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Independent Development Evaluation
African Development Bank

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Evaluation of the AfDB's Role in Increasing Access to Finance in Africa

Executive Summary

An IDEV **Thematic Evaluation**

AFRICAN DEVELOPMENT BANK GROUP

July 2020

Executive Summary

Background

The African Development Bank's Ten-Year Strategy (2013-2022 TYS) focuses on improving the quality of Africa's growth through inclusive growth and the transition to green growth. It commits the Bank to strengthening financial sector development. Increasing access to finance is one of three objectives of the 2014-2019 Financial Sector Development Policy and Strategy (FSDPS) approved in October 2014. The other objectives were deepening financial markets and safeguarding the stability of Africa's financial system (AfDB 2014). Conscious of the importance of the financial sector in advancing economic development across the continent and ensuring financial inclusion, the Bank is keen to help Regional Member Countries (RMCs) to improve access to financial services.

The Independent Development Evaluation (IDEV) evaluated the Bank's 2014-2019 FSDPS, with a focus on the role of the Bank in increasing access to finance and financial inclusion in Africa. This evaluation is part of IDEV's work program to provide credible information to help improve policies and strategies going forward.

The evaluation assessed: (i) the relevance and the quality of design of the FSDPS; and (ii) the relevance, quality of design, effectiveness, efficiency, and sustainability of financial sector development (FSD) operations approved between 2011 and 2018, focusing on access to finance. The period covers both the pre- and post- periods of the adoption of the FSDPS in October 2014. The evaluation presents a summary of findings, and makes recommendations to inform the preparation and implementation of the new strategy.

The report's evidence comes from a triangulation of quantitative and qualitative data collection methods presented in the inception report. These include: (i) a desk review of AfDB's and other relevant documents and databases; (ii) a survey through a questionnaire sent to managers and task managers; (iii) interviews with Board members, task managers and managers in charge of the financial sector; and (iv) case studies in Burkina Faso, Cameroon, Kenya, Nigeria, Namibia, Tunisia and Egypt. Egypt was selected because it hosts the African Export-Import Bank (Afreximbank), which received trade finance operations to on-lend to several countries in Africa. The evaluation faced the following limitations: (i) a lack of easily usable databases at AfDB; (ii) unavailability of information at the client and end-beneficiary levels; (iii) limited availability of local financial sector specialists with expertise in evaluation; (iv) measuring the results at the end-beneficiary level; and (v) the fungibility of resources limiting the attribution of the achievements to AfDB support. These limitations represent obstacles to the evaluation of the effectiveness of the operations, especially at the end-beneficiary level. As a result, the performance of the operations is assessed at the client level.

To address these challenges, IDEV planned the evaluation in collaboration with the Financial Sector Development Department (PIFD), and AfDB's regional and country offices. In addition to IDEV's internal review, results of the evaluation were reviewed by an Evaluation Reference Group (ERG) comprising experts from the financial sector and private sector departments at headquarters and decentralized offices, financial policy analysts, risk analyst officers, and three external peer reviewers. Meetings were held with the ERG to discuss the emerging findings and to decide on which recommendations to consider from the desk review in May 2019, the synthesis of the fieldwork in February 2019, and the whole evaluation in May 2020.

Findings

Recent trends in financial sector development in Africa

Recent developments in the financial sector require attention in the revision of the 2014-2019 FSDPS. First, the de-risking phenomenon that resulted in developed country banks withdrawing capital from emerging markets led to a reduction of correspondent banking relationships in jurisdictions that were less attractive, such as those in Africa. Second, there has been an increase of the number and spread of pan-African banks operating in several countries under different regulatory and supervision arrangements. Third, the emergence of fintechs and digital payment platforms that have increased the use of mobile money, remittances, savings, credit provision, etc. have also increased the need for different regulatory regimes and oversight. Fourth, the growing need by African governments and corporates to raise funding from local capital markets to supplement traditional funding sources. Going forward, digitization is likely to be even more important in the post-COVID-19 era. Fifth, the pandemic has pushed most of the world into a lockdown, causing economic recession, financial scarcity, and GDP declines, inevitably increasing bankruptcies and Non-Performing Loans (NPLs) in many countries. This situation requires governments, central banks and International Financial Institutions (IFIs) to significantly increase their financial support to corporates and Micro, Small and Medium-sized Enterprises (MSMEs). To this end, they need to strengthen their financial intermediaries (FIs) and Non-Bank Financial Institutions (NBFIs), including capital and financial markets. The negative effects of the COVID-19 pandemic have seen NPLs surge, spreads widen, and liquidity evaporate as funding sources dry up and bond markets crash. For regulators, these new developments in the financial sector ecosystem and the associated risks require the need to balance financial sector stability, i.e. safety, increased access and innovation.

