

# **Policy Briefs on the Financial Crisis**

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## **Africa in the Wake of the Global Financial Crisis: Challenges Ahead and the Role of the Bank**

**African Development Bank**

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# **Africa in the Wake of the Global Financial Crisis:**

## **Challenges Ahead and the Role of the Bank**

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### **Introduction**

2010 is a critical year for Africa as the continent attempts to emerge from the crisis it did not create and to move ahead with its development agenda. It is in this context that this note is developed to: (i) assess the state and prospects of African economies; (ii) highlight the African Development Bank's response to the crisis in support of its regional member countries (RMCs), and (iii) discuss key actions needed to help Africa pull out of the crisis and achieve and sustain high long-term growth. The note especially focuses on what the Bank, in partnership with the international community, can do to help bring the continent back on a high and sustainable growth path.

### **1. Africa among the fastest growing regions before the crisis**

#### ***1.1 Rapid and broad-based growth before the crisis***

- During 2000 - 2008, Africa was among the fastest growing regions in the world (Figure 1). Prudent macroeconomic policies and reforms together with favorable external conditions, led to the region's highest growth rates during the past 30 years.
- The growth was not only high but also broad-based – 40 percent of African countries (representing about 70 percent of population) grew, on average, by 5 percent or more during 2000-08 (Figure 2).
- In terms of GDP per capita, however, Africa's growth was still below that of most other developing regions. Moreover, progress in poverty reduction has been slow, as up to 73 percent of sub-Saharan Africa's population still lived on \$2 or less in 2008 compared to 76 percent in 1990.

#### ***1.2 Improved macroeconomic stability***

- During 2000 – 08, Africa experienced a period of high growth while inflation stabilized in single digits. This was so in more than half the African countries, despite the surge in world food and fuel prices in 2007 and parts of 2008 (Figure 3). Indeed, the commodity boom combined with prudent macroeconomic policies led to improvements in macroeconomic

positions across the continent (Figure 4). Many countries also benefited from debt relief, resulting in a lower debt burden. Due to these factors, Africa was on a stronger footing than before the crisis of the early 1990s (Figure 5). In particular, the reserve buildup helped oil exporters to manage volatile revenues more effectively than in the past (Figure 6).

## **2. Africa has been hit hard by the crisis**

### ***2.1 The first round effects were limited***

Africa's rapid growth of the 2000s was interrupted abruptly in 2009 by the crisis. At the onset of the crisis, many economists underestimated its likely impact on Africa, on the premise of low integration into the global financial system. By early 2009, however, it became clear that the crisis had profound effects throughout the continent, through trade, capital flows, tourism and other real sector channels. As the crisis deepened, the key question became how to contain its longer-term impacts, and preserve the continent's recent economic achievements.

However, not all countries were immune even to the first round effects of the financial crisis. For example:

- South Africa experienced “sudden stops” of capital flows already in 2008. Its external equity and bond issuance reached about USD 20 billion in 2007 only to decline to less than USD 4 billion in 2008.
- Several countries saw their stock market indices plummet at the end of 2008 and the first quarter of 2009. For example, the indices of South Africa and Egypt suffered losses similar to other emerging market economies (EMEs), although they have been slowly recovering since the second quarter of 2009.
- Nigerian banks faced difficulties accessing trade credit lines in the United States and in Europe. In August 2009 the Central Bank of Nigeria had to inject funds into the banking system, when five leading Nigerian banks posted losses due to excessive lending to the energy sector, and the bursting of the stock market bubble.

Finally, the financial sectors of several countries suffered from the second-round effects due to the weakening of the real sector. For example, the banking sector in Ghana has suffered declining profitability and increasing non-performing assets, which reached almost 10 percent of total assets in March 2009.

### ***2.2 Delayed but deep and varied impact of the crisis***

#### ***2.2.1 Marked overall growth slowdown***

The crisis has hit the continent mostly through real channels, notably deteriorated terms-of-trade and reduced demand for exports (Figures 7a and 7b), decline in FDI, remittances, tourism (Figure 8), and possibly also aid inflows. But the financial channels also became significant, as the credit crunch on global financial markets constrained the continent's access to trade credit.

The crisis brought about a marked decline in Africa's growth in 2009. As the crisis unfolded, the 2009 growth outlook deteriorated rapidly, from a 2.8 percent forecasted by the Bank in February 2009 and 2.3 percent in May's revisions to only 2 percent according to the Bank's October forecasts (Figure 9). This growth rate implies that in 2009 Africa has recorded the first decline in real GDP per capita in a decade. The outlook for 2010 has improved, but not substantially. Because of the expected global recovery and domestic policy responses, Africa's growth is projected to reach 4.1 percent in 2010, still well below the growth rates of the pre-crisis years.

### *2.2.2 Varied growth impact*

The growth impact of the crisis has also varied across countries. While many countries have experienced sharp deteriorations in growth prospects, others have continued to record improvements. In fact, only 6 out of 51 African countries experienced a contraction in 2009 relative to 2008. This is a commendable performance when compared to OECD countries where GDP of all but two countries (Australia and South Korea) contracted.

In Africa, two groups have been heavily hit: (i) emerging and frontier markets, such as South Africa or the Seychelles; and (ii) resource-rich countries, such as Angola or Botswana. Thus, some of the countries that grew the fastest in 2008 experienced the sharpest falls in 2009. Most notably; Botswana, one of Africa's success stories, GDP fell by 7.3 percent in 2009. The key challenge for Botswana going forward is to diversify its production and export base to reduce growth volatility. Among oil exporters, Angola's growth has also collapsed from 14 percent in 2008 to stagnation in 2009, while growth in Equatorial Guinea turned from a positive 12 percent in 2008 to negative 4.1 percent in 2009. In contrast, resource-scarce, land-locked countries have weathered the global downturn relatively better (Figure 10). Similarly, GDP growth in emerging and frontier markets has slowed more rapidly than in the rest of the region, because of the relative openness of their economies.

When analyzed on the basis of income levels, upper-middle income countries contracted by 0.5 percent (un-weighted average) in 2009, driven by a contraction in output in South Africa, Botswana, and the Seychelles. Lower middle income countries<sup>1</sup> fared better, reaching growth rates of up to 3.8 percent in 2009. And due to their limited integration into the global economy and the relatively better performance in international prices of some agricultural exports such as coffee and cocoa during the crisis, the poorest countries have proven to be the most resilient and grew at 3.3 percent, with the smallest decline in growth compared to 2008. While the slowdown is less pronounced in low-income economies, it is particularly harmful given widespread poverty and the risk of policy reversals. In addition to these risks, in fragile countries, deteriorating growth prospects raise the possibility of return to higher fragility.

### *2.2.3 Widened twin deficits*

As a result of the crisis, Africa has lost about 30 – 50 percent of its 2008 export revenues in 2009. Despite some relief on import bills due to falling food and oil prices, the overall trade balance deteriorated markedly (Figure 11).

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<sup>1</sup> With GDP per capita between \$ 786 and \$ 3115

Overall, the continent has moved from a *current account* surplus of 3.4 percent of GDP in 2008 to a deficit of 4.2 percent in 2009. Again, there were substantial disparities across countries and country groups. Oil exporters recorded a deficit of 1.4 percent of GDP in 2009, which is a major deterioration from a surplus of 11 percent in 2008. In a similar vein, exports of several oil importers have also collapsed due to the contraction of demand in advanced economies.

The decline in export revenues, reduced remittances and, in a few instances, aid, put pressures on *exchange rates*, with currencies of many African countries depreciating relative to the dollar. The message here is clear: unless sufficient FDI and aid are available to cover the external deficits stemming from the crisis, Africa's foreign reserves, which took years to accumulate, may deteriorate rapidly. For example, Angola's official reserves are projected to decrease from 15 months of imports in 2008 to 9 months in 2010. Similarly in Chad, reserves are projected to fall by half from 4 months of imports in 2008 to 2 months in 2010, while Ghana's reserves have reached precariously low levels of about 2 months of imports for the past 12 months.

Similarly, the continent's *fiscal balance* is also projected to worsen, as a surplus of 3.3 percent of GDP in 2008 turns into a deficit of 4.2 percent of GDP in 2009. Fiscal space has been particularly affected through two channels: (i) directly through revenue losses, and (ii) indirectly through automatic stabilizers associated with slower economic activity. Commodity-related revenues have been affected the most, with the fiscal balance in oil exporting countries turning into a deficit of 5.4 percent of GDP in 2009, from a surplus of 6.6 percent in 2008. Oil-importing countries also experienced an increase of the fiscal deficit from 1.3 percent of GDP in 2008 to about 2.7 percent in 2009.

#### *2.2.4 Social consequences*

The world over, the crisis is now turning into an unemployment crisis, raising serious concerns. In Africa, unemployment is estimated to have increased by more than 10 percent between 2008 and 2009. Moreover, the ILO projects that the number of the working poor and vulnerable employment (workers without formal arrangement) could reach unprecedented levels. The number of working poor in Africa could rise by a staggering 35 million people and vulnerable employment by 31 million people during 2007 – 2010.

