The Growth Trajectory of Non-Sovereign Operations within the African Development Bank

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Non-Sovereign Operations & Private Sector Support Department
A triple rated institution established fifty years ago by independent African States supported by 75 member countries, the African Development Bank has delivered on its mandate by financing more than USD 100 billion of projects for Africa’s development, an increasing number of which focus on private sector development. Since the launch of its private sector window, Bank’s investment has grown faster than the overall portfolio—representing currently one third of the total outstanding portfolio. The number of operations, the geographic outreach, the diversity of mobilized financing instruments and the policies and procedures have experience the same path.
AfDB Private Sector’s financing has recorded a very high growth rate these last years, by allowing allocating 50% of the risk capital available for lending from GCI-VI to non-sovereign operations. This has significantly enhanced the reliance of the Bank in RMCs, particularly Low Income Countries (LICs) with limited access to capital markets at cheapest cost. Annual approvals increased from modest average of USD 287 million during the early 2000s to USD 2.5 billion in 2017 (Fig. 1).

The Bank’s private sector operations cover a wide-range of sector across the continent. The figure below illustrates the sectors with the largest outstanding balances as at the end of 2017: the financial sector (63%), the infrastructure sector (24%) and the Industry sector (14%).

In addition to its own resources, the Bank through its private sector operations mobilized USD 4.28 billion financing in 2017.

As at end 2017, the cumulative volume of gross approvals including loans, equity investments, guarantees and technical assistance grants amounted to USD 20.24 billion involving 603 operations.
To address the major constraints of private sector operations and SMEs, which relate to access to finance, the Bank invested significantly in the Financial Sector in 2017. The Bank invested USD 1.4 billion in 2017 in the region’s financial sector, providing critical support to the African’s banking and financial sectors, especially loans to boost financing for small and medium enterprises (SMEs), Soft Commodity Finance Facilities, Trade Finance LoCs, RPAs, etc. These facilities include also Private Equity, Regular LoCs, the Africa SME Program, etc.) An estimated 19,500 African small and medium sized enterprises benefited from access to finance from these interventions with an average loan size of circa $60,000 per SME.

The Bank also invested nearly USD 575 million in private power and transport sponsored projects. New sources of funding and innovative instruments have been mobilized to overcome infrastructure deficits with a particular emphasis on renewable energy. In the power sector (African power utility company), the Bank has recorded in 2016 a landmarked syndicated financing of almost USD 1 billion from commercial co-financiers. Through large-scale investments in regional corridors (Nacala, Lobito), ports and airport (Senegal integrated infrastructure - Dakar container terminal expansion, Dakar-Diamniadio toll highway and the new Blaise Diagne International Airport), Southern Africa Rail network, etc.

The Bank has contributed to create the enabling environment for regional integration, improve efficiency of essential services and extend these to the landlocked countries.

The Bank developed technical assistance (TA) projects targeting inclusive private sector development. A total amount of USD 64 million of grants funded 68 TA projects from 2006 to 2017. Areas of intervention included amongst other: SME access to finance (54% of the portfolio), skills development (17%) and inclusive industry projects with a focus on value chain development, SME business linkage, value addition and local content (18%). At end of 2017: 350,000 SMEs accessed finance, 270,000 new depositors registered, over 1,000,000 low income earners being served for the first time, 10,000 Bank/MFI staff trained in SME lending, over 3,900 SMEs trained in various business-related areas to trigger effective demand for the lines of credit and 60,000 new direct jobs created.

A particular feature is the increased relevance in underserved markets: low-income countries (LICs), including Transition States received 23% of approvals. Transition States benefited directly from only 4% of approvals. However, they potentially also benefited from the 33% of approvals accruing to multinational investments in LICs notwithstanding additional advantage through Bank’s co-financing efforts. Since 2010, non-sovereign lending to LIC countries has reached USD 3.307 billion, with a further USD 3.543 billion.

*In 2017, 100% of new lending in our power portfolio was in renewable energy.
4.314 billion leveraged through co-financing, hence playing its catalytic role.