While there has been substantial progress over the past decade, access to finance continues to be one of the key constraints to private sector development in Africa, particularly among SMEs. Small and Medium Enterprises (SMEs) often mention access to finance as their biggest constraint. Fifty-two percent of SMEs in Sub-Saharan Africa (SSA) are regarded as financially constrained, with an unmet financing requirement of about US$331 billion in 2017. The percentage of adults with an account in a financial institution or mobile wallet was almost 20 percentage points higher in 2017 than in 2014 for all categories of countries classified by income level. However, access to finance in Africa remains lower than in other regions. Also, within Africa, there was a high disparity between countries, with the highest access in Mauritius (90 percent) and very low access in the Central African Republic (14 percent) and South Sudan (9 percent). The percentage of adults using mobile money was by far the highest in SSA, at 21 percent, compared with 6 percent in the Middle East and North Africa, 4 percent in South Asia, and 3 percent in Latin America and the Caribbean.

Financial sector development policy and strategy

The 2014-2019 FSDPS was a hybrid document combining both a policy and a strategy. While the document reflected the state-of-the-art in financial sector knowledge, there was limited clarity on the relationship between the policy and the strategy, and the definitions of the concepts used. Some other AfDB documents combined policies and strategies as documented in the Classification Paper on Bank Group Policies, Strategies and other Directional Documents approved on 25 March 2019. The FSDPS also contained missteps in designing and planning activities, such as: (i) weak conceptual clarity and priority setting, as well as a lack of definition of AfDB's comparative advantages and clear areas of focus; (ii) a lack of clarity on how specific priorities such as fragile states, agriculture, and innovation should be reached; (iii) the lack of a theory of change to explain how activities undertaken by AfDB would translate into desired results: outputs, outcomes and impacts; (iv) the lack of an appropriate business plan with monitorable indicators; and (v) a weak monitoring and evaluation system: weak definition of target groups, indicators often not related to FSD, and the lack of baseline data for most indicators selected.

Findings from the case-studies in Burkina Faso, Cameroon, Kenya, Nigeria, Namibia, Tunisia showed that the high priority given to access to finance in the FSDPS and partner countries was not reflected in the Country Strategy Papers (CSPs). All countries visited consider access to finance and financial inclusion to be a priority for economic development, including rural development, employment, and women's economic empowerment. The CSPs refer to the financial sector mostly as a channel to improve financing for priority sectors, but do not place sufficient emphasis on the need to build strong, sustainable and resilient financial systems.

Despite increased internal capacity to deliver, there was weak coordination of FSD activities in AfDB. The number of professional financial sector staff in PIFD almost doubled in 2014-2018, from 22 to 42. However, there was a shortage of staff in the supervision and monitoring functions after disbursement. PIFD's 2018 budget was 1.5 times that of 2014 (OFSD). However, the unifying role played by OFSD has been lost since the implementation of the Development and Business Delivery Model (DBDM) in 2016, implying weak synergy and efficiency in delivering the FSDPS objectives. Despite this, a strong partnership with other actors in the financial sector has helped AfDB to extend its capacity to support the sector.

Structure and the evolution of the portfolio

The number and volume of FSD operations approved almost doubled from 2011-2014 to 2015-2018. The share of FSD operations in the total amount approved by AfDB increased from 17.4 to 21.6 percent from the pre-FSDPS period to the FSDPS period. Financial sector operations accounted for a large share of Non-Sovereign Operations (NSOs). The number of Sovereign Operations (SOs) increased from 8 percent during 2011-2014 to 18 percent of the financial sector during 2015-2018, while the amount increased from 12 to 28 percent of the total amount approved between the two periods for the financial sector. This increase is explained by the increased support to a number of development banks with national and regional outreach.

Lines of credit (LOCs) remained the main instrument used, but approved amounts decreased from 60 percent of FSD operations during 2011-2014 to 34 percent during 2015-2018. Trade finance LOCs (TFLOCs) steadily increased from 5 to 26 percent of the amount approved in the the two periods. The amount approved for TFLOCs during 2015-2018 and the number were 9 times higher than in the previous period. Guarantee amounts increased 2.5 times (but from a small base). Risk participation instruments, first introduced in 2013, represented 5 percent of approvals during 2015-2018. While the FSDPS intended to support all FSD, Program-Based Operations (PBOs) and Technical Assistance (TA) were very limited, although many countries need interventions that explicitly foster FSD as an objective.