#### *2.2.5 Regional differences – East Africa faring relatively better*

The growth impact of the crisis has varied also across countries and regions. In relative terms, East Africa has fared better, with a real GDP growth of 4.5 percent in 2009 (Figure 12). While inflation was in double digits in 2008, it is expected to decline significantly in 2010. The sub-region is also in a better shape than others in terms of fiscal and current account positions. For East Africa, especially Kenya, Uganda and Tanzania, to have weathered the crisis better, two factors seem to have played a decisive role: (i) greater regional integration, combined with lower

dependence on the global economy, and (ii) timely and effective stimulus packages, which were made possible thanks to the pre-crisis prudent macroeconomic policies.

### ***2.3 Second wave of the impact of the crisis: The case of the Dubai Debt Crisis***

The fear of the second wave of the crisis came to the surface on November 25, 2009 when the Dubai's flagship company Dubai World announced its intention to postpone debt service payments for 6 months, until the company is restructured. While the scale of Dubai's debts is comparatively modest at \$80 billion, the surrounding uncertainty led financial markets across the world to react very negatively. Africa escaped largely unscathed even though the Dubai World group has significant holdings across the continent, including tourist properties in South Africa, Comoros, Zanzibar, Djibouti and Rwanda. Fortunately, restructuring plans do not include these and other financially stable properties of the group such as the Dubai Ports World, which runs facilities in Senegal, Algeria and Djibouti.

Of course, not all countries were immune. North African markets were most hit, as investors from the Gulf Cooperation Council countries had expanded heavily into other Arabic-speaking markets. Subsequently, a weakened investor sentiment towards the Middle East affects the Maghreb countries, with Egypt and Morocco being particularly affected. While other countries in the continent fared better, there were concerns that the debt crisis would lower investors' appetite for emerging market investments. This would be damaging for countries such as Angola, Senegal and Kenya, which plan to raise finance on the international capital markets in 2010.

## **3. African countries responded decisively, but prudently to the crisis**

### ***3.1 A broad range of domestic policy responses to the crisis***

As in other regions, Africa adopted several instruments to minimize the impacts of the crisis, including fiscal stimulus packages, easing of monetary policy, targeted sectoral assistance, capital and exchange controls, and new regulations in the banking sector. In addition, many countries were able to draw on their reserves to cushion the shock (e.g., South Africa, Tunisia, and Morocco). South Africa set aside \$100 billion for public investment for 2010 – 2012; Kenya issued its first public infrastructure bond; Uganda, Kenya and Tanzania raised public expenditure on infrastructure by 20–30% in their 2009/2010 budgets to enhance economic growth; Tunisia increased public investments by 20% in 2009 to compensate for 35% decrease in FDI; Morocco is expected to do similarly for 2010; Botswana received \$1.5 billion from the AfDB to sustain support to the private sector through infrastructure development.

Not all African countries, however, were in a position to implement expansionary policies. Ghana could not afford a stimulus package due to limited policy space, with twin deficits of 10% of GDP each for the fiscal and current account, both after grants, and about 15% inflation.

### ***3.2 Stimulus policies need to be carefully selected and globally coordinated***

Despite the positive steps taken in a number of economies, it is clear that African countries do not have adequate domestic resources to fully offset the impacts of the crisis. While reforms aimed at increasing domestic resource mobilization are high on the policy agenda, the results are likely to take time to materialize. This has left the majority of African countries with limited options to adopt discretionary counter-cyclical fiscal measures. Moreover, even in countries where expansionary policies are feasible, the question remains as to whether low income countries should spend the reserves accumulated during the boom to mitigate a crisis that is not of their making.

But, even countries that have the space to adopt fiscal stimulus need to do so cautiously. Past evidence from emerging countries indicates that while the effects of a fiscal stimulus tend to be positive, they remain modest, especially for small open (import dependent) economies. Effective fiscal stimulus packages must contain discretionary measures that are timely, targeted, and temporary (with clear exit options).

In this context, it is reassuring to note that the measures adopted by our countries were generally timely and well targeted. While some measures stimulated domestic demand (offset declining exports), many strived to ease the supply bottlenecks and support businesses as well. As most of the measures are temporary, they are not expected to interfere with the medium term fiscal targets.

Africa's domestic measures need to be well coordinated with policies at the international level given that global economic recovery is a prerequisite for the continent's own recovery from the crisis. Moreover, there is a need for clear commitment by developed countries to refrain from any protectionist inclinations and ensure that their demand for imports from Africa picks up.

## **4. Preventing a development crisis and restoring high growth after the crisis**

### ***4.1 Recovery in Africa could be delayed***

While there are early signs of global recovery, “green shots”, it is still too early to celebrate a genuine recovery. For Africa the real question is whether and when it will return to a high and sustainable growth path. A sluggish world recovery, coupled with potential waning of popular support for reforms at home – a possible side effect of the global crisis – could jeopardize the continent's longer term growth potential. Moreover, during growth decelerations, such as the one that Africa is experiencing now, some of the fundamentals of the economy may be eroded, including the quality of institutions, foreign direct investment inflows, savings and human capital, with possible long-term consequences for growth.

The losses listed above could lead to a much lower growth trajectory in post-recovery period, possibly causing perhaps permanent hindrance to some countries' future development. If this scenario prevailed and the key drivers of growth are hampered, the global financial and economic crisis could degenerate into a development crisis. To prevent this scenario, Africa needs to forge ahead with reforms to address structural and institutional bottlenecks. In addition, the actions of African countries need to be coordinated with and supplemented by those of developed countries, including adequate commitments and timely delivery of financial aid and technical assistance as well as measures to insure adequate market access for African products.

#### ***4.2 Structural reforms to restore Africa's economic potential***

While Africa's macroeconomic achievements prior to the crisis have been impressive, progress with structural reforms has been mixed. Although the continent is becoming more open to trade and FDI, structural transformation, and in particular industrialization, remains limited. Moreover, the continent continues to suffer from weaknesses in infrastructure and institutions, including the business environment (Figures 13 and 14).

African countries could turn the crisis into an opportunity to restore their economic potentials and bring their economies on high growth paths. This requires a focus on key structural reforms such as enhancing competition in the financial sector, streamlining labor market regulations, developing financial markets and strengthening governance, promoting private sector development and promoting economic diversification. These reforms need to be accompanied by measures to establish social safety nets for the most vulnerable segments of the population.

Encouraging private sector development to spur investment is one of the key medium term challenges, which would also provide a base for a more diversified growth in the coming years. Improvements in the business environment, including enforcement of property rights and good governance, are important for raising competitiveness. Moreover, private sector development requires adequate access to capital. Hence, securities exchanges, venture capital or other forms of long-term financing need to be further developed.

Countries with more developed financial sectors and a high share of foreign ownership have taken steps to protect domestic banks from the impact of the financial crisis. As in other emerging market economies, cooperation in the areas of financial supervision and crisis prevention between foreign parent banks and domestic branches are critically important in Africa. Greater financial literacy of all market participants, especially awareness of the risks associated with various forms of loans (including in foreign currency and/or at variable rates), also needs to be promoted.

#### ***4.3 Substantial financial needs***

Africa was an innocent victim of the crisis. To prevent the crisis from derailing the continent from its high growth trajectory and to preserve poverty reduction gains, substantial external financial resources are required. It is estimated that the continent would need about \$50 billion

per year of additional financing to achieve the GDP growth rates needed to achieve MDG Goal 1 of halving poverty by 2015. The infrastructure gap for the continent is estimated at between \$50 billion and \$100 billion.

While financial needs to mitigate the economic and social consequences of the crisis are substantial, they must be met. Africa cannot be left alone, or viewed as the last priority, when it comes to dealing with a crisis which originated elsewhere in the developed world. Of course, higher financial assistance and other support will be challenging to mobilize in times of economic stress in donor countries. But the returns to helping Africa weather the storm are equally very high, given the growth potential and the increased management capacity demonstrated by African governments over the past years.

The fact that Africa has been faced with a tremendous setback as a result of a crisis it did not create has been widely recognized at the highest decision-making levels of the international community. Moreover, helping Africa to overcome challenges posed by the crisis is not only a moral imperative for the advanced countries, but it is also consistent with their longer-term interests in ensuring a stable and prosperous global economy. Hence the solution to Africa's challenges posed by the crisis must be all encompassing, should rely on enhanced and more inclusive international cooperation, and Africa needs to be a key part of this global solution. And this is where the African Development Bank can play a key role.

## **5. The Role of the African Development Bank**

### ***5.1 Shaping Bank Responses – Partnerships and Enhanced Policy Dialogue***

At the onset of the crisis, the Bank used its convening power, in collaboration with the Economic Commission for Africa, the African Union Commission, and the NEPAD Chairman, to facilitate the debate on appropriate policy responses and mobilize the calls for international support to the continent. Thus, a conference of African Ministers of Finance was organized in November 2008. The Committee of Ten Ministers of Finance and Central Bank Governors (Committee of Ten) was then created to provide guidance on policy responses to the crisis. The Bank's knowledge products provided analytical underpinning of discussions and policy options in the wake of the crisis. Together with its partners, the Bank has played a key role in providing input into Africa's position at the G20. As a continent, Africa was able to speak with one voice and the global community has taken the Bank's views very seriously; this has transpired in the G20 Declarations and global pledges for new funding.

