AFRICAN DEVELOPMENT BANK GROUP
GROUPE DE LA BANQUE AFRICAINE DE DÉVELOPPEMENT

# Lending Capacity of Multilateral Development Banks

**G-24 TECHNICAL GROUP MEETING**
**17 July 2023**

# The Global Economic Landscape is Fast Changing

- Conflict and Security
- Overlapping Crises
- Slower Economic Growth
- Reversal of recent Hard won Development Gains
- Debt Sustainability Challenges
- Increasing Poverty
- Climate Change

# Bridging the SDG financing gap in Africa

**USD 1.3 trillion annually needed to achieve the SDGs (which are already off track) on the continent**

- **Africa's challenges are a matter of global concern**
- **Immense power deficit across the continent**
- **Africa's growth potential not fully realized**
- **Millions in Africa lack basic water and sanitation services**

## Impact delivery from projects completed by the Bank Group in 2022

- 1.3 million people with new electricity connections
- 774 km of new or improved power distribution and transmission lines
- 612 MW of new power capacity installed, of which 113 MW renewable
- 2.6 million tons of $CO_2$ emissions reduced

- 2.9 million people benefited from improvements in agriculture
- 1,682 km of feeder roads built or rehabilitated
- 11,100 hectares of land with improved water management

- 833 km of roads constructed, rehabilitated, or maintained
- 4.1 million people benefited from investee projects
- 396,500 owner-operators and MSMEs got access to financial services

- 146 km of cross-border roads constructed or rehabilitated
- 2.9 million people gained access to better transport services

- 12.3 million people with new or improved access to water and sanitation
- 340,000 people trained, of which 66% women
- 60,000 people benefited from better access to education

**The Bank's High 5s are at the center of Africa's transformation**

# Africa's challenges are a matter of global concern

## Demographic

- More than 232 million people are hungry or malnourished (roughly 1 in 4)
- 11% GDP loss in Africa is caused by malnutrition
- 34% of children under 5 are stunted

## Economic

- Over $100 billion made in revenue each year from chocolate…
  …of which Africa just receives 2%
- 60% of the world's arable land not yet put into production is in Africa

## Environmental

| | |
|---|---|
| Devastating storms and floods afflicted Southern Africa in 2019 and expected return of El Niño could suppress agricultural output and growth in East Africa | Weather shocks costing 2% contraction in GDP |

## Our over-arching goals

End hunger and malnutrition

Contribute to eliminating extreme poverty

Make Africa a net food exporter

Move Africa towards the top of export-orientated global value chains

Unleash prosperity to lift millions out of poverty

## Our role

Reduce poverty

Promote agricultural development

Improve food security and nutrition

Boost economic growth

**Development impact** from projects completed in 2022

- **2.9 million people** benefited from improvements in agriculture
- **1,682 km** of feeder roads built or rehabilitated
- **11,100 hectares** of land with improved water management

**Transforming agriculture, the wealth of Africa, is central to growth, poverty eradication and food security**

# Global leaders are calling on MDB's to transform themselves and play a key role in support of the reform agenda

## RENEW MISSION AND VISION

Renew their missions and vision, update operating model and financial capacity, to rise to the challenges, within confines of respective mandates

## UPDATE OPERATING MODELS

Adjust institutional and operational models to meet these new challenges

## SCALE UP FINANCING FOR DEVELOPMENT

Making more efficient use of their capital, pursue financial innovation, including the option for channelling Special Drawing Rights through MDBs and, when appropriate, increasing their capital base

## STEP UP PRIVATE SECTOR MOBILIZATION

Mobilize private sector f by expanding the use of innovative risk-sharing tools and platforms, improving the business environment and providing project preparation, improving execution capacity, and greater use of blended finance

## USE OF CONCESSIONAL FINANCE

Use concessional and low-cost finance where additionality and impact are greatest

