A New and Improved African Development Bank?

An update on recommendations from the CGD working group

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CGD Brief

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Since the African Development Bank is now asking for major new contributions, the Center for Global Development is revisiting its six recommendations for the Bank and its shareholders. How much progress has the Bank made?

In late May 2010, the African Development Bank (AfDB) will be seeking approval from its shareholders for a tripling of its capital base. The Bank is concurrently negotiating with shareholders for their triennial contributions to its soft loan window. In essence, the AfDB is asking not only for substantial new money, but also a de facto vote of confidence in its long-term future. Thus, it seems both timely and prudent to ask how the Bank is doing.

The AfDB's history has been tumultuous. Despite its ambitions to be the leading development institution in Africa, the Bank found itself nearly bankrupt in the mid-1990s and, by many accounts, had clearly lost its way. By the early 2000s, the AfDB had fixed its balance sheet and restored its AAA credit rating, but was still searching for its niche among the other international financial institutions and, to many observers, had yet to prove its *raison d'être*. The Bank was financially sound again, yet strategically adrift. The case for continuing to attract donor support or seizing regional economic leadership was yet to be made. To make matters worse, the Bank was forced by political violence in Abidjan to flee to a new temporary location in 2003. Arriving at its emergency home in Tunisia, the direction of the AfDB—and indeed its very existence—was very much in doubt.

Into this deep uncertainty stepped Donald Kaberuka, a former finance minister of Rwanda, who was elected President of the AfDB in 2005. His task was to reinvigorate the Bank—to fulfill its original mission to help lead Africa away from the margins of the global economy toward a better future.

To help examine strategic options for the AfDB, the Center for Global Development convened an expert working group in 2006 to assess, in a frank and independent manner, the challenges the Bank faced. The group's report, *Building Africa's Development Bank,* laid out six specific suggestions for both the shareholders and the then-new management.[2]

The AfDB is today facing another pivotal moment. Its appeal for a general capital increase (GCI) of 200 percent is significant, comes in the midst of a period of fiscal tightening by most shareholders, and coincides with similar GCI requests from nearly every other international financial institution. At the same time, the Bank's soft loan window, the African Development Fund (ADF), is also in the middle of negotiations for its regular triennial contributions to enable

1. Todd Moss (tmoss@cgdev.org) is senior fellow at the Center for Global Development. Thanks to Julia Barmeier for her assistance and to numerous colleagues who provided comments. Any errors are solely my own. CGD is grateful for contributions from the Norwegian Ministry of Foreign Affairs in support of this work.
2. Dennis de Tray and Todd Moss, *Building Africa's Development Bank: Six Recommendations for the AfDB and Its Shareholders*, Center for Global Development (2006), http://www.cgdev.org/content/publications/detail/10033.

concessional lending to its low-income clients. It is a huge request at a difficult time.

As part of GCI and ADF discussions, shareholders are engaged in trying to measure the Bank's efficiency and effectiveness. It also seems an opportune time to revisit each of the six recommendations of the Center's AfDB working group and ask: How is the Bank doing?

It is first worth putting the current debate in perspective. Even the consideration of a GCI today is a major sign of success. Just four short years ago, the question was whether the Bank should even exist. Was recovery just wishful thinking? Was it better to just fold the portfolio into the World Bank? Such questions make no sense today. Instead, policymakers are seriously debating whether the Bank should be two times or three times larger. This alone shows that the Bank is once again (or perhaps, finally) a major player.

Recommendations for Bank management

Our report made three specific recommendations for President Kaberuka and his management team. Below is an update and, for shorthand, grades for progress on each:

1. Define your future: Promoting economic growth should be the Bank's primary objective.

GRADE: B+ With donor agencies increasingly targeting the social sectors and public service delivery, the working group recommended a strategic focus on generating higher rates of economic growth in client countries, which, operationally, would mean (a) increasing support for the private sector, (b) working deliberately to connect Africa's fragmented markets, and (c) promoting better economic governance. This agenda became even more urgent following the global economic crisis, which pushed the region's overall growth rate down from 5 percent in 2008 to just 1.7 percent in 2009.

The AfDB responded aggressively to changing global conditions, launching large emergency liquidity and trade finance facilities (contributing to the need for the GCI) and frontloading disbursements, including accelerated lending to low-income countries. These actions likely mitigated the effects of the crisis and helped prevent the region from falling into recession.

Perhaps more important for the long term, the AfDB has been shifting its portfolio to align with growth objectives. Lending through the private sector window has risen steadily, from less than US$300 million per year to more than US$1.5 billion in 2009 (Figure 1). Recent private sector projects have included banking in Liberia and the Democratic Republic of Congo, power projects in South Africa and Egypt, and loans to regional private equity funds. Much of the new request for capital infusion is to maintain this high level of private sector operations.