But important concerns still remain. In spite of the large amounts of resources mobilized through the G20 processes, little of these new resources will be channeled to African countries. Moreover, the bulk of the new resources availed to the IMF are short-term and are thus not tailored to the specific needs of the continent which are of a structural nature. The continent needs financing to alleviate supply-side constraints – especially infrastructure – and support trade. This will require new long-term predictable funding; such funds have not been forthcoming in the G20 process.

Another important unresolved issue is that the April G20 summit made no commitment to further changes to the IMF quota system, leaving Africa's voice marginalized in a key international financial institution. The proposed solutions to weaknesses of the governance of these institutions largely fall short of the continent's needs, and hence further actions are needed to make the global financial architecture work for all.

The Bank has done its best to support the continent by both leveraging its own resources and consolidating partnerships. The Bank has demonstrated speed and flexibility in response to the 2008-2009 food, energy and financial crises, through front-loading of resources, provision of additional resources to budget support operations, introduction of a trade facility, and portfolio restructuring in order to unlock additional resources. More specifically, so far the Bank's effectiveness in dealing with the crisis can be ascribed to four important factors: (i) The Bank fully exercised its convening and honest broker roles to galvanize both African and international opinion in addressing the crisis; (ii) Internally, the Bank advocated a flexible response to the crisis, comprising frontloading of resources and restructuring projects to deliver resources where most wanted; (iii) The Bank was willing to partner with others in addressing the crisis. A number of initiatives were co-financed with other donors, such as the Global Trade Liquidity Program (GTLP) administered by the IFC to ensure that trade finance continues to flow to Africa; and (iv) The Bank revamped its analytical work and knowledge services to cater for the specific needs of its Regional Member Countries during the crisis. Going forward, the Bank could be even more effective in assisting the member countries if its financial base was adequately strengthened in response to additional needs created by the crisis. This point is further developed later.

## ***5.2 The Bank's Preparedness and Capacity***

Notwithstanding the hurdles, the African Development Bank has quickly gained a track record of effectiveness in its response to the crisis. When the food and oil crisis hit the continent a couple of years ago, the Bank responded quickly and flexibly. The Bank was able to draw on the lessons from this experience in responding to the current crisis, even in the absence of readily available crisis response instruments and limited resources. Existing resources were front-loaded, our portfolio restructured, and the processing time shortened. The Emergency Liquidity Facility, established to help inject liquidity into our economies as global liquidity dried up, has proven to be timely, though inadequate given the rising demand from RMCs. Moreover, to address market constraints related to the crisis, and in particular the trade finance shortage, the Bank established a multiphase US\$1bn Trade Finance Initiative in early 2009. The Bank has both provided financing and played a catalytic role in mobilizing financing from sister organizations and private financial institutions, which has been a major boost to trade and investment in our RMCs.

## ***5.3 Increasing Private Sector Operations***

Private Sector Operations are increasingly gaining momentum. The 2008-10 business plan projected the volume of approved operations to rise from UA 700 million in 2008 to UA 850 million in 2009, and reaching UA 1 billion in 2010. However, in response to the global financial crisis, the Board approved UA 882 million of new operations by the end of July 2009. This

represents 104% of the full-year target. Of this amount, UA 388 million was for trade finance and UA 65 million for emergency liquidity operations, both of them being fast disbursing and more flexible instruments. Overall by end 2009, approvals for new lending and investment operations and new technical assistance (TA) grants amounted to UA 1.2 billion, well above the pre-crisis target.

Private sector operations (PSO) with financial institutions represented 53% of new approvals followed by infrastructure (25%) and industries and services (22%). This concentration of operations towards financial institutions reflects the short-term impact of the financial crisis, and the need to respond to the difficulties faced by private sector operators in accessing international credit.

Given the Bank's development focus, approved operations in 2009 were dominated by regional operations and projects in low income countries (LICs). As a result, operations in LICs account for 70% the portfolio (including the share of regional and multi-country operations targeting low-income countries).

Consistent with the scaling up of PSO and enhanced confidence in the Bank, non-regional members have pledged to contribute additional resources: Japan, a USD 30 million grant for FAPA2 (Technical Assistance Fund); France, EUR 11 million to develop programs for remittances; Spain, EUR 15 million over 3 years for microfinance; Denmark, EUR 67 million towards an African Guarantee Fund for SMEs, and EUR 40 million towards a renewable energy program, from 2010 to 2014. In addition, Canada provided resources to launch the African Finance Partnership (AFP), Finland sponsored a senior advisor for private sector development and the Netherlands provided funding for PPP specialists.

Apart from scaling up its private sector operations, the Bank is increasingly assuming a leading role among the group of lenders to the continent, especially in the area of telecommunication and public-private partnership, such as the Main One submarine telecommunications cable, the Tunisia Enfidah Airport, the Dakar-Diamniado Toll Road Project, the N'Diass highway in Senegal, and the Gibe hydropower project in Ethiopia. Public-private partnerships in agriculture are also being developed and linked to operations in the financial sector to promote small and medium enterprises.

#### ***5.4 Public Sector Investments Scaled Up***

In addition to the increased private sector operations and emergency assistance in response to the crisis, public sectors operations were also scaled up. By the end of 2009, the Bank financed over UA6 billion worth of public sector projects, with UA 4.3 billion going to middle income countries. This is over 300 percent of the earlier projection of UA 1.34 billion. On the other hand, the ADF delivered UA 1.8 billion during 2009, characterized by substantial frontloading of resources to countries.

The Bank's response to the financial crisis continued to be guided by its Medium Term Strategy for both the ADB and ADF windows. Lending for infrastructure comprised 58.6 percent (or UA

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<sup>2</sup> Fund for African Private Sector Assistance

3.791 billion) of total public sector financing, while that for programmatic operations, including budget support and governance operations, comprised 35.3 percent (or UA 2.286 billion). The latter includes the substantial lending to Botswana during the year. The recently approved budget for 2010-2012 projects that this sector thrust will be maintained during 2010.

Similarly, in spite of the increased demands from RMCs, the subsequent innovations and greater flexibility of Bank instruments, its emphasis on selectivity was central in maintaining focus on its mandate. The increase in human resources and improved internal processes also helped in ensuring expeditious delivery of the Bank's services. However, further reforms and innovations will be undertaken to ensure that the recent gains are sustained.

### ***5.5 Enhanced Organizational Capacity and Efficiency***

Even with its commitment to play a countercyclical role, the Bank's interventions have remained aligned with its strategic focus to finance longer-term development. The Bank's interventions have been in line with its strategic orientation and drew on the four pillars of its Medium-Term Strategy 2008-2012: (i) infrastructure; (ii) private sector development; (iii) governance; and (iv) higher education.

In this process, the Bank Group has continued to reinforce its capacity to efficiently manage the increasing volumes and instruments of development assistance, with the aim of maintaining the highest standards of corporate governance and integrity in executing its mandate. Despite the difficult economic circumstances in 2009, all three windows of the Bank Group (the ADB, ADF and NTF) are expected to continue the trend of positive earnings. Such positive earnings reflect not only the efficiency in the conduct of the core operations of the Bank Group, but also the positive effects on the Bank Group's treasury activities of the recovery in the financial markets.

The Bank also continues to enjoy the highest ratings from all the major rating agencies, thanks in large part to the continued strong support of Regional and Non-regional Member Countries, and to the prudent and proactive financial and risk management policies and practices employed by the Bank Group. As a result of such excellent credit rating, the Bank has been able to raise funds in the capital markets at very attractive rates, despite the significant upheavals in the financial markets over the past 18 months. In 2009, the Bank raised over UA 4.8 billion (over USD 7.5 billion equivalent) from the capital markets at a weighted average cost of approximately 6 month LIBOR flat. At a time when the world's financial system was under unprecedented stress, the ability to leverage its AAA credit rating and borrow money at attractive rates, combined with a strong level of capitalization at the beginning of the year, have enabled the Bank to significantly scale up its development assistance activities and play its countercyclical role in the continent.

Indeed, the Bank is aware of the need to continuously adapt to the dynamic environment. In this regard, an enterprise-wide review of the Bank Group's risk management framework and processes is underway, with a view to formulating recommendations for further improvements. The outcome of the review will be reported to the Board of Governors in due course.

The year 2009 has seen further consolidation in the Bank's efforts to get closer to RMCs, which has improved client focus and awareness through decentralization. A total of 25 offices were

operational at December 31 2009, compared to 22 at the end of 2008. More importantly, the number of staff in the field offices is on the rise, in line with the Bank's goal to increase visibility and capacity on the ground. The increased decentralization is being accompanied with increased attention to internal controls and improved communication and coordination mechanisms.

Improving human resources capacity has been a key dimension of the internal reforms in the Bank. Accordingly the Bank is implementing its Human Resources Strategy, which focuses on (i) the recruitment and deployment of high-calibre staff to operations and country/regional offices and (ii) a more competitive and rationalized staff Compensation and Benefits Framework to ensure that we attract and retain highly qualified staff.