## ENHANCE TOOLS FOR CLIMATE AND DISASTER FINANCING

Enhance MDBs' tools for climate and disaster risk finance and insurance mechanisms. including the inclusion of climate resilient debt clauses

## SUPPORT COUNTRIES GREEN TRANSITION

Support countries to devise pathways to sustainable development and green transition, with a strong focus on capacity building, policy dialogue, reforms. And underlying analytics

## OPERATE EFFECTIVELY AS A SYSTEM

Operate more efftcively as a system and enahnace collaboration among the many development players including ccivil society organisations and base don comparative advantage

# The G20 Capital adequacy recommendations will help enhance MDB capacity and leverage existing capital within the system

**The recommendations grouped under 5 main categories:**

1. Redefine the Approach to Risk Appetite in Capital Adequacy Frameworks
2. Incorporate Uplift from callable Capital into MDB Capital Adequacy Frameworks
3. Implement Innovations to Strengthen MDB Capital Adequacy and Lending Headroom
4. Improve Credit Rating Agency Assessment of MDB Financial Strength
5. Improve the Enabling Environment for Capital Adequacy Governance

# Financial Innovations – Leveraging the Bank's Balance Sheet

## BALANCE SHEET OPTIMIZATION RATIONALE FOR THE BANK

**Risk Transfer**
Going beyond shareholder capital

**Create Headroom**
Reduce overall capital consumption or specific exposures

**Mobilize Investors**
Create pathways for investors to increase support for development financing

## INSTRUMENTS

| | |
|---|---|
| • **Exposure Exchange Agreement** | • **Risk Participation Agreements** |
| • **Securitization** | • **Asset Sale Down (incl. equity)** |
| • **Credit Insurance** | • **Credit Default Swaps** |
| • **Guarantees** | • **Hybrid Capital Issuance** |

## Why do we do it?

To **reduce the capital consumption** and **create additional lending headroom** for the Bank

Make more **efficient use of shareholder resources**

Enables the Bank to provide more development lending **without solely relying on additional shareholder capital**

# BSO Transactions - A proven approach to increase headroom

**Jan 2015**
**EEA**: The Bank entered into the first MDB exposure exchange on its sovereign portfolio with the World Bank and IADB

**Apr 2015**
**PSF**: The Bank was the first MDB to create a Private Sector Credit Enhancement Facility (PSF) to share risk on NSO in low-income countries

**Nov 2018**
**SST**: The Bank entered into the first MDB synthetic securitization on its non-sovereign loan portfolio with Mariner (Newmarket) and Africa50

**Dec 2018**
**CI**: The Bank entered into the first MDB portfolio credit insurance deal on its non-sovereign financial sector portfolio with ATI

**Nov 2019**
**CI**: The Bank entered a credit insurance transaction with private insurers on a guarantee provided to Senegal to back swaps on the country's Euro bond obligations

**2021**
The Bank has executed 3 partial assets sell downs since 2010 (most recent was closed in end 2021)

**Mar 2022**
**Guarantee**: The Bank executed the Lusophone Compact Guarantee for EUR 400 million in support of private sector in Portuguese-speaking Africa

**Oct 2022**
**R2RS**: The Bank executed a USD 2 billion transaction on the Bank's sovereign window with the UK's FCDO and private insurers leading to additional lending capacity for climate finance.

**May-June 2023**
The establishment of master framework agreements and insurance templates to accelerate mobilization

2015 · 2018 · 2019 · 2021 · 2022 · 2023

The Bank is discussing a new EEA with AsDB (USD 1 billion) to further enhance headroom available to countries that are near or high risk

The Bank is structuring a new SRT transaction on a USD 900 million diversified portfolio of private sector loans involving institutional investors to bring NSO approvals back to pre-COVID levels

**The Bank has executed risk transfer operations covering both its sovereign and non-sovereign loan windows and continues to originate new transactions in line with the G20 Recommendations on Capital Adequacy**