**Diversified product mix:** The Bank's private sector deploys four types of instruments: debt (project and corporate finance facilities), equity (direct and indirect through funds), and (to a much lower extent) guarantees and risk management products, which have historically been deployed with financial intermediaries. NSO achieved a high multiplier effect (around 6) in bringing other investors in the transactions.

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To achieve its objectives, the Bank, through its AAA rating, lends to borrowers via various financial instruments: senior debt, guarantees, subordinated debt, lines of credit, equity and technical assistance. Over the past seven years, the Bank has approved more than USD 6.33 Billion through these financial instruments, namely senior and subordinated debt as well as direct equity and equity fund.

**Credit Enhancements & Local currency financing** - To scale up investments in energy financing and local currency infrastructure financing, the Bank has been deploying a wide range of innovative financing instruments which include, amongst others: (i) Private Sector Risk Sharing facility (PSF-specifically dedicated to private sector operations in fragile states), (ii) Climate finance support - through the CIFs, GEF etc. - for a variety of projects; and (iii) Africa Growing Together Fund which is a partnership with China with initial funding of USD 2 billion. The Bank continued to intensify the use of its Credit Enhancement Facilities (PCG, PRG) to mitigate perceived risks in low-income countries and attract investors.

**The use of local currency in private sector operations** is also getting momentum. Eight percent (8%) of active net approvals were denominated in South African Rand and 2% in other African currencies, indicating a 10% use of regional currencies. The Bank's continuous use of the TCX Fund platform should enhance efforts at increasingly lending in local currency to reduce currency risk in NSO projects. This would grow local currency markets and strengthen local financial markets and systems in the Bank's RMCs.

**The Bank has also been a key player in the African equity market.** The committed portfolio of equity investments has grown steadily from USD 102 million in 1997 to USD 1.36 billion as at the end of 2017. Through equity investments, the Bank contributes to the fulfilment of private sector development by nurturing and creating niches of growth for enterprises. It invested in 681 investee companies of all sizes and supported the emergence of African Fund Managers. Close to 60% of Funds in which the Bank has invested are managed by first time Fund Managers (or first time teams). The Bank continues to have a critical role to play in bringing those Funds and Fund manager to a level where DFIs will no longer be required as investors, when commercial investors will get enough comfort from realized track record. The portfolio is relatively well diversified both sectorally and geographically with a significant reach to Low Income Countries (LICs).
HIGH PORTFOLIO QUALITY WITH STRONG IMPACT

Net value addition to the Bank’s financials
Private Sector is a key contributor to the Bank’s long-term financial sustainability. The return on private sector operations has averaged 4% as compared to 2.5% for sovereign lending. Income contribution of NSO has registered a fourfold increase, from nearly USD46.7 million to USD286.5 (Equity investments dividends included) million between 2007 and 2017, and now accounts for more than 30% of total revenue from all operations.

The Bank has contributed to improve the result on the ground of its operations.
The development outcome of close to 98% of the private sector portfolio is rated good (ADOA rating of 3) or better and the additionality and complementarity ratings stand at a weighted average rating of 1.86 (scale from 1 to 3) with close to 97% of rated projects scoring a satisfactory rating. Additionally, the Equity investment portfolio provides multiplier effects (above 680 portfolio companies benefited from risk capital). The Bank has also been instrumental in the financial market diversification and deepening. The assessment of the portfolio indicated that the Bank’s investments played a key role in attracting strategic partner investors, and catalyzing growth of domestic businesses. It did play the role of honest broker and comfort arranger among investors in Africa, as it is the case with large infrastructure projects.

Track-record in business portfolio development
The Bank has increased its disbursement volume per year over the last year thanks to: (i) an improvement to the quality of pipeline with greater focus on quality at entry combined with growing lending volumes; (ii) a streamline process; (iii) greater focus and acceleration in a delivery

A DECREASING NON-PERFORMING LOAN (NPL) SHARE OF THE PORTFOLIO

Despite operating in a challenging market and highly vulnerable to exogenous shocks, the Bank is continuously improving the effective portfolio and risk management oversight functions. The recent improvement of the NPL level is the result of: (i) enhanced risk management, (ii) active portfolio management, (iii) creation of Special Operations Unit (SOU).