The number of countries receiving financial resources increased from 19 to 31 (not including multinational operations, which represent almost 44 percent of the amount approved during each period considered). There was a much lower concentration of resources during 2015-2018 than in 2011-2014. For example, Nigeria received 8.3 percent of the total amount approved in 2015-2018 compared with 29.8 percent in the previous period. The operations from UA 5-50 million increased the most, with amounts and numbers 2.3 times higher than those of the previous period. The small and large operations (less than UA 5 million and above UA 100 million) also increased, but to a lesser extent.

AfDB has at least doubled the number of clients in most categories, but the number of microfinance and insurance companies significantly decreased. The main clients remained commercial banks and equity funds. The number of microfinance institutions supported fell from 10 during 2011-2014 to three during 2015-2018 and that of insurance companies from four to zero. Sovereign client organizations (governments and central banks) almost tripled, highlighting AfDBs' increasing support for public entities to support FSD.

Use of local currency and guarantees, as well as some other FSD operations, increased. First, there was an increase in local currency operations from just two in 2011-2014 to 11 in 2015-2018; amounts approved similarly increased from 2.4 to 10 percent. So far, four currencies have been used (South African rand, Nigerian naira, Botswanan pula and Zambian kwacha). Second, since the end of 2014 until 2018, the operations to support financial capital markets amounted to UA 1,331 million, or 14.3 percent of the total amount approved. Fifty-four percent of this amount was meant to provide guarantees for local currency risk hedging, while 36 percent was for financial sector budget support. The remaining 10 percent consisted of TA to support regulatory authorities, and financial infrastructure and payment system development. Third, while operations in technology and renewable energy were few, the number and amount approved during the FSDPS was 4 times and 4.5 times, respectively, compared with the previous period.

Performance of the operations evaluated

AfDB operations were in line with the FSDPS objectives and relevant to their respective client and country contexts, but the majority did not necessarily serve the underserved. AfDB operations mostly focused on channeling long-term funding to FIs for on-lending to priority sectors of the real economy. Given the broad scope of the FSDPS and significant gaps in FSD, the operations were in line with the FSDPS, and with client and country needs. Furthermore, many other constraints mentioned in partner countries' strategies and the FSDPS remain unaddressed, such as weak payment systems, regulatory constraints, and a lack of innovation and informality, among others.

In the six case-study countries in which AfDB had multiple financial sector operations, there was no evidence that these were part of a coherent Bank strategy toward FSD. The lack of thorough country financial sector diagnostics to understand the underlying constraints may have contributed to the weak strategic clarity and focus. Except for the operations in Tunisia and Morocco, AfDB's financial sector operations were decided on their case-by-case viability and did not represent a coherent set of interventions that jointly contribute to achieving FSDPS objectives. The lack of a Bank vision for FSD at the country level is also reflected by the fact that AfDB is not visible as a leader in policy dialogue on FSD.

While the operations were effective in providing resources and services otherwise unavailable to client financial institutions, it was not feasible to track and measure development outcomes for end-beneficiaries. Development outcomes and end-beneficiaries were not clearly defined in Project Appraisal Reports (PARs) and in reporting. Although LOCs often target specific underserved and excluded population segments (such as the rural population, women and young people), related results information was missing in many cases. When information was available, it showed that the intended targets represented only a small part of the portfolio of client institutions benefiting from AfDB's LOCs. LOC objectives loosely refer to access to finance, but without defining clear targets for reaching underserved target groups such as women and youth. Furthermore, the positioning of SME finance as a driver of growth and job creation led to a focus on high-growth SMEs. While the focus on strong SMEs makes sense from a private sector development perspective (for instance, to promote enterprises' development for job creation), it risks not focusing on the underserved. The diverse financial needs of households and individuals, other than business needs (e.g., management of shocks, reduction of vulnerability/poverty, women's empowerment, access to other basic services), are hardly considered in project designs. This raises questions regarding strategic clarity and whether operations are effectively targeting SMEs, the underserved, and excluded segments of the population.

The efficiency of AfDB's FSD operations were partially satisfactory. Half the evaluated operations were efficiently prepared and implemented. Others faced time overruns that, in some cases, led to additional costs for clients or missed lending opportunities. Even in operations with satisfactory efficiency, clients stated that processes were overly prolonged apart from those for repeat operations. Among the main reasons advanced to explain the situation were onerous AfDB conditions precedent to disbursement, inefficient communication, and the lack of an automated procurement system.