# Moving from billions to trillions with the private sector

**Global Investor Base**

- In 2020, institutional investors, sovereign wealth funds, and insurance companies collectively held over USD 110 trillion in assets globally, and this figure has soared over the past decade, and expected to reach **USD 150 trillion by 2025.**

**Africa's Investor Base**

- Sovereign wealth funds, pension funds, insurance companies, and other investment vehicles across Africa currently hold around **USD 2 trillion in assets**

**The private sector has the relevant capacity to bridge many of the significant financing gaps the continents is already facing if we are to meet the SDGs and continents climate change commitments as expressed through NDC’s**

# Mobilizing the private sector at scale

**Private Sector Mobilization interventions are needed to attract more of the global and regional investor pools that exist**

- Enabling Policy Environment and string Regulatory Frameworks
- Mobilizing Project preparation resources
- Enhanced products & tools to mitigate risks taken by private sector investors
- Reducing Transactions Costs
- Intervening in projects at scale

Supported by a strong Financial Sector and domestic capital markets

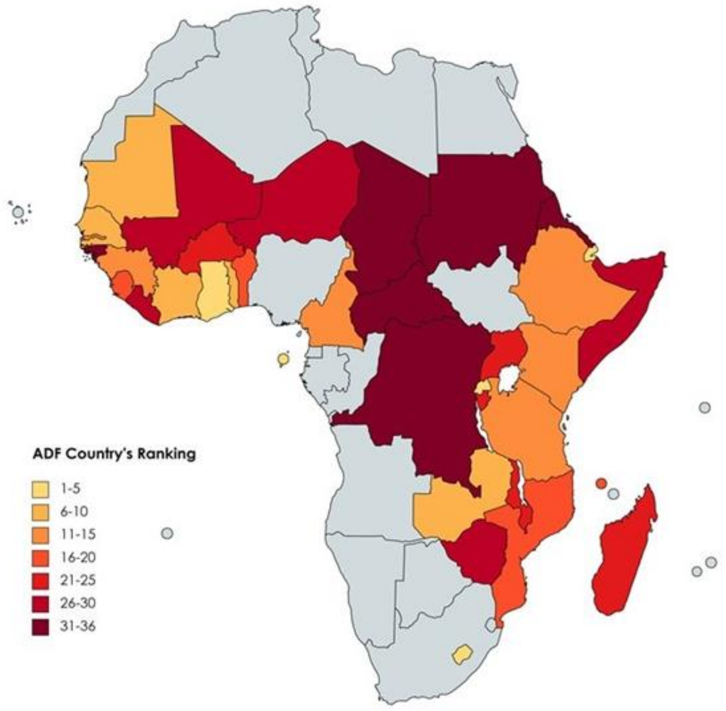
Capacity Building and Technical Assistance support to countries

# Escalating Loss and Damage in ADF

## ADF Countries most vulnerable to climate

**9 out of 10 countries most vulnerable to climate change in the world are ADF Countries** *(Notre Dame University, 2021)*.
**All 9 are conflict-affected and among the 20 ADF transition states**

ESCALATING LOSS AND DAMAGE IN ADF COUNTRIES




**Agriculture is the most exposed sector**:
decrease in yields of between 8 – 22% for Africa's rain-fed staple crops in the next 20 years