Aiming to continually decrease its NPL, the Bank is developing a comprehensive result and quality tracking framework with quality rating and monitoring systems to ensure quality at entry, supervision and exit in order to avoid credit deterioration over the project life.

*Expressed in # of Funds in which the Bank has committed capital.
NEW INITIATIVES & PROGRAMS TO SCALE-UP PRIVATE SECTOR DEVELOPMENT IN RMCs

Building on its record of accomplishment, the Bank is embarking on new initiatives to scale up its interventions aiming at contributing to transform Africa’s private sector into the engine of inclusive growth towards attainment of the Sustainable Development Goals.

The Bank’s African Financial Markets Initiative (AFMI)
The initiative, which was launched in 2008 has recently been reshaped to help deepen the African domestic bond markets, boost private sector financing and improve the availability and transparency of bond market data. In 2015, AFMI launched the AfDB/AFMI Bloomberg Africa Bond Index (ABABI), which includes the six most liquid bond markets in Africa (Egypt, Nigeria, South Africa, Kenya, Botswana and Namibia). AFMI is working to link four African stock exchanges – Casablanca, Johannesburg, Nairobi and Nigeria – to deepen financial integration and increase liquidity. AFMI is also supporting the African Exchanges Linkage Project (AELP) which aims to deepen African financial markets’ contribution to fund African economies, increase intra-Africa regional trade and address the lack of liquidity in African financial markets by creating linkages across markets.

The Affirmative Finance Action for Women in Africa (AFAWA)
This is a Pan-African initiative, to address the barriers that women face in accessing finance for their businesses and to unlock their entrepreneurial potential for inclusive growth in Africa. Under this initiative, the Bank aims to mobilize $3 billion to close the financing gap for enterprises across Africa that are owned and led by women.

The Facility for Energy Inclusion (FEI)
The Facility for Energy Inclusion is a debt financing platform for small-scale projects (off-grid solar, small IPPs and mini-grids) with the objective of aggregating capital, structuring bankable projects and accelerating delivery as to increase access to clean energy across Africa.

The Africa Investment Forum (AIF)
The Bank is championing the AIF, a multi-stakeholder, multi-disciplinary collaborative platform for the economic and social development of the continent. This forum will be a fully transactional marketplace dedicated to advancing projects to bankable stages, raising capital and accelerating the financial closure of deals.

SUPPORT THE RMCs’ AGENDA FOR IMPROVING THE ENABLING ENVIRONMENT

The Bank’s portfolio indicated progress towards alignment of its core interventions through program support operations with the core objectives of improving the investment climate and promoting regional investment & trade. It has also used its convening power with policy makers and host government institutions, to improve the regulatory frameworks in RCMs. In this regard, the Bank has launched specific initiatives and flagship programs under its Industrialization Strategy. (Approved in 2016) to foster enterprise development. Within trade and regional integration, agenda the Bank intend to expand access to markets and strengthen its support to Regional Economic Communities (RECs).

Under pillar 3 of the Governance Strategic Framework and Action Plan 2014-2018 related to Investment and Business Climate, the Bank has supported 63 projects across RMCs. The outputs aimed at: (i) Strengthening policy and regulatory frameworks; (ii) Removing barriers to setting up and running businesses; (iii) Improving investment codes; (iv) Promoting MSME growth- women entrepreneurship? Improving Access to finance; (v) Land-Property access; and (vi) Job creation. For Cote d’Ivoire for instance, 50 MSMEs have been supported and a Centre for Agro-industrial competitiveness was established. In Senegal, a Financial literacy program was delivered and a simplified process of business registration for SMEs was put in place. In Egypt, Industrial licensing has been reduced from 632 days to 7 days.
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