

SUPPORTING THE TRANSFORMATION OF THE PRIVATE SECTOR IN AFRICA

Private Sector Development Strategy, 2013-2017



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AFRICAN DEVELOPMENT BANK GROUP

Acronyms and Abbreviations

AAA	Lowest risk rating of institutional long-term credit	ISS	Integrated Safeguards System
AAAA	Analytical, Advisory, and Advocacy Activities	KPI	Key Performance Indicator
AfDB	African Development Bank	LIC	Low Income Country
ADF	African Development Fund	MDB	Multilateral Development Bank
ADOA	Additionality and Development Outcome Assessment	MIF	Multilateral Investment Fund (of the Inter-American Bank)
ADR	Africa Development Report	MIGA	Multilateral Insurance Guarantee Agency
AML-CFT	Anti-money laundering and combating the financing of terrorism	MIC	Middle Income Country
AsDB	Asian Development Bank	MSMEs	Micro, Small and Medium Sized Enterprises
BEE	Business Enabling Environment	MTS	Medium Term Strategy
BDS	Business Development Services	NSO	Non-Sovereign Operations
DAC	Development Assistance Committee of OECD	ODA	Official Development Assistance
DPs	Development Partners	OECD	Organization for Economic Cooperation and Development
CFF	Commodity Finance Facility	OIVP	Infrastructure, Private Sector, Water & Sanitation and NEPAD, Regional Integration and Trade Operations Vice Presidency (AfDB)
CIMM	Corporate Information Management and Methods Department (AfDB)	OPSM	Private Sector and Microfinance Department (AfDB)
COBS	Programming and Budget Department (AfDB)	ORCE	Central Africa Department (AfDB)
CoST	Construction Sector Transparency Initiative	ORPF	Procurement and Fiduciary Department (AfDB)
CSP	Country Strategy Paper	ORPC	Operational Resources and Policies Department (AfDB)
CSR	Corporate Social Responsibility	ORQR	Results Department (AfDB)
DFID	Department for International Development (UK)	ORVP	Operations Vice Presidency for Country & Regional Programs & Policy (AfDB)
EBRD	European Bank for Reconstruction and Development	OSAN	Agriculture and Agro-Industry Department (AfDB)
EPZs	Export processing zones	OSGE	Governance, Economic / Financial Sector Reform Department (AfDB)
EITI	Extractive Industries Transparency Initiative	OSHD	Human Development Department (AfDB)
ESW	Economic and Sector Work	OSVP	Corporate Services Vice Presidency (AfDB)
FAPA	Fund for African Private Sector Assistance	PBA	Performance-Based Allocation
FDI	Foreign Direct Investment	PBO	Policy Based Operation
FIs	Financial Intermediaries	PPP	Public-Private Partnership
FTRY	Treasury Department (AfDB)	REC	Regional Economic Communities
FNVP	Finance Vice Presidency	RPA	Risk Participation Agreements
GBS	General Budget Support	PRG	Partial Risk Guarantee
GCI-6	Sixth General Capital Increase	PSD	Private Sector Development
GDP	Gross Domestic Product	PSDSC	PSD Steering Committee
GTLP	Global Trade Liquidity Program	PSO	Private Sector Operations
GTF	Governance Trust Fund	RECs	Regional Economic Communities
IADB	Inter-American Development Bank	RFIP	Regional Framework for Investment Promotion
IBRD	International Bank for Reconstruction and Development	RISP	Regional Integration Strategy Paper
ICD	Islamic Corporation for the Development of the Private Sector	RMC	Regional Member Country
IDA	International Development Agency	RMF	Results Monitoring Framework
IFC	International Finance Corporation	SBS	Sector Budget Support
IFIs	International Financial Institutions	SMEs	Small and Medium-Sized Enterprises
IFRS	International Financial Reporting Standards	TA	Technical Assistance
ICF	Investment Climate Facility	TFLOC	Trade Finance Line of Credit
ICT	Information and Communication Technology	USAID	(US) Agency for International Development
IsDB	Islamic Development Bank	WARR	Weighted Average Risk Rating
ISPs	Institutional Support Projects		



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Voices from Africa

“Assistance to the private sector goes beyond the provision of incentives, and government is looking at wider interventions to lower the cost of doing business. Improvements are being made to economic infrastructure such as ports, roads and electricity generation to cater for the needs of business.”

Pravin Gordhan, Minister of Finance, The Republic of South Africa, 2012

“At the time I started my first business in the 1950s, it was difficult for a young African to dream of political freedom, let alone entrepreneurial success. Today, Africa is free and democracy is taking root. The African economy is growing, and presenting opportunities for entrepreneurs that at my time were a pipe dream.”