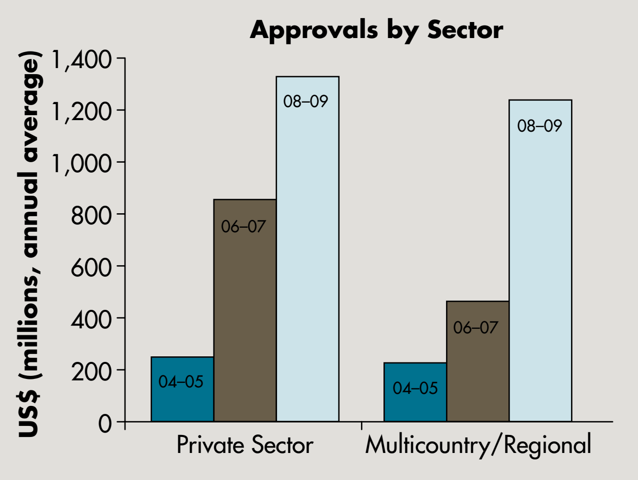
New approvals for complex multicountry or regional projects are showing similar dramatic increases, at least in terms of pushing new loans out the door (Figure 1). The lion's share of these projects is in transportation and power, for example, a new segment of the Bamenda-Enugu Corridor of the Nigeria–Cameroon Highway and a Nile Equatorial Lakes regional power grid.

The more difficult area is good governance, where the instruments and impacts are less obvious. Arguably, the AfDB is

REPORT CARD

BANK MANAGEMENT	
Promoting economic growth:	**B+**
Specializing in infrastructure:	**A–**
Leading on critical issues:	**A**
SHAREHOLDERS	
Reducing shareholder demands:	**C** (2007); **Incomplete** (2010)
Transforming the Board into a nonresident, nonexecutive body:	**F**
Settling the location issue:	**Incomplete**

Figure 1



Source: AfDB.

better placed than its Washington-based peers to push its clients toward best practice, but its leverage and role are still far from clear. The Bank is reportedly working on new country diagnostics, but more promising may be collaboration with other initiatives, such as AfDB support for the Investment Climate Facility for Africa and the Extractive Industries Transparency Initiative (EITI).

2. Specialize in one sector that matters to growth: Infrastructure.

GRADE: A– Lack of infrastructure is a major impediment to economic growth in the region.[3] Decades of underinvestment, combined with growing donor aversion to financing large infrastructure, have left a significant gap in sanitation, transportation, and energy.[4] Not only is the demand for new projects tremendous, but infrastructure is a sector in which the AfDB has a reasonably good record and reputation. The working group even recommended moving toward a portfolio of new loans exclusively in infrastructure.

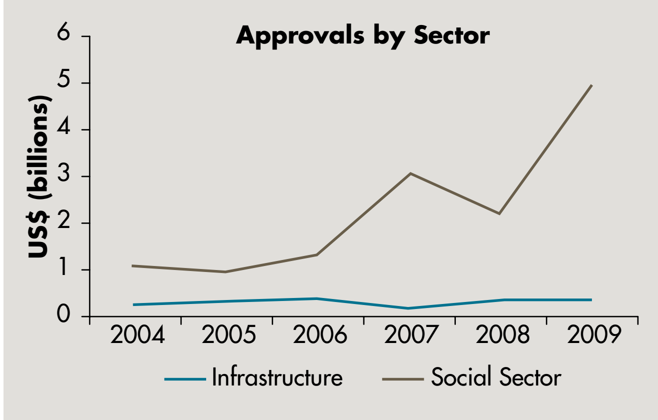
The AfDB has made major progress in becoming largely an "infrastructure bank." Although the 100 percent infrastructure goal was more of a device than a realistic target, the Bank has substantially increased amounts of new lending directed to that sector, with total infrastructure approvals reaching more than US$5 billion in 2009, greater than all new Bank lending just two years earlier (Figure 2). The proportion of lending for infrastructure has also risen, while social sector projects fell to just 3 percent of the total in 2009.

3. Lead, but don't lend, on critical regional and global issues.

GRADE: A The working group felt strongly that the AfDB was much larger and more important than its loan portfolio, and in a distinctive position to push for reforms. We urged the Bank to play a leading role as a voice for the continent in global fora, to be aggressive on international issues of relevance to Africa, and, at the same time, to resist the inevitable urges to dilute the portfolio. In short, Kaberuka should not be shy about using his unique soapbox.