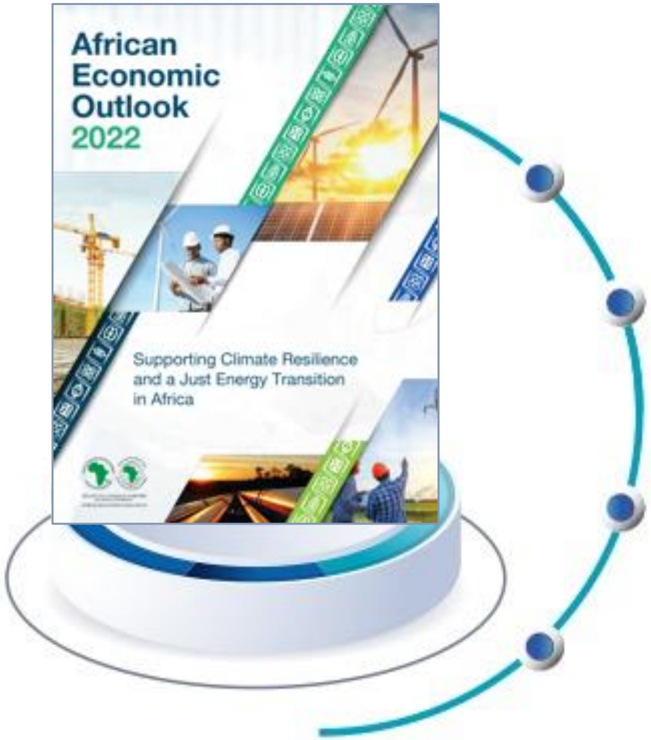
**246 million Africans go to bed hungry**,
including 59 million children under the age of 5 years old who are malnourished and stunted

### Catastrophic Loss from Disasters. Case of 2019 Cyclone Idai in 3 ADF countries, Mozambique, Malawi and Zimbabwe

- Between **800-1,000 deaths**
- About **3 million people affected**
- More than USD 2 billion worth of **Infrastructure damaged**
- More than **1 million acres of crops destroyed**
- More than **100,000 households damaged**

# Climate Finance demand in ADF Countries

## SURGING DEMAND FOR CLIMATE FINANCE IN ADF COUNTRIES




01 According to the 2022 African Economic Outlook, the climate finance needs of ADF countries amount to, on average, USD 600 billion by 2030.

02 Current resources are insufficient. Based on current trends, Africa's Nationally Determined Contributions will not be delivered. Worse still, countries may turn to exploit reserves of natural capital, often carbon-rich and biodiverse

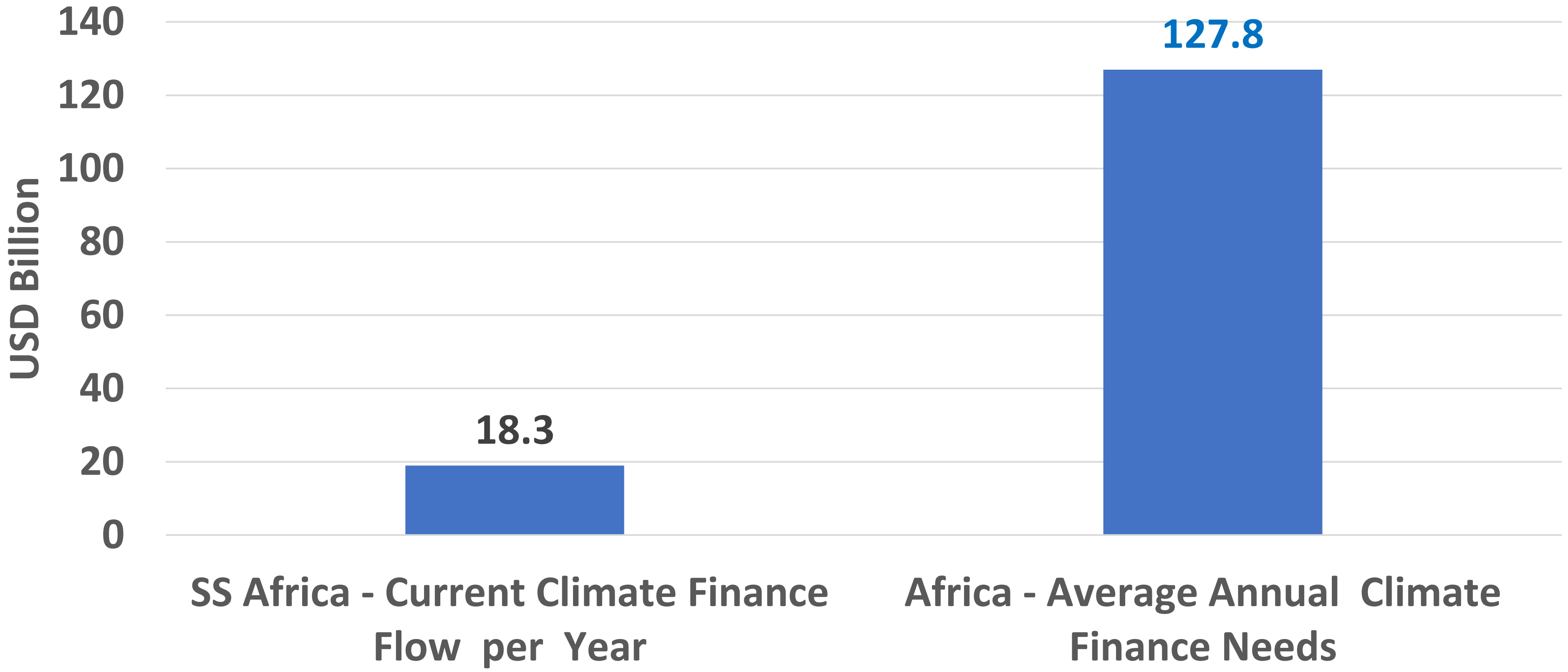
03 Sovereign debt distress is significant, with 23 African countries either in or at risk of debt distress, Climate change threatens to further undermine economic performance, reducing GDP by as much as 15% by 2050.