Richard Maponya, Lifetime Achievement Award Winner, Africa Awards for Entrepreneurship, 2012

“While many of the challenges facing businesses in key African markets are no more significant than elsewhere in the world, the rewards on offer are substantial. Critically, it is this risk-reward equation that makes African investment so compelling – the returns remain among the highest in the world, while risks are diminishing and can be effectively managed.

Diana Layfield, Africa CEO, Standard Chartered Bank, 2013

“As governments, we need to improve the business environment and strengthen dialogue with the private sector. Our efforts to create wealth will be in vain if we fail to create an environment that allows entrepreneurs to thrive.”

Mompoti Sebogodi Merafhe, Honorable Vice President of the Republic of Botswana, 2012

“Despite the options available for government to raise finance, the overwhelming consensus is that it cannot be done without private funds. At their best, private funds ease budget constraints and raise efficiency by leveraging private sector management expertise and innovation.”

Sanusi Lamido Sanusi, Governor of the Central Bank of Nigeria, 2012

“Africa needs its business leaders as never before – to help it generate more electricity, grow more food, and create more jobs to keep growing strongly, while also improving people’s well-being through less poverty, better health and education, and more hope.”

Thierry Tanoh, C.E.O. Ecobank Group, 2012

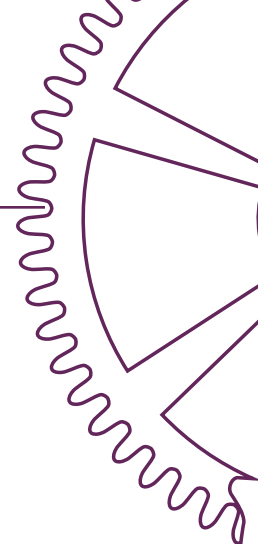
“Our analysis of gains in political stability, deep investments in infrastructure and improved environments for doing business in select geographic regions in Africa suggests that the time for large-scale manufacturing clusters is ripe.”

Jean-Louis Warnholz, Co-founder and Managing Director, FastAfrica, 2013



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Executive Summary

Africa is experiencing unprecedented economic growth, and the key objective of the Bank Group's Strategy 2013-2022 is to support the transformation of the continent by improving the quality of that growth – making it shared and more sustainable.

The future of African economic growth – and the futures of millions of Africans and thousands of African communities – is closely tied to the private sector.

However, the primacy of the private sector in African growth must be seen in context. The public sector still needs to create an environment in which the private sector can thrive and the two must work together to deliver services and opportunities.

African business offers both a potential blessing and a potential curse. Fifteen million new job seekers enter the African market annually and; they can shine in employment. Trapped in unemployment, they will become a threat to themselves and society.

It is African businesses that will create African jobs, by training and using African talent, and by developing the potential of services and industries, through the sustainable management and prudent use of Africa's considerable natural resources. This will plough the dividends of enterprise back into the lives of Africans and African societies. The private sector can also deliver services to society's most vulnerable people and – if it is properly regulated and responsible – it can help to make society at large well-regulated and responsible.

There has been a fundamental change of Africans' thinking in recent years, as governments recognize the centrality of the private sector's role in generating more business. The African Development Bank is responding to this change.

The Bank issues this Private Sector Development Strategy for 2013 to 2017 at a time that the private sector already generates two-thirds of Africa's investment, three-quarters of its economic output, and nine-tenths of its formal and informal employment. While the bulk of Bank lending is to

governments, it has directly and indirectly supported private sector operations in Africa since the end of the 1980s. Its private investment operations have increased nearly tenfold since 2000, from US\$250 million in 2005 to US\$2 billion in 2012. Increasingly, the Bank is moving and will continue to move from public to private investment, and from making investments itself toward encouraging others to do so, by unlocking further funds. Recent research shows that a dollar of AfDB money invested in the continent brings in a additional six from the private sector.

The private sector faces many obstacles in Africa, including inadequate government regulation, restrictive policies, poor infrastructure (particularly in power and transport), severe skills shortages and mismatches between employers' needs and available workers (particularly those just out of school), trade restrictions, tariff and non-tariff barriers to African exports, difficulties in obtaining medium- and long-term finance on affordable terms, and a large informal sector.

Business has also harmed itself when companies have failed to recognize the need for, and the potential of, widening their activities. Private sector growth in Africa, where it has occurred, has often been uneven, and exploitation of natural resources – the continent's largest area of growth – has failed to create enough new jobs.