Improved Technology in Support of Bank's Operations is also key to streamlining work flows, equipping staff with the necessary tools for efficient delivery and effective communication within the Bank, and between the Bank and its stakeholders. The plan includes an already completed Broadband Integrated Telecommunication Services that has improved the reliability and throughput of telecommunications. Finally, an upgrade of the Bank's Enterprise Resource Planning platform (SAP) has recently been initiated. This comprehensive upgrade is expected to not only help further streamline transaction processing but also enhance reporting and related decision-support tools given an increase in the volume of the Bank's operations.

#### ***5.6 A call for scaling up the Bank's resource envelope***

The decline in export revenues and capital inflows has created large and growing financing needs in Bank's RMCs. As a result, the Bank has seen a drastic increase in the demand for its resources. Specifically, while demand for Bank lending for 2009 was estimated at UA 5 billion before the crisis; it has increased to UA 8 billion. The Bank's discussions with regional members also indicate a sharp increase in demand for Bank resources to about UA 8 billion per year during 2010 and 2011. This increased demand reflects the worsening of the financing gap for pre-existing deficits, notably in energy and infrastructure and especially power and transport. The new demand brings the Bank close to its maximum lending capacity, and the Bank will soon exhaust its lending envelope and additional resources need to be secured so the Bank can continue to assist effectively its members in these challenging times.

The demand for the Bank lending is projected to remain high in the medium to long term due to a combination of two important factors. First, while the continent was recording growth acceleration before the crisis, the rates of growth were insufficient to make adequate progress towards reaching the MDGs. The continent still faced structural financing gaps, notably in the areas of infrastructure. These financing gaps have only been exacerbated by the crisis, and will need to be met even after the recovery. Second, the Bank has established itself as a partner of choice for RMCs, including middle income countries that traditionally borrowed from international markets. For example, in the 3rd quarter of 2009 the African Development Bank was the biggest lender in Africa, followed by the European Investment Bank and the World Bank among ADB countries. The RMCs' limited access to capital markets and their heightened confidence in the Bank as the lender of choice imply higher demand for Bank's resources. At the same time, RMCs have substantially improved their macroeconomic management capacity as well as transparency, and hence are able to absorb higher levels of external resource inflows.

For these reasons, the Bank will need to operate at systematically higher levels than before the crisis. This will not be possible without a major scaling up of its resource envelope. The Bank is therefore appealing to its members to increase its resources through a General Capital Increase and the replenishment of the ADF.

## **Conclusion**

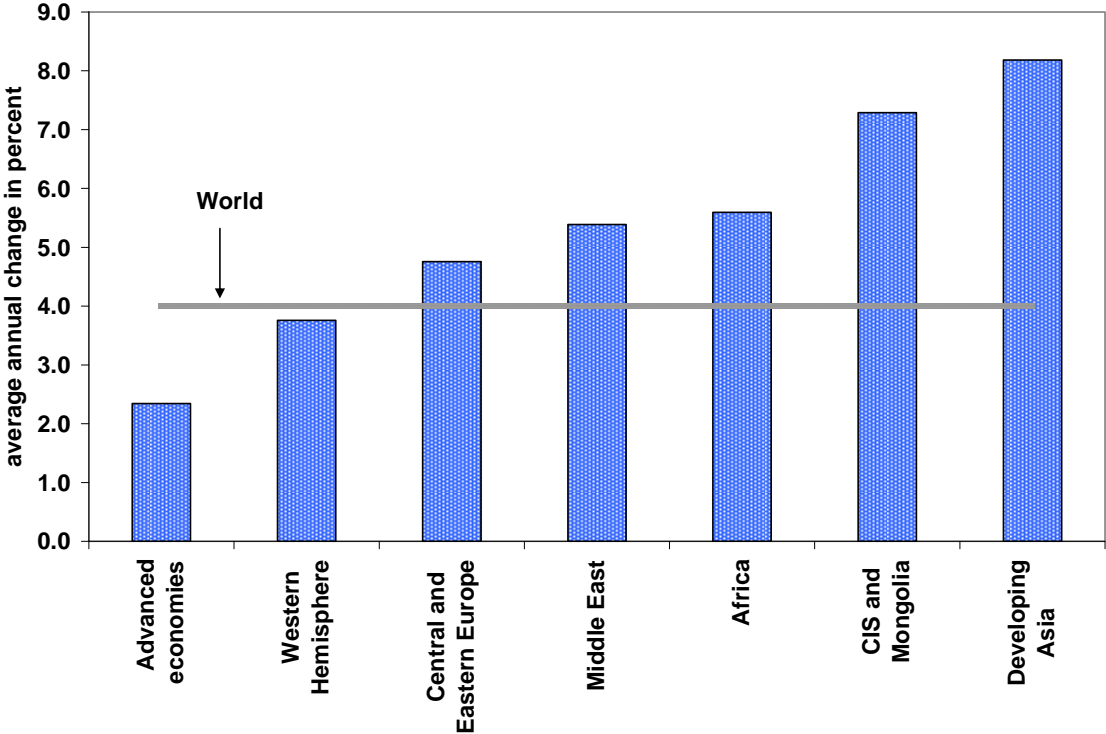
In spite of the tremendous challenges of 2009, the Bank has concluded the year with resounding success. Given the immensity of its challenges, the crisis emerged with hard questions about the Bank's capacity as Africa's premier development institution and its preparedness to lead Africa's development path through turbulent periods such as the one just behind us. With what the Bank has been able to achieve this year, it has fully demonstrated its potential to deliver and lead, even under critical emergency situations.

The already substantial development needs of Africa have increased further due to the recent global financial and economic crisis, as reflected in the recent significant increase in demand for financing from the Bank. Even prior to the crisis, the Bank had raised its profile among its members through dialogue, increased lending and non-lending activities, and an efficient and speedy response to their needs. The effective way in which the Bank has handled the crisis so far only solidifies its role as a partner of choice for RMCs. At the same time, the increased demand for Bank's resources has led to their faster utilization than earlier anticipated. In order for the Bank to maintain its current and projected level of activity beyond 2010, there is an immediate and urgent need for additional funding in the form of a General Capital Increase.

While the remaining challenges facing Africa are still very numerous, the continent can surmount them all. But this will only be possible with continued support of the Bank and other development partners and the collective efforts of the entire international community.