04 Dedicated and additional resources are needed to help ADF countries respond to the growing climate crisis.

# Low access to international climate finance

## 3% OF GLOBAL CLIMATE FINANCE FLOWS TO AFRICA

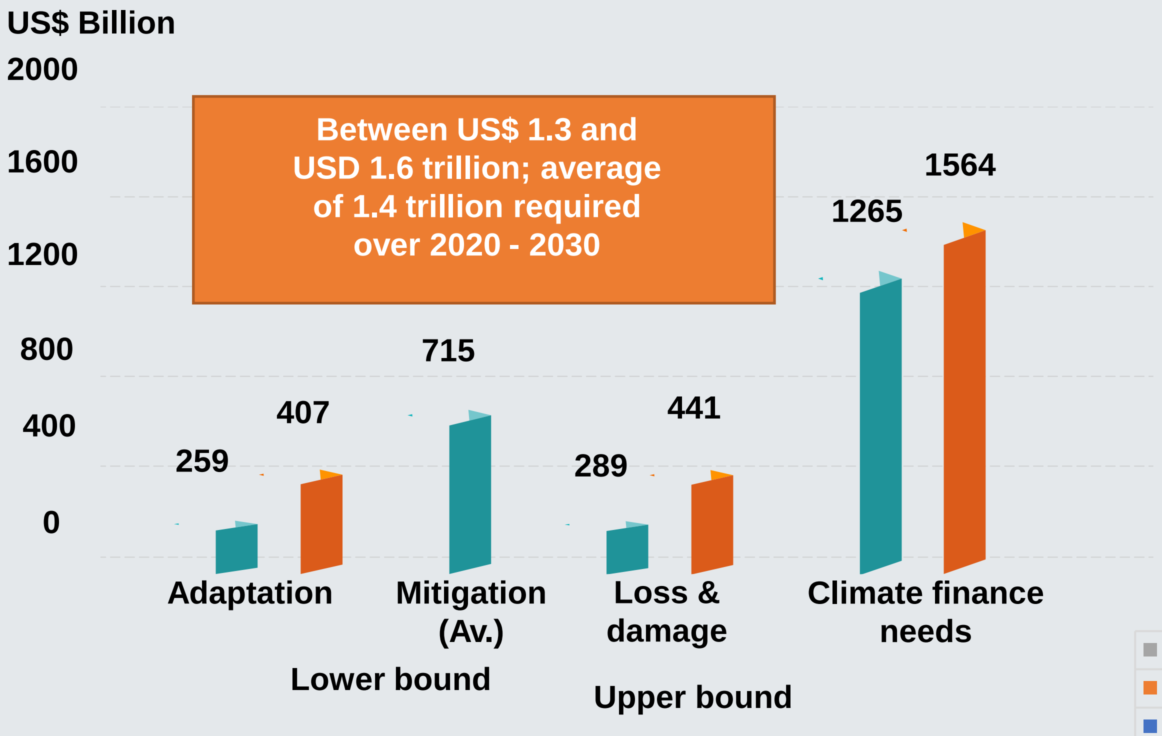
**Only 3% of global climate finance goes to Africa (USD 18.3 billion on average over 2016-2019) while climate finance needs of the continent range between USD 118.2 billion to USD 145.5 billion for the period 2020-2030.**