This new Strategy's overriding vision is of a competitive private sector across Africa that will be an engine of sustainable economic growth, employment and poverty reduction on the continent in the next decade and beyond.

Several features distinguish this Strategy from its predecessors. It looks at Africa's private sector in its entirety, rather than at just some of its component parts. It commits to upstream policy work – across nations, regions and sectors, and using all available Bank expertise – as much as to individual projects, recognizing that short-sighted policies can quickly diminish the development impact of projects. It makes stronger linkages between the money that the Bank lends to governments and the money it lends to private organizations. It promises significant support to small businesses – key elements of any economy – while not



ignoring larger ones. It is carefully aligned with the Bank's overarching vision, by putting two objectives at its core: the quest for inclusiveness (that growth and opportunity should be shared by all – women and men, young people and old, rural communities and urban) and the gradual transition to green development as Africa commits to moving toward environmentally sustainable growth. The Bank moreover strengthens the implementation of the Strategy with establishment of a new steering committee to reinvigorate private sector development as a priority throughout the organization. In so doing, it sets measurable targets, and expects to be held accountable and to be able to continue to show what it has achieved.

The strategy is built around three pillars of activity that combine analysis and advice with practical assistance and financing. Activities dictated by these pillars will be delivered through sovereign and non-sovereign lending and through non-lending and other activities.

First, the strategy aims to improve Africa's investment and business climate by supporting governments' efforts to strengthen the laws, policies, tax systems, rights, regulations and procedures that govern business, as they nurture not just their domestic private sectors, but also those of their regions. This also means helping governments fight corruption, promote financial transparency, and further develop the formal sector. The Bank will also help governments plan infrastructure investments, deepen and expand their financial and capital markets, strengthen their labor markets, and build the business skills of young people and entrepreneurs.

Second, it aims to expand business access to social and economic infrastructure. 'Hard' infrastructure (transport, telecommunications, water, power systems, and fixed assets needed to provide education, health and sanitation) and 'soft' infrastructure (legal and regulatory frameworks, payments clearance and settlement systems, financial intermediaries and capital markets, collateral registries, credit rating agencies, and skills development) are prerequisites for business as much as for society. The infrastructure gap in Africa remains huge, dramatically limiting national, regional and international trade. The Bank will continue to

finance infrastructure. It will also use its resources to attract private investment to fill the infrastructure gap, supporting both public and private sectors to do so, knowing this will galvanize business activity.

Third, it aims to promote enterprise development by helping business gain access to finance, building its skills, and helping to add value to its activities. The Bank will continue to provide financing for small businesses, using a variety of channels and ways of lending. It will also direct some of its training and mentoring work with small businesses to equip them to receive and use such money to the best effect and highest return. The Bank will also work to make sure Africans can draw the greatest benefit from their raw material products by ensuring that primary resources are managed sustainably and used efficiently, and that downstream stages of processing and production (in key areas such as extractive industries, forestry and fishing) occur in Africa. It will also invest in technology that can stimulate agricultural businesses.

An important new venture within this third pillar involves financing trade. Beyond the Bank's support to business start-ups for domestic markets, a new facility will pave the way for, and actively invest in, trade among and beyond African nations.

Mirroring the Bank Group 2013-2022 Strategy, three further priorities will apply to these pillars. Activities are to support fragile states as much as strong states – with a commitment to take risks for them where necessary and to be both flexible and versatile to achieve quick and tangible results. They are to work to empower women, as half of the workforce, to achieve their full economic potential. Finally, they are to support initiatives to sustainably manage and prudently use African agricultural potential, deal with food security and open the way for greener development.

A vibrant private sector is both an engine of growth and an agent for development through eroding poverty, strengthening communities and societies, and providing services for all. This strategy embodies the African Development Bank's development of a vision for private sector growth to drive African growth, and a plan to implement it.

01

Introduction

A vibrant private sector¹ is the engine of growth which generates decent jobs and creates increased opportunities for more inclusive and green growth. While government can empower poor people through regulation, funding and providing public goods, private initiative can also provide services and generate much-needed employment. A large and formal private sector can also be a strong advocate for policy reform and a force for good governance, establishing a virtuous circle in which an improving business environment brings private sector growth, which in turn strengthens governance reforms.

