infrastructure it could create an area of specialisation, for example in green finance, renewable energy and sustainable infrastructure. But it is equally important that the NDB defines and refines its understanding of what constitutes sustainable infrastructure.
- The evolving nature of MICs requires MDBs to adopt a bespoke approach to those countries in terms of both business processes and provision of technical support, concentrating on closing existing capacity gaps. The NDB's focus should be on the main challenges faced by these countries, such as inequality and unemployment; such an approach calls for a concentration on more inclusive development as well as on priorities such as infrastructural development. The NDB's main clients are likely to be MICs. As in the case of Nigeria (but equally in the BRICS themselves), such countries are not immune to exogenous shocks: the NDB should ensure that contingency plans are in place, in readiness for sudden external shocks in order to respond swiftly and effectively.
- The NDB, given its unique positioning within countries of the global South, should exploit this competitive advantage and apply its services in areas where other institutions might struggle. A notable example lies in carrying out the requisite project preparation, which at the moment poses a major bottleneck

for further infrastructure development. In addition, the NDB should consider financing infrastructure in those sectors that attract less interest from other financiers, such as water and sanitation (while still maintaining its 'sustainable' specialisation, for example, in the treatment of waste water).

- The NDB should promote greater equality in its governance processes, including gender equality. Greater inclusive development could be achieved if gender considerations are taken into account from institutional arrangements and policies throughout the lifecycle of infrastructure financing. The NDB is unlikely to respond adequately to gender inequality issues in project implementation if it fails to achieve an equitable gender distribution in its senior management.
- The use of domestic currencies remains a critical issue for governments seeking to access MDB infrastructure finance. Although lending in foreign and domestic currencies each has its pros and cons, the NDB could explore modalities around blended currency loans, which would allow borrowers to direct different currencies to areas where they can be most efficiently used, while at the same time ameliorating currency risk.
- Infrastructure funding institutions have different strengths and weaknesses. By co-operating with other types of funding sources (eg, private finance, ODA or DFIs), the NDB could draw on various partners' unique advantages, thereby ensuring more favourable outcomes (such as decreased risk, lower cost and greater development impact).

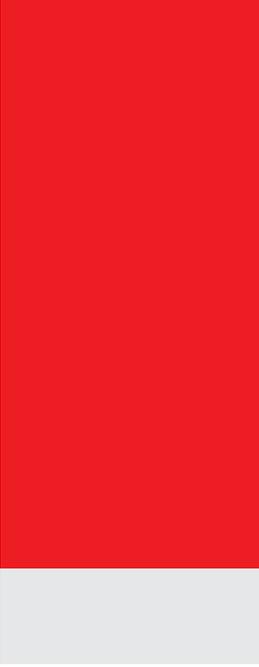
Specific institutional constraints – lengthy loan approval processes; limited use of countries' own systems; sensitivities attending environmental and social safeguards and excessive conditionalities; the need for responsiveness; and the importance of knowledge services – have all been discussed. For the most important of them, particular attention is warranted and action recommended:

- Lengthy and costly loan approval processes have been flagged as one of the most significant business practices that discourage borrowing from MDBs. This paper has offered a number of ways in which to improve this situation, including drawing on the experience of the CAF in which certain approvals can be given by the institution's senior management (as opposed to board approval for every project). Equally, the NDB should implement simplified and standardised procedures for smaller loans, which will assist in facilitating the lending process. In addition, in cases where capacity gaps hinder greater borrowing, help in capacity building should be offered to borrowers.
- UCS (eg, ESF or procurement) is already a central issue for the NDB, highlighted in various policy documents. It is recommended that the stress should be on supplementing existing systems in member states, which will inevitably differ from each other, rather than compelling these countries to duplicate efforts by complying with 'NDB specific' PFM processes in addition to their own. Instead of placing the onus on member countries to comply with bank-specific processes, the reverse should apply: it should rather be for the

bank to comply with the processes of member states. It is also important to explore linkages with local DFIs, partly with a view to learning from their experience and also for complementing existing infrastructure development initiatives.

- The current membership structure of the NDB places it in the unique position of preventing non-borrowing countries from holding significant sway in its policy decisions. Conditionalities tied to loans from so-called Washington Consensus institutions should therefore pose less of a problem to its members and borrowers if the current structure is maintained. Nevertheless, if the NDB wants to maintain and enhance its credibility it needs to adhere to international best practices in terms of ESF and ensure that these are reflected in the projects it finances. In this respect, broad-based principles should be pursued (eg, transparency; do no harm; and result orientation) rather than its issuing very prescriptive directives.
- Knowledge services remain an important – although in many respects a niche – facility provided by MDBs. A distinction needs to be drawn, however, between ‘soft’ knowledge services and more technical assistance programmes. Whereas the former tends to be less valued by some clients, technical know-how should be a key offering of the NDB to ensure ‘ownership’ and the sustainability of the projects it finances. Nevertheless, it is important for the NDB to attract the best possible expertise as it develops its niche in the sustainable infrastructure financing landscape.
- The AfDB has achieved appreciable legitimacy among regional member states by campaigning for their interests and responding to their needs. In this regard the NDB has already made significant strides as a champion of the global South and emerging countries generally. Not only will this enhance relations between the NDB and governments from member countries but it will also probably lead to closer working relationships. The NDB should exploit the privileged positions of its five member states in global forums such as the G20 to promote the infrastructure financing interests of emerging and developing countries.

The NDB was launched to provide BRICS nations with a real alternative in infrastructure financing. It wishes to position itself as a bank that manages to overcome the bottlenecks typically found in infrastructure financing and to become a faster, leaner lending outfit that can properly address the needs of BRICS members. In order to realise this ambition it needs to learn from the experience of existing MDBs and, based on those lessons, chart a new way forward in pursuit of context-specific solutions and a flexible engagement process.



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