**Between USD 118.2 billion - USD145.5 billion is required annualy over period 2020-2030**

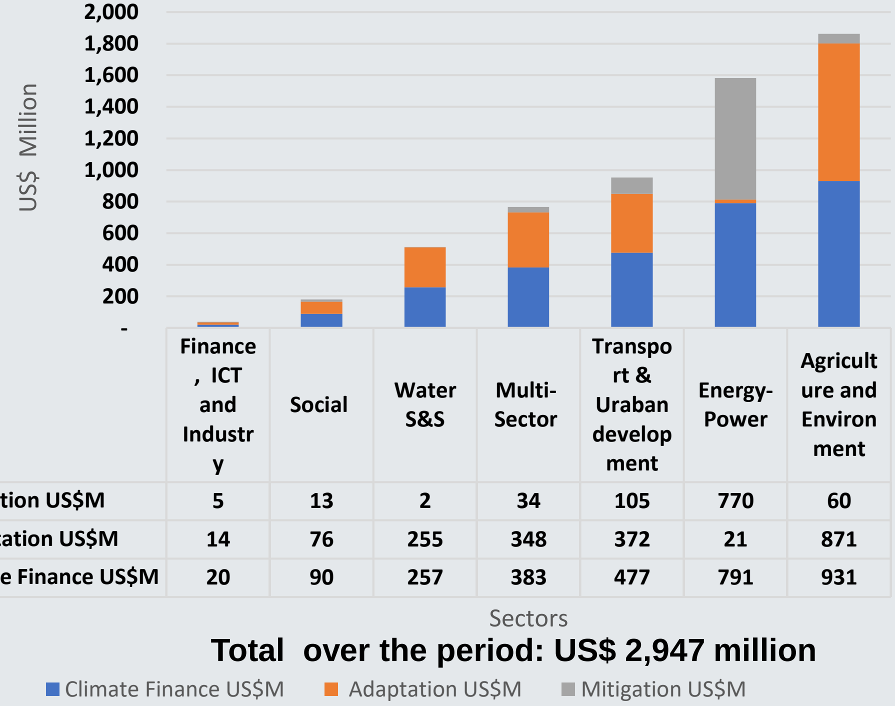
# ADF ramps up Climate Finance in Low-Income Countries

## FROM 2016 TO 2021, ADF PROVIDED USD 2.9 BILLION AS CLIMATE FINANCE. A SIGNIFICANT GAP REMAINS




African climate financing needs 2020-2030 - Need to close the gap

### ADF contribution to total climate finance disaggregated by adaptation and mitigation by sector (2016-2021)




| | Finance, ICT and Industry | Social | Water S&S | Multi-Sector | Transport & Uraban development | Energy-Power | Agriculture and Environment |
|---|---|---|---|---|---|---|---|
| Mitigation US$M | 5 | 13 | 2 | 34 | 105 | 770 | 60 |
| Adaptation US$M | 14 | 76 | 255 | 348 | 372 | 21 | 871 |
| Climate Finance US$M | 20 | 90 | 257 | 383 | 477 | 791 | 931 |

Total over the period: US$ 2,947 million

# Climate Action Window: the CAW

## STRUCTURE OF THE WINDOW

**Structured around three focal areas, and six sectors**


### Adaptation:

**Sectors**: Scale up investments in agriculture, resilient cities and rural infrastructure, water, blue economy & climate information and risk early warning.