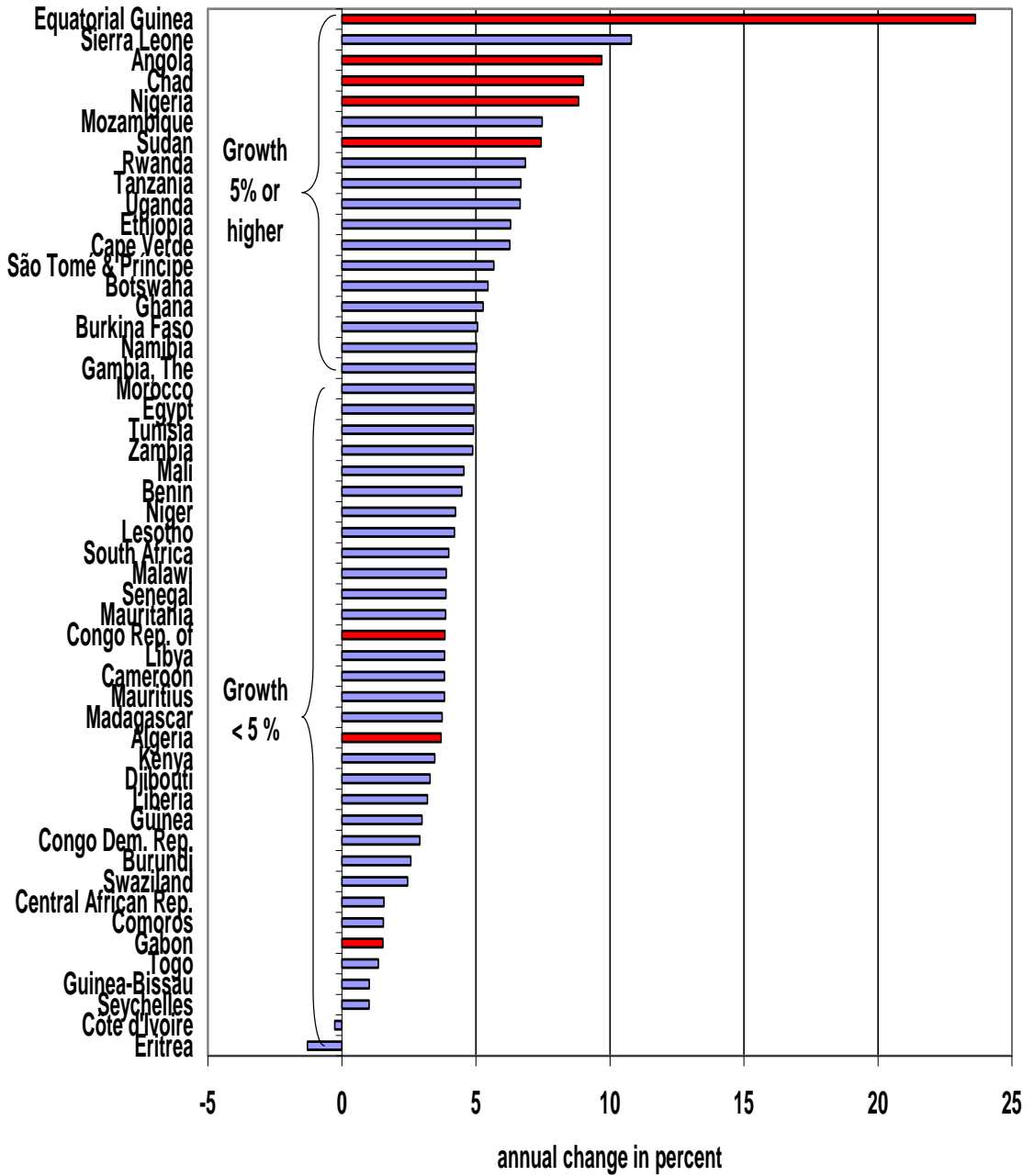
**FIGURES**

**Figure 1.** Growth of real GDP by regions, 2000 – 2008



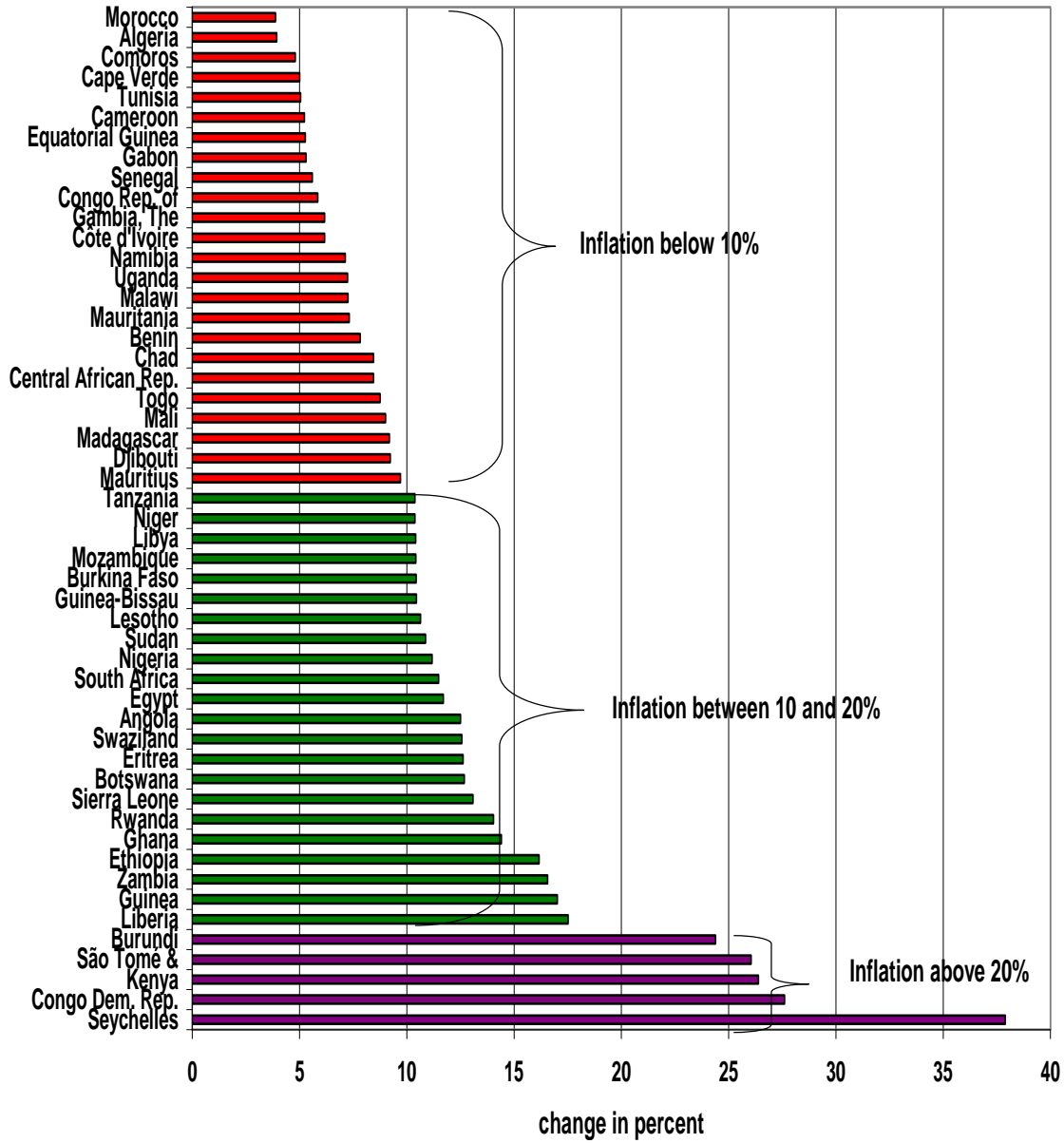
Source: IMF WEO database (October 2009).

**Figure 2.** Average annual growth during 2000 – 2008, by country (in percent) 1/



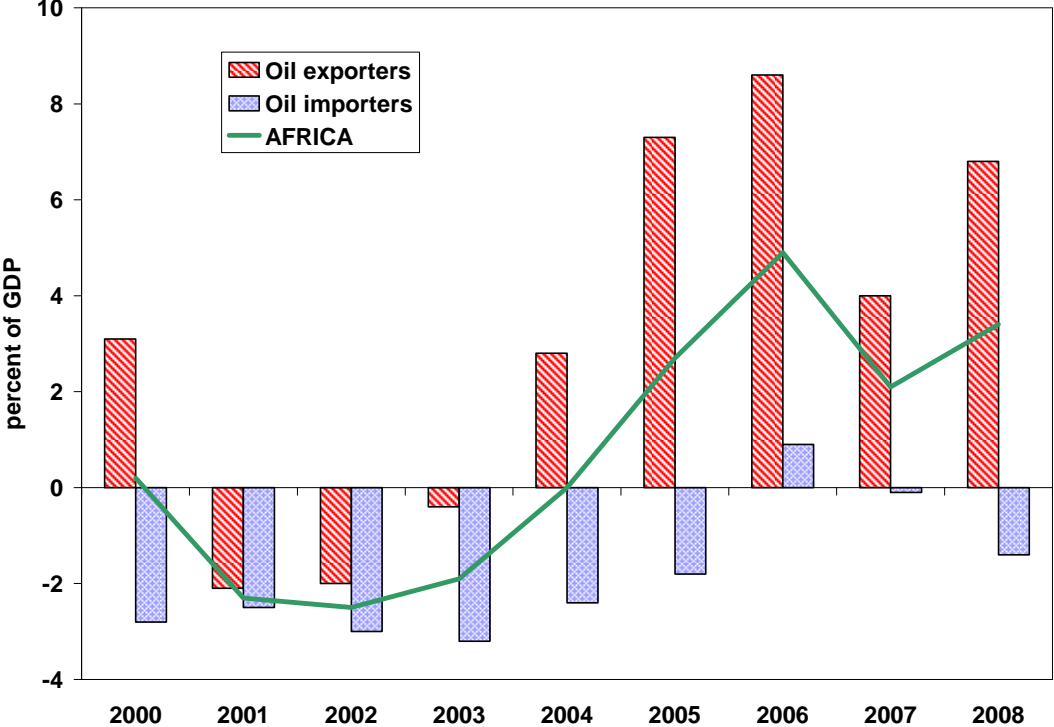
**Source:** African Economic Outlook database (October 2009). 1/ Oil exporters are in red. Excludes Zimbabwe and Somalia.

**Figure 3.** Inflation in 2008, by country 1/



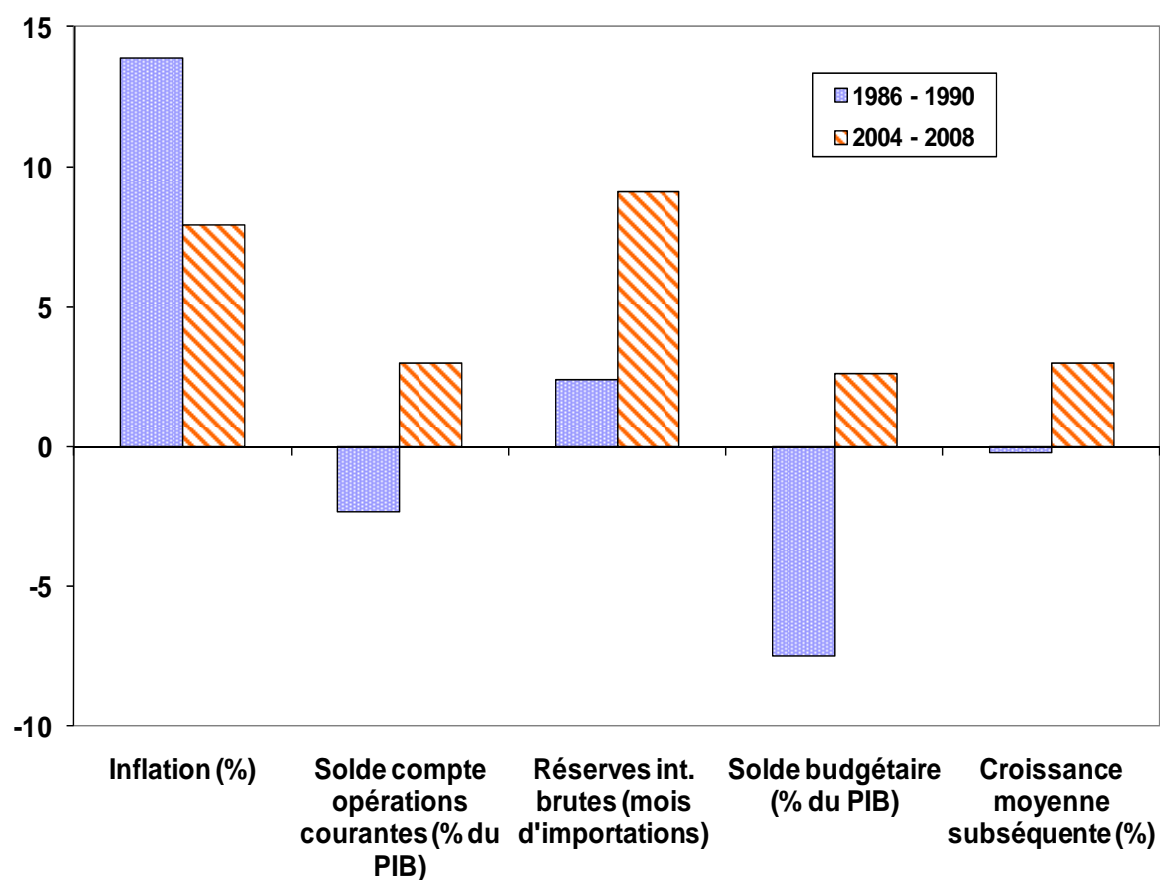
**Source:** African Economic Outlook Database. 1/ Excludes Zimbabwe and Somalia.