This strategy sets out the framework for African Development Bank Group (AfDB) Private Sector Development (PSD) activities for 2013 to 2017. Those activities go beyond its non-sovereign private sector operations, and include other lending and non-lending interventions, many backed by sovereign guarantee, which support private sector development. The Strategy is based on the vision of a transformative African private sector promoting inclusive and sustainable economic growth and poverty reduction in RMCs by contributing to income generation and increasing private investment

1 In this document, the 'private sector' refers to a basic organizing principle of economic activity where private ownership is an important factor, where markets and competition drive production and where private initiative and risk taking set activities in motion – based on the OECD's Development Assistance Committee's (DAC) guidelines. See, Organization for Economic Cooperation and Development. 1995. *Support of Private Sector Development*. Development Cooperation Guidelines Series. OECD. Paris.

in infrastructure, creating sustainable livelihoods for all segments, including the vulnerable.

Therefore, the Bank Group identified private sector development as a core operational priority in its Strategy 2013-2022 (Figure 1). Continent-wide consultations reaffirmed Africa's ambition to be a global growth pole. The Bank Group Strategy 2013-2022 puts the Bank at the center of Africa's transformation into a more stable, integrated and prosperous continent with competitive, diversified and sustainable economies, with the private sector at its core. The Bank believes that private sector development is fundamentally about people – releasing and harnessing their productive potential and satisfying their needs and desires, and creating pluralistic societies that provide both freedom and security. The strategy emphasizes promoting African business, local entrepreneurship, and integration into global value chains to promote economic efficiency and competitiveness, social welfare, and inclusive and sustainable growth.

1.1 Why a Strategy Now?

Africa is at an important junction. Its economies are growing faster than those of many other regions. They are growing at twice the rate of the 1990s. Following decades-long market-oriented reforms and peace across much of the continent, exports are booming and export markets have become more diversified. Africa has exhibited exceptional resilience since the

Figure 01 | Strategy 2013–2022 – Core Operational Priorities



global financial crisis began in 2008. The continent is enjoying higher savings rates, rising demand and stronger capital markets. Driven by a combination of trade and investment, Foreign Direct Investment (FDI) has increased by a factor of six during the past decade. Increasing flows of private capital to the continent offer real alternatives to Official Development Assistance (ODA).² With FDI exceeding ODA in Africa, the engagement of the private sector is key for successfully promoting the transition to green growth. There is also an emerging African middle class of several hundred million consumers. Africa's young people are embracing new technologies that provide information, opportunity and connectivity. Private entrepreneurs, many of them young, have emerged as a dynamic force for change, driving innovation and transforming outdated business models.

At the same time, Africa faces significant structural deficiencies and other challenges. The continent has deep and persistent inequalities, which can bring devastating consequences. They slowly erode the trust that holds societies together, and they undermine economic growth, productivity and the development of markets, as well as public confidence in governments and institutions. The challenge of inequality is compounded by high rates of youth unemployment, with 15 million new job seekers coming onto the job market each year. These young people are increasingly educated, with high expectations which, if unmet, could lead to social unrest. Furthermore, several of the continent's middle-income countries, especially in Southern Africa, seem to have reached a 'middle income trap' that is contributing to these challenges.

An opportunity now exists to help Africa to create millions of new, decent (productive, well-paid and secure) private sector jobs in the next decade, which could lead to sustained social and economic development. Continued political and social stability makes Africa more attractive for investors; growing intraregional trade and the creation of new regional common markets has attracted new economic partners and private investors.

A healthy and growing African private sector can

promote inclusive growth and offer opportunities for more comprehensive development efforts that value human, social and natural capital, efficiently and sustainably use ecosystem goods and services, and build resilience as countries, industries and people are become increasingly interconnected. A growing private sector can also be a major source of wealth, dynamism, competitiveness and knowledge. It can also support the overriding goal of all development assistance because jobs and more equitable distribution of incomes created by private enterprises would lead to a fairer sharing of growth's benefits among more people. Micro, small and medium-size enterprises (MSMEs) in particular can directly help in lowering poverty and integrating women and other marginalized groups into society. Private sector development can also engage Africans more actively in productive and decision-making processes that affect their lives.

A growing private sector also creates new stakeholders in the economy, bringing about a more pluralistic civil society that can lead to more accountable political systems. The combination of greater competition, market forces and the profit motive can lead to better use of Africa's human and material resources. It expands the tax base, and the potential for market-based policy instruments designed to make the best use of financial, social and environmental capital by pursuing investments that use resources more productively and efficiently.

Africa's development partners, including the AfDB, have to recognize the importance of these changes and adjust their development partnership strategies. For the AfDB, this means adopting a more focused strategy, in close coordination with others, aimed at assisting the continent build on the foundations for sustainable growth by targeting known obstacles to private sector development.

The rest of this section briefly discusses key lessons from previous private sector strategies. Section 2 presents the key features of the proposed Private Sector Development Strategy; Section 3 focuses on implementation; and Section 4 on risk and mitigation issues.

1.2 Lessons from Previous Private Sector Strategies

In January 2008, the Board of Directors approved an update of what was then the Bank's Private Sector Development (PSD) Strategy and the 3-year Business

² See Boston Consulting Group. 2010. "The African Challengers: Global Competitors Emerge from the Overlooked Continent." BCG, Boston; Paul Collier. 2010. "The Case for Investing in Africa." McKinsey Quarterly, June; and, Charles Roxburgh, Norbert Dörr, Acha Leke, Amine Tazi-Riffi, Arend van Wamelen, Susan Lund, Mutsa Chironga, Tarik Alatovik, Charles Atkins, Nadia Terfous, and Tili Zeino-Mahmalat. 2010. "Lions on the Move: The Progress and Potential of African Economies." McKinsey Global Institute.



Plan for its private sector operations (PSOs).³ Covering the period 2008 to 2010, the update built on the Bank's 2004 PSD Strategy, and was informed by the Bank Group's High-Level Panel Report, ADF-11 discussions, and preparations for the Bank's 2008-2012 Medium Term Strategy (MTS). A Mid-Term Review of that Strategy was released in 2010 to take stock of the progress in implementation and integrate lessons learned in the first two years of strategy implementation.

The 2008 PSD Strategy update set out five related priorities: improving the investment climate, supporting private enterprises, strengthening financial systems, building competitive infrastructure and promoting regional integration and trade. These areas had been identified as pivotal when the 2004 Private Sector Development Strategy was drawn up. Implementation of that Strategy concentrated the Bank's efforts on diagnostics and strategy development, enabling environment programs, and non-sovereign catalytic transactions to encourage investment from other sources of finance. These three activities aimed to improve the status of private sector in Regional Member Countries (RMCs) and to foster strong private sector-led growth in Africa.

3 The Bank Group has had PSD strategies and policies for almost 25 years, starting in October 1989 with the approval of the first Private Sector Development Strategy and Policy. The most recent Strategy dates back to 2004, and was updated in 2008 to last through 2012. See, African Development Bank Group: "Private Sector Development Strategy"; Bank Board Document No. ADB/BD/WP/90/77; September 18; 1990 (supplemented by an Addendum: Bank Board Document No. ADB/BD/WP/90/77/ Add.1; November 30, 1990). That Strategy was subsequently updated and replaced by the Revised Private Sector Operations Policies (Document No. ADB/BD/WP/94/127/ Rev.2), which was adopted by the Boards in 1995 and supplemented by the Strategy for Private Sector Operations approved by the Board in May 1996 (Document No. ADB/BD/WP96/38/Rev.1), approved by the Board in May 1996). At its meeting on 20 December 2004, the Bank Boards approved a revamped PSD Strategy, which, in response to comments and issues raised by Board members while approving the strategy, prompted Management to submit more specific clarifications (Document No. ADB/BD/WP/2004/71/Rev.1/Add.5 / Fund Board Doc. No. ADF/BD/WP/2004/81/ Rev.1/Add.5) on 26 January 2005 and updated in 2008.

Reviews of past PSD strategies have noted that while the broad priorities and operational areas have been relevant, implementation has often fallen short, often because of inadequate adoption of the PSD mandate across the Bank and insufficient cooperation between Bank Group sovereign and non-sovereign operations (Figure 2). Regarding the latter, the Bank has not always improved the development effectiveness of its private sector activities as much as possible. Stand-alone private sector operations have often had limited effect on more fundamental sector- or country-wide private sector challenges and have not fully exploited economies of scale. On the other hand, fiscal constraints and weak institutional capacity have precluded achievement of better development results through public intervention alone.

This PSD Strategy therefore takes into account all Bank Group activities that contribute to development through the private sector. In effect, this implies a need for consistent cooperation and action between its sovereign and non-sovereign windows. It also points to a need for greater coordination with various stakeholders in government, among donors, in civil society and in the private sector.

Evaluation of Private Sector Operations: Non-sovereign operations (NSOs) are an integral part of the Bank's support to private sector development through various interventions such as, direct loans, credit lines, direct equity investments, participation in private equity funds, and to a lesser extent through risk sharing facilities. From single digit levels prior to 2000, non-sovereign operations have since averaged about 30 percent of total Bank lending. Between 2008 and 2011,

Figure 02

Key Lessons from Previous PSD Strategies

Unclear corporate priorities for PSD, resulting in strategic drift;
Insufficient attention to weak institutional environment and regulatory constraints;
The need to mainstream PSD, with country and sector strategies reflecting PSD as a priority