### Mitigation:

**Sectors**: Focus on just energy transition and greening brown assets that boost access to renewable, energy, create green jobs, increase access to green finance


### Technical assistance, capacity building and policy support:

**Cross cutting:** Create enabling environment to catalyze climate action, and increase access to climate finance

**Impactful innovations by the African Development Bank are already helping to support Paris Alignment**

# Impactful innovations by the African Development Bank are already helping to support Paris Alignment

## A new blended risk transfer arrangement to support climate finance

### KEY TRANSACTION FEATURES

**Risk sharing mechanism on a USD 2 billion subset of Bank's sovereign portfolio:**

- Up to USD 400 million of first loss insurance provided by private insurers
- USD 1.6 billion of second loss guarantee provided by UK Foreign Commonwealth and Development Office (FCDO)

| | | |
|---|---|---|
| **Bank to cover its pro-rata share of the losses** | **50% exposure retained by the Bank at all times** | **AfDB remains lender of record** |

### ADDITIONAL CLIMATE FINANCE LENDING

**Scaling up Bank's commitment up to USD 2 billion towards climate finance projects over 2022-2025**

**Strengthening Africa's climate resilience**

# Scaling impactful financial Innovations…through SDR Rechanneling

"The allocation is a **significant shot in the arm for the world** and, if used wisely, **a unique opportunity to combat this unprecedented crisis**"

- ❑ Boost global liquidity
- ❑ Build confidence
- ❑ Foster the resilience and stability of the global economy
- ❑ Fund critical needs

Uneven SDR distribution across continents, countries and income groupings

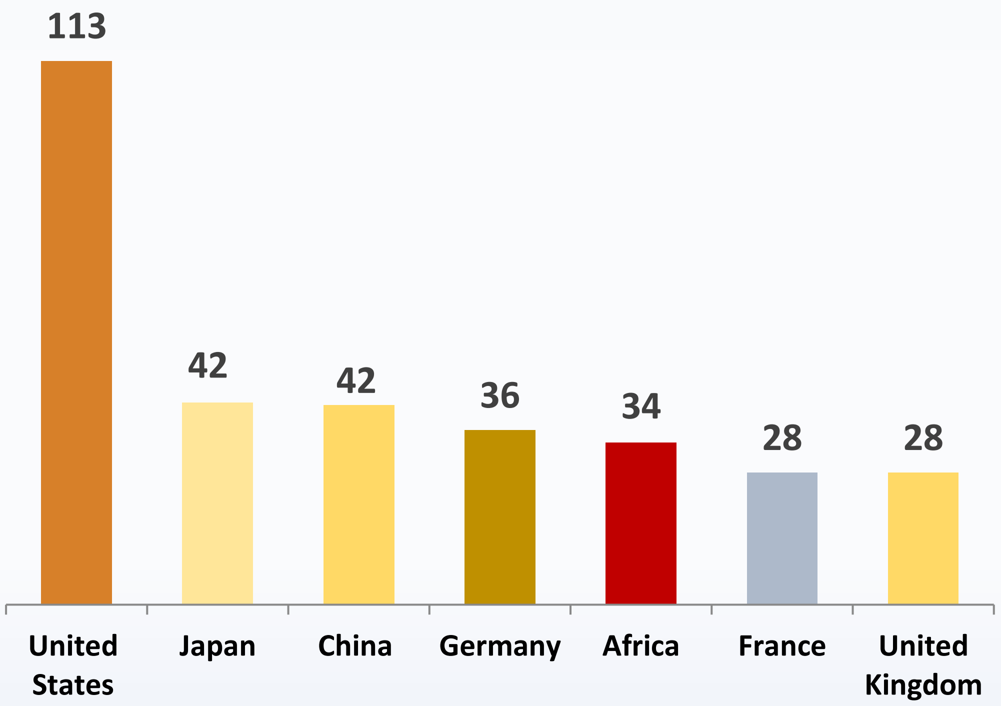
**61% allocated to developed countries**