Although AfDB provides much needed long-term funding to its target markets and has often helped clients access additional funding from other IFIs, its operations tended to provide temporary solutions and did not address underlying constraints in FSD. The lack of long-term funding was addressed only temporarily through supporting end-beneficiaries via financial intermediaries. AfDB supported regulated, financially sustainable institutions, but the likelihood that they will continue to serve underserved target groups beyond the period of AfDB support is questionable. This is because most operations did not address the underlying constraints that prevent financial institutions from serving the underserved segments of the population and the economy, including SMEs. Such constraints include insufficient capacity and willingness to serve certain segments of the market, weak regulation and supervision, a lack of competition, information asymmetries, and high transaction costs and risks. These factors contribute to the high interest rates prevailing in African financial sectors.

There were few innovative ways to increase access to finance through digital and other alternative delivery channels in the evaluated portfolio, despite the disrupting role that technology plays in a number of African financial sectors. More recently, however, AfDB has become more active in supporting the development of capital markets and digital financial services.

While AfDB played an important role in introducing Environmental and Social Management Systems (ESMSs) and trained clients on environmental and social (E&S) issues, its performance in supervision was poor. Its E&S safeguards performance at appraisal was found to be strong and significantly improved over time. However, performance in supervision was poor because of a lack of the following: (i) a specific reporting template; (ii) asking clients to submit reports on E&S perfomrnace, even in cases where this was included in the loan agreement; (iii) evidence; (iv) candor in the assessment; and (v) expert support during supervision missions-and more generally, inadequate staffing with E&S experts.

Recommendations

IDEV makes the following recommendations:

1. **Clarify AfDB's role in financial sector development.** Priority areas of action include:

- Focus the Bank's strategic priorities, which are broadly defined in the current FSDPS document. Separately, revise the strategy and update the policy to address conceptual and practical concerns in the current FSDPS.
- Conduct sector diagnostics that identify barriers to access to finance at country and regional levels.
- Be more explicit on how operations contribute to FSD.

2. **Position AfDB as a key player in financial sector development.** Priority areas of action include:

- Step up AfDB's engagement in policy and regulatory dialogue aimed at strengthening the financial sector environment.
- Formalize coordination of departments involved in financial sector activities and institute a Bank-wide information system on financial sector activities to facilitate evaluation and decision-making.
- Improve outreach and the depth of relationships with sector stakeholders, including clients.
- Consider increasing the resources for operations aimed at fostering regional financial integration.
- Prepare an action plan and adequate staffing to address E&S issues.

3. **Improve benefits for the intended target groups.** Priority areas of action include:

- Better define and measure project development outcomes and the benefits for target groups.
- Include a clear definition of what constitutes an SME in PARs and CSPs.
- Build on effective approaches to support SME finance.
- Move from a pipeline approach to a portfolio approach, focusing on increasing the relevant target portfolio.
- Use of a more deliberate approach to narrow the gender gap in access to finance.

An IDEV **Thematic Evaluation**

About this Evaluation

This evaluation presents a summary of the work carried out to assess the assistance of the African Development Bank (AfDB or "the Bank") in increasing access to finance in Africa over the period 2014-2019. The period covered both the pre- and post-periods of the adoption of the Financial Sector Development Policy and Strategy (FSDPS). It made recommendations to inform the preparation and implementation of the new strategy. Its findings are based on quantitative and qualitative information collected from different sources, and that combined both a summative approach for the completed operations and formative approach for those still ongoing.

It was found that all countries visited during this evaluation consider access to finance and financial inclusion to be a priority for economic development, including rural development, employment, and women's economic empowerment. Despite increased internal capacity to deliver, there was weak coordination of Financial Sector Development (FSD) activities in the Bank. Nonetheless, the share of FSD operations in the total amount approved by the AfDB increased from 17.4 to 21.6 percent from the pre to post FSDPS period. The operations were in line with the FSDPS, as well as with client and country needs, though only half the evaluated operations were efficiently prepared and implemented.

Three core recommendations, each with priority areas of action, were made to improve the Bank's intervention in increasing access to finance in Africa: 1) The role of the Bank in FSD should be clarified; 2) Position the AfDB as a key player in FSD; and 3) The Bank should improve the benefits for the intended target groups.

IDEV
Independent Development Evaluation
African Development Bank

African Development Bank Group
Avenue Joseph Anoma, 01 BP 1387, Abidjan 01, Côte d'Ivoire
Phone: +225 20 26 28 41
E-mail: idevhelpdesk@afdb.org

Design & layout: A Parté Design

idev.afdb.org