This is where the Bank's transformation is most apparent. The AfDB has stepped forward as an advocate and convener for the continent, and helped ensure that Africa was not ignored

Figure 2



Source: AfDB.

during the financial crisis. It created a committee of finance ministers and central bank governors (the C-10) to formulate a common position ahead of the G-20 meetings, which was critical to enabling a "fiscal stimulus" for Africa. Kaberuka was active in the Copenhagen climate negotiations, pushing for rich country commitments to help Africa tackle the consequences of global warming. He is increasingly a visible and credible voice on global health, food security, and other issues of deep relevance to the Bank's constituents.

Recommendations for the shareholders

The working group also made three specific recommendations for the Bank's shareholders, stressing that the AfDB can succeed only with strong (but not overbearing) support of its members.

1. Back off: Reduce the laundry lists of shareholder demands.

GRADE: C (2007); INCOMPLETE (2010)

Successive ADF replenishments had seen long and growing lists of special requests and requirements from individual shareholders, which reduce Bank management's ability to make calculated decisions. Although all multilateral development banks suffer from this syndrome, the working group felt it was most debilitating for the AfDB since its strategic focus had been so thoroughly dissipated.

The last ADF replenishment agreement (ADF-11, 2007) appears to be no worse than the previous two rounds. The current negotiations for ADF-12 are ongoing, with a July 2010 target. Once they are completed, we will have a better sense of whether or not shareholders loaded the Bank

3. Vijaya Ramachandran, Alan Gelb, and Manju Shah, *Africa's Private Sector: What's Wrong with the Business Environment and What to Do About It*, Center for Global Development (2009).

4. Vivien Foster, *Overhauling the Engine of Growth: Infrastructure in Africa*, Africa Infrastructure Country Diagnostic, World Bank (2008).

The Center for Global Development works to reduce global poverty and inequality through rigorous research and active engagement with the policy community to make the world a more prosperous, just, and safe place for us all. The policies and practices of the United States and other rich countries, the emerging powers, and international institutions and corporations have significant impacts on the developing world's poor people. We aim to improve these policies and practices through research and policy engagement to expand opportunities, reduce inequalities, and improve lives everywhere.

with new directives. Some shareholders are likely to press for new operations in food security, climate change, and other areas. Current signs are fairly positive, however, with many shareholders talking about ADF-12 as a period of consolidation rather than introducing new initiatives.

2. Lighten up: Transform the Board into a nonexecutive, nonresident body.

GRADE: F Shareholders are still missing the opportunity to streamline governance of the AfDB by aligning the structure and function of the board with 21st century best corporate practice. Moving to a nonexecutive, nonresident board would reduce costs of all kinds and clarify the distinctive roles of shareholders and management. Indeed, the AfDB could be an example to other international financial institutions of a more efficient model.[5] Yet there has been no progress, and no real discussion of this option among the shareholders. Indeed, all signals point to a heavier board presence, with the possible addition of even more board seats.

3. Confront the location issue since the unsettled "temporary" headquarters status is a roadblock.

GRADE: INCOMPLETE Political sensitivities are such that it has been nearly impossible to hold a frank, open debate about the future location of the Bank. However, the next annual meetings of the AfDB are scheduled to take place in Abidjan at the end of May 2010. This is presumably a test-case for Côte d'Ivoire's readiness for a possible return of the Bank to its original headquarters. Despite positive signs that Bank staff are adapting well to Tunis (and vice-versa), the temporary status of its location will continue to hamper recruitment and other operational issues. It is hoped that, once the meetings are complete, the Bank will be better able to decide to return to Abidjan, remain permanently in Tunis, or seek another location.

Conclusion: Shareholders are lagging

Any frank assessment of the AfDB today would still identify numerous, thorny challenges remaining if it is to stay competitive and increase its impact—for instance, loan quality, results assessment, disclosure, recruitment, problematic criteria for budget support, and other operational issues. There is, of course, still much work to be done, and the shareholders are right to hold the Bank to high standards. At the same time, the promising changes over the past few years suggest that the AfDB has taken several giant and impressive steps toward fulfilling its ambitious mission. Bank management has clearly articulated a strategic vision, substantially shifted its loan portfolio to reflect this plan, and asserted leadership on a range of global issues critical to the future of Africa. So far the shareholders have largely stood still. The coming months should present opportunities for them to play their part in helping Africa's Bank continue to build on its path to success.

5. Dennis de Tray and Todd Moss, "Fixing International Financial Institutions: How Africa Can Lead the Way," CGD Notes (September 2006), http://www.cgdev.org/content/publications/detail/10391.