**Figure 4.** Fiscal balances (including grants) in Africa, by sub-groups, 2000 - 2008



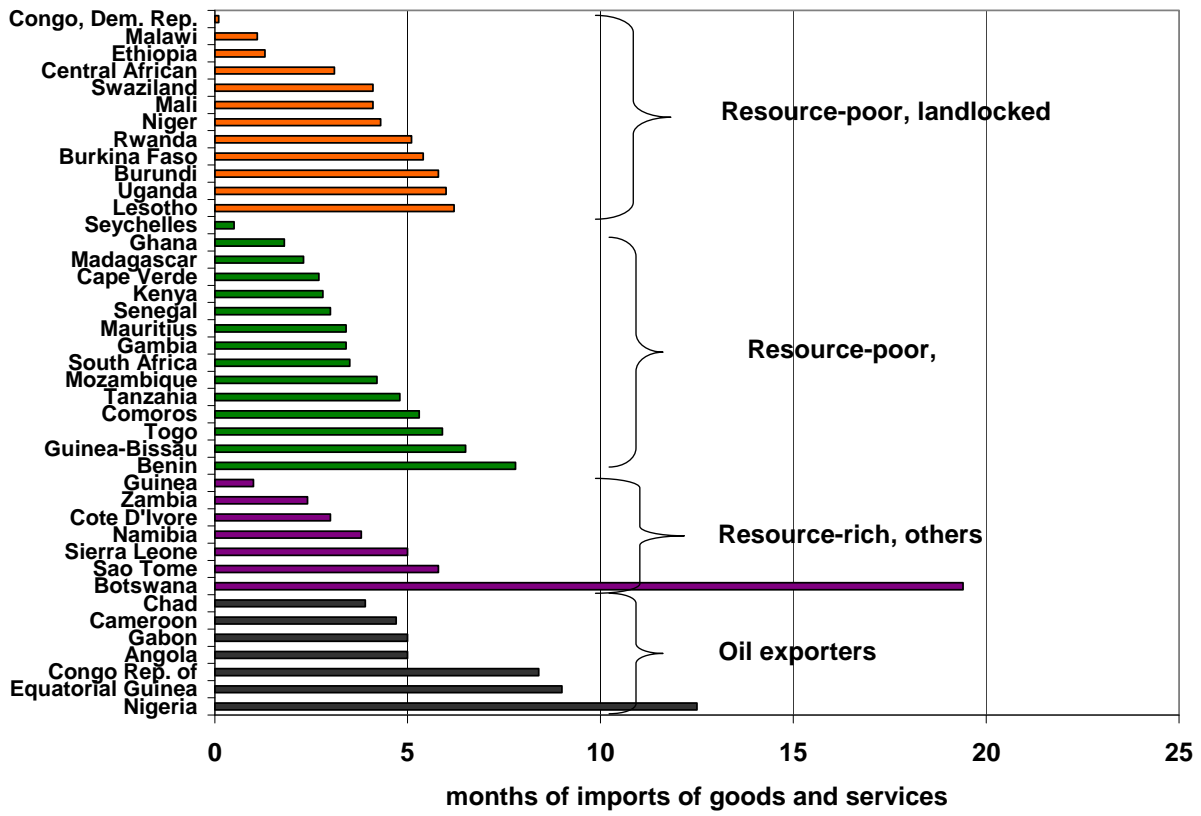
Source: African Economic Outlook database.

**Figure 5.** Africa's macroeconomic indicators before the two latest crises



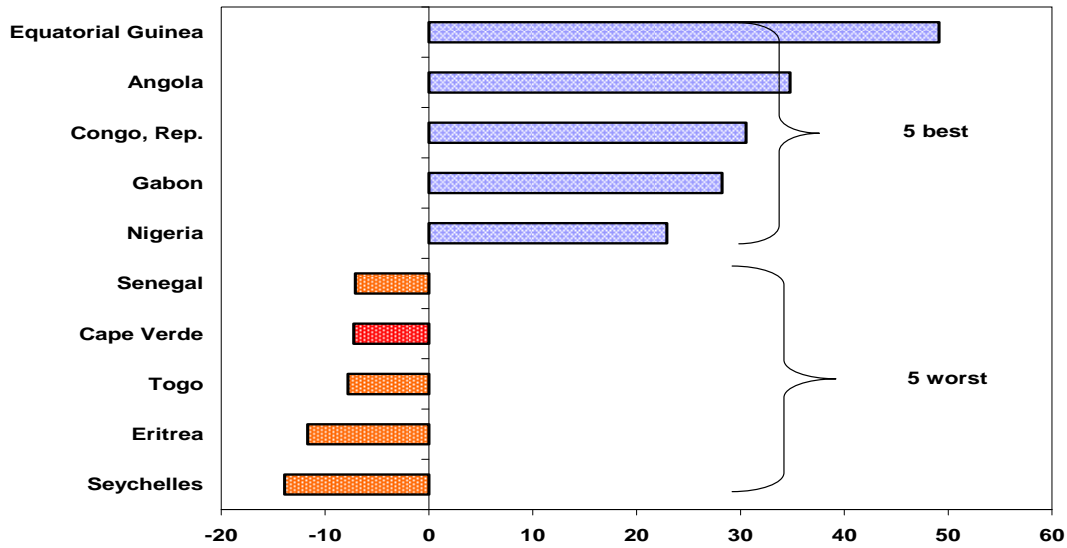
**Source:** African Economic Outlook database (October 2009). 1/ Fiscal and current account balances include grants. 2/ Average of actual growth rates in 1991 and 1992 for the first recession and of forecasted growth rates for 2009 and 2010 for the second recession.

**Figure 6. Reserve coverage of imports of goods and services, 2008**

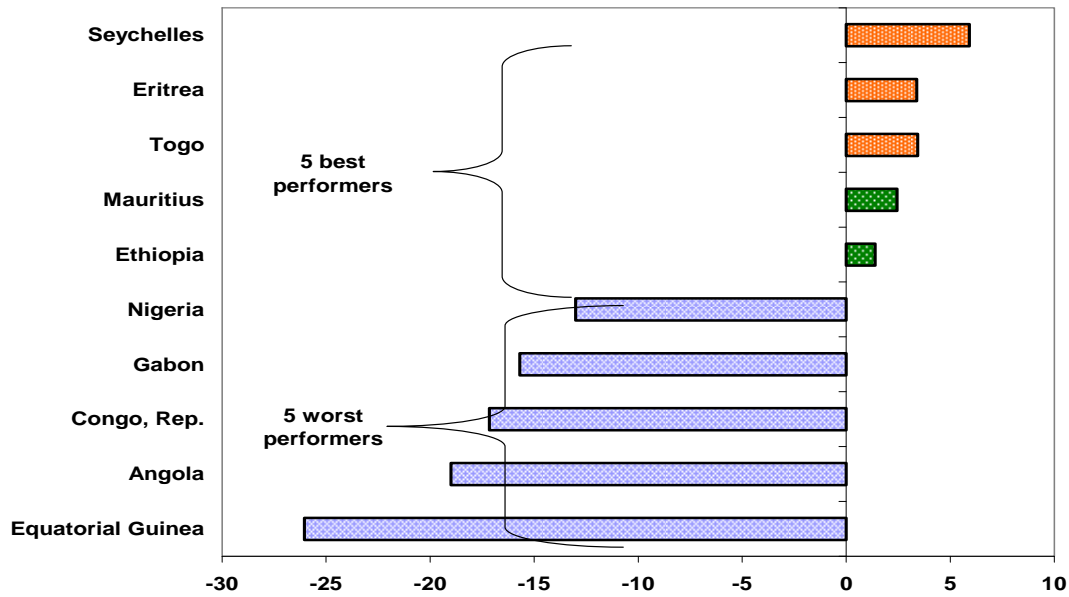


Source: IMF Regional Outlook for sub-Saharan Africa.

