# Africa's development banks: the urgent need for scale

*There is a moral case for international provision of large-scale concessional funding to Africa. The continent is projected to feel the impacts of climate change the most, while having an estimated annual sustainable development goal financing gap of $200 billion.* ***Nimrod Zalk*** *writes that African countries should rapidly raise the capitalisation of development banks to enable higher levels of lending, and discusses way to do that.*

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Developing countries in general, and African countries in particular, confront an enormous financing challenge to meet the UN's Sustainable Development Goals (SDGs), featuring prominently at the 2021 United Nations climate change conference (COP26). Yet, even prior to COVID-19 the prospects of mobilising the annual $2.5 trillion needed to meet the SDGs by 2030 was rapidly receding despite a global savings and liquidity glut. The bulk of SDG funding is needed to close gaps in electricity, transport and water infrastructure in ways that place the continent on a decisive trajectory towards net zero emissions. Concurrently, substantial funding is required for agricultural modernisation and greener industrialisation.

The moral case for international provision of large-scale concessional funding to Africa is overwhelming.  African countries are projected to feel the impacts of climate change the most, despite accounting for a minuscule share of cumulative global $C0_2$ emissions. Climate funding from multilateral development banks (MDBs) has been growing, but it comes nowhere near the estimated annual African SDG financing gap of $200bn. While figures for the whole continent are not readily available, the $7.4bn of MDB commitments to Sub Saharan African countries in 2019 is reflective of the scale of the financing gap. Ambitious recommendations have gained little traction—such as the UN's Task Force on Financing for Development proposed development of long-term financing instruments such as 40-50 year bonds, necessary to fund a global Green New Deal.

Rather much emphasis is placed on the role of 'blended finance' to plug the SDG financing gap by leveraging scarce low-cost funding via multilateral development banks and overseas development assistance. In the World Bank's conceptualisation, billions of dollars of such concessional funding can be used to crowd in trillions of private investment by 'de-risking' SDG-aligned projects to render them attractive to private investors. One key question is whether this approach de-risks projects to enable development, or de-risks investor returns through complex financial engineering, regardless of outcomes. Most fundamentally, blended finance projects have failed to take off at scale, reaching only about $20bn per annum for all developing countries combined.

Rather far more effort is needed to capacitate African national and regional Development Banks (ADBs), to mobilise public and private investment for structural transformation, as they have done elsewhere in the world including Europe's EIB, Germany's KfW, Brazil's BNDES and China's policy banks. Development banks have played a pivotal role in mobilising long-term finance for industrialisation, developing new industries, and project de-risking through developing capabilities to undertake project development, implementation and monitoring. Effective development banks act as important voices for shaping favourable economic policy for productive investments. They crowd in private finance directly and unlock private investment up and down-stream from catalytic projects.

Africa in fact has a lot of development banks. There are 95 of them, representing 21% of national and regional banks worldwide. However, a handful dominate assets and financing: the regional African Development Bank (AFDB) and African Export and Import Bank (Afreximbank) and national banks in Morocco, South Africa and Egypt. But the rest are mostly small and undercapitalised. Hence African development banks collectively account for only 1% of development bank assets worldwide.

African countries cannot afford to tread water waiting for the global multilateral and private financing system to become more equitable or responsive (although they do need to fight for this in the medium to long term). Rather they should rapidly raise the capitalisation of their development banks to enable higher levels of lending. How is this to be achieved when public debt in Sub-Saharan Africa is at a two-decade high and viewed as unsustainable by ratings agencies and multilateral finance institutions? First, there is a strong case for the consolidation of fragmented and under-capitalised national banks into larger sub-regional development banks. Second, shareholding from other development banks in the South with proven scale and expertise should be encouraged. Third, by directing proceeds from periodic commodity booms and clamping down on illicit financial flows towards development banks. Fourth through the state's selective extension of sovereign guarantees. Fifth, fiscal transfers at appropriate points in the sovereign debt cycle should not be ruled out. Finally, if central banks are serious about ensuring long term financial stability they need to support financing instruments that address long term social and climate risks.

The scaling up and consolidation of African development banks would also improve governance and developmental capacity. A broader range of shareholders would make it more difficult for crude political appointments at managerial level that are closely associated with poor performance. Other Southern development banks bring technical expertise critical to building capabilities needed to de-risk projects, including project development, monitoring and enforcement. Furthermore, the scaling up of African development banks could well induce multilateral development banks to raise their own financing efforts in Africa. Rather than crowding out private financing, the scaling of African development banks offers the most promising route to crowd in long-term private finance to achieve the SDGs and structural transformation.

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*Notes:*

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