**G7 countries received about USD 277 billion**

**39 Low-income African countries received 2.2%**

- General SDR allocation breakdown

*SDR allocation (in USD billion)*

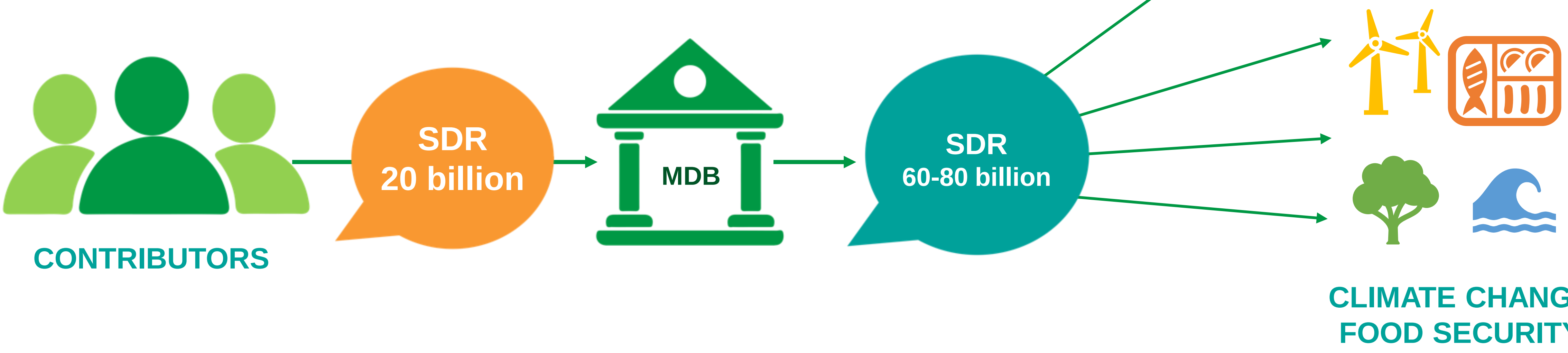



**SDR resources allocated inversely to needs**

# SDR and Hybrid Capital

**01** Shareholders invest part of their SDR allocation into a hybrid debt instrument issued by an MDB. The instrument will be treated as quasi-equity by the MDB, to increase its lending capacity.

**02** MDB uses the additional lending capacity to fund development projects in borrowing member countries via existing financing instruments. Middle-income and low-income countries eligible to borrow from each MDB will benefit from the additional lending capacity.



# Boost Lending Capacity

**Hybrid Capital supplements shareholder capital**

- 100% accounted for as equity from both accounting and rating agencies perspective
- 100% accounted for in the Bank's own internal capital adequacy metric (Risk Capital Utilization Rate)

**Leveraging sustainable hybrid capital Each 1$ invested in Hybrid Capital will fund 3$ to 4$ of additional financing for climate and social projects**

- Additional lending capacity estimated at [3-4]x
- Will contribute to supporting ESG financing on the continent

**Hybrid Capital cannot replace a GCI, it complements it**

- The purpose of Hybrid Capital is to increase the Bank's lending capacity, not replace existing mechanisms for receiving capital from shareholders
- Shareholder support unequivocally reaffirmed in 2019 following the approval of a 125% General Capital Increase (GCI-VII)

**An opportunity to provide billions of dollars in ESG financing for Africa**

# Thank you

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