**Figure 7a. Change in 2008 trade balance as % of 2006 GDP**

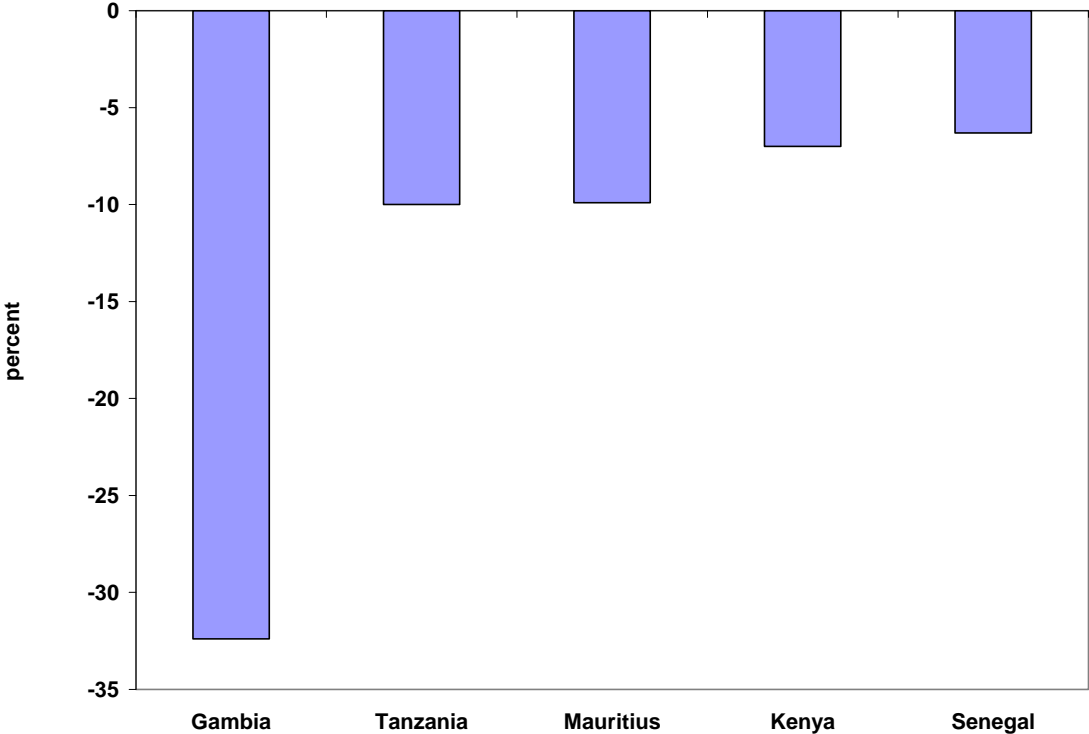


**Figure 7b. Change in 2009 trade balance as % of 2006 GDP**

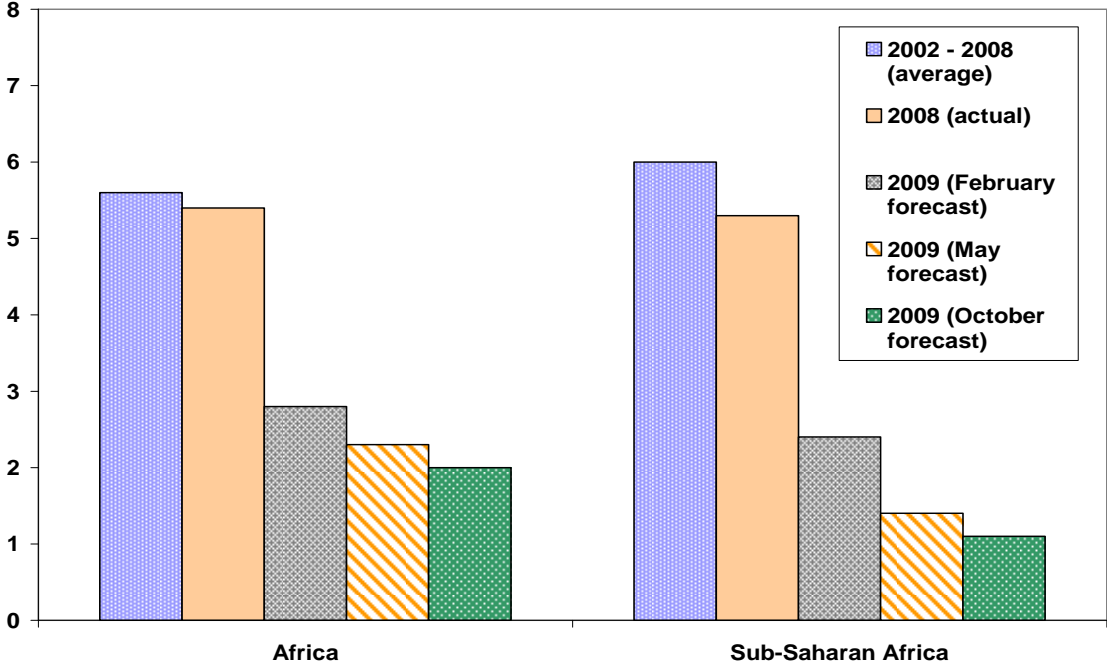


Source: African Development Bank and World Bank.

**Figure 8.** Change in tourist arrivals (Jan – Apr 2009 compared with Jan – Apr 2008)

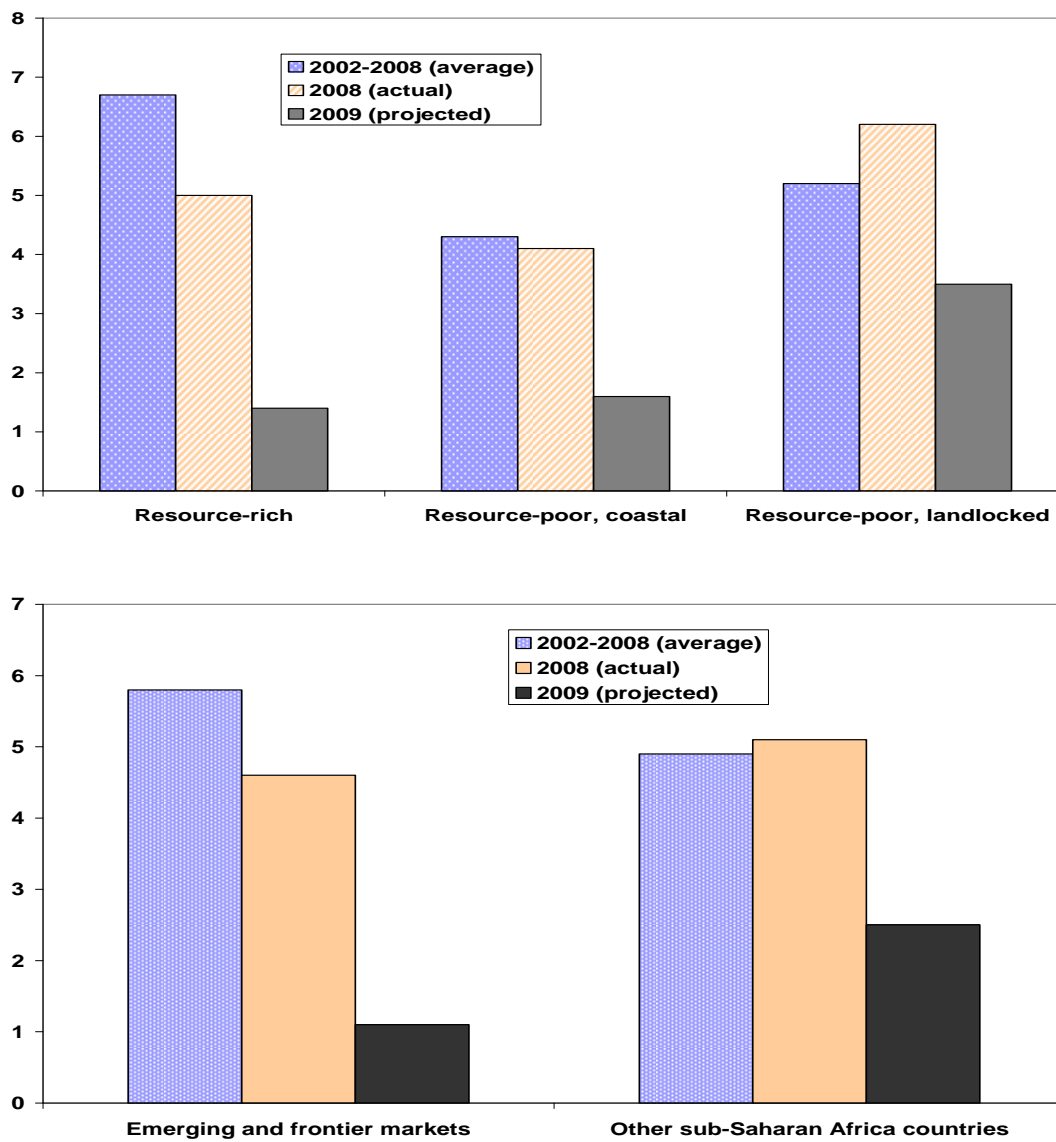


**Figure 9.** Real GDP growth in Africa and Sub-Saharan Africa (percent)



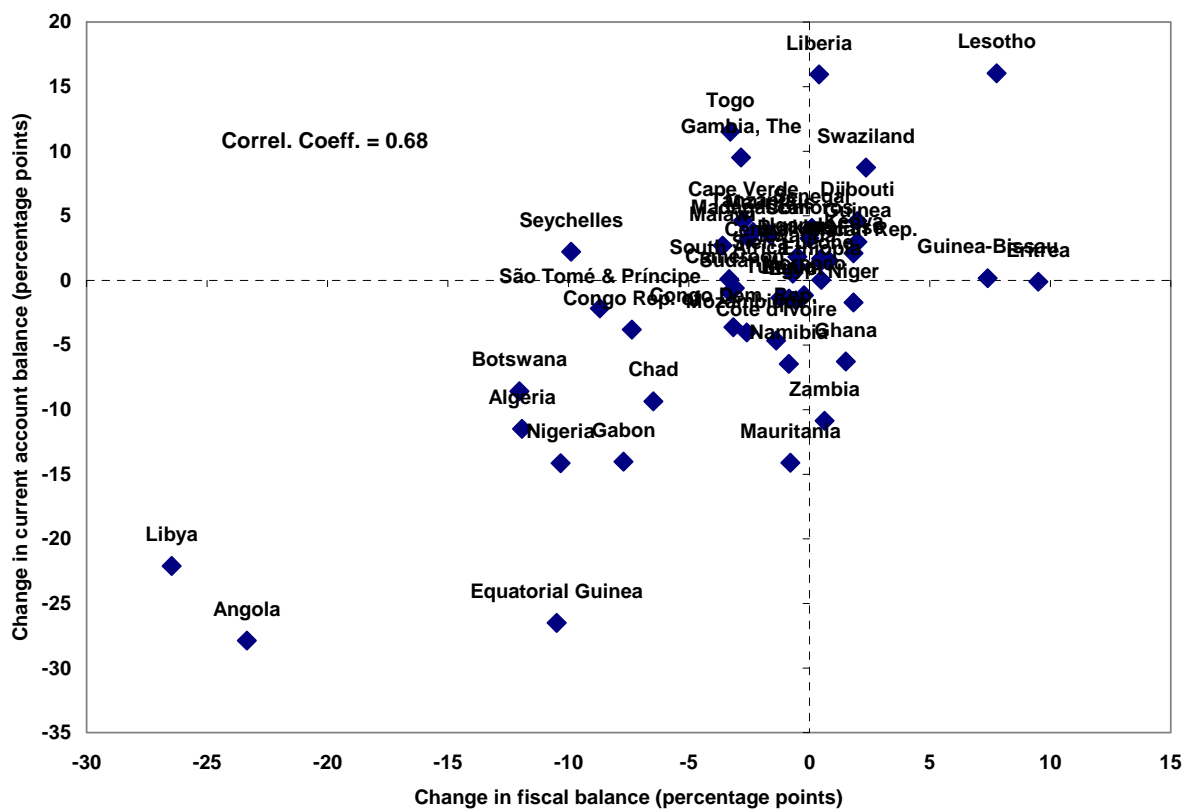
Source: African Economic Outlook database.

**Figure 10.** GDP growth in sub-Saharan Africa sub-groups (percent) 1/



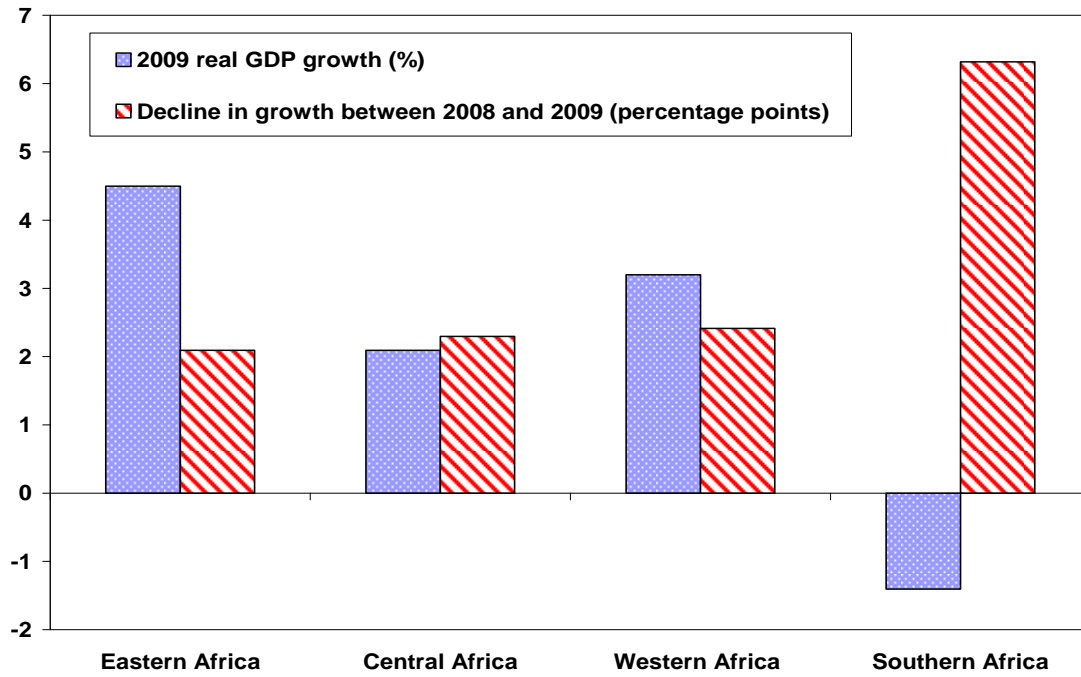
**Source:** African Economic Outlook database (October 2009) and authors' calculations (unweighted averages). 1/ Country classification is in Annex.

**Figure 11.** The “twin deficits”: changes in fiscal and current account balances, 2009 relative to 20081/



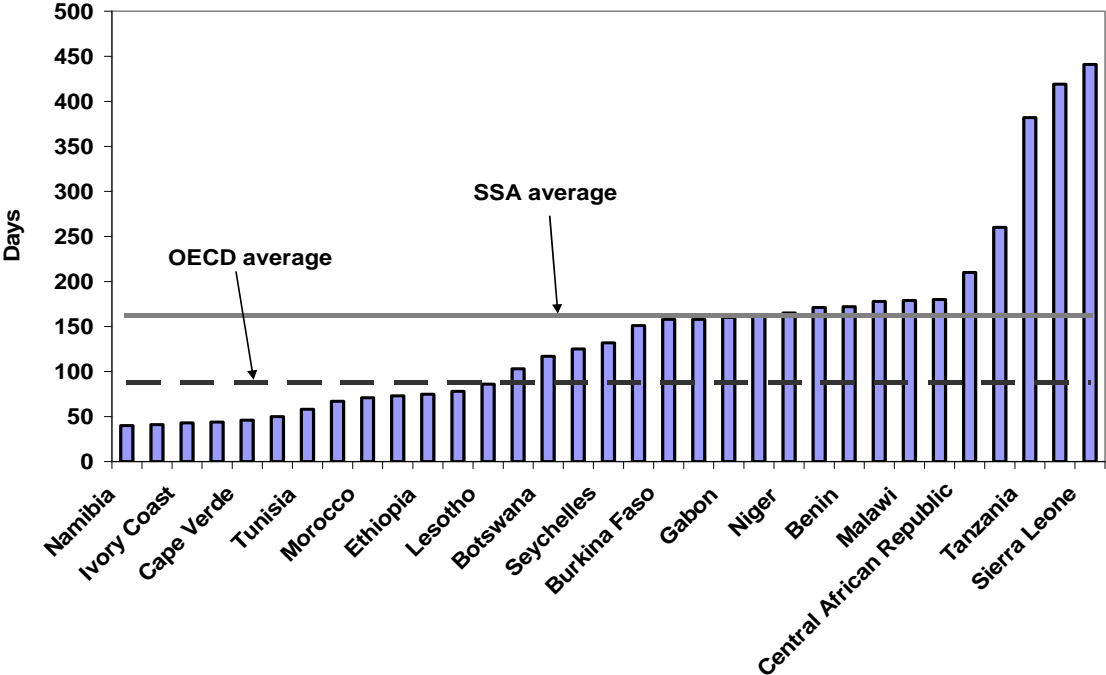
**Source:** African Economic Outlook database (October 2009) and staff calculations. 1/ Negative sign means deterioration in 2009. Both fiscal and current account balances include grants. The change is calculated as balance in as a share of GDP (in percent) in 2009 minus balance in 2008.

**Figure 12. Real GDP growth in Africa's sub-regions**



**Source:** African Economic Outlook database.

**Figure 13.** Time to get electricity in 2009 (days)



Source: World Bank doing Business.

**Figure 14.** Share of working hours lost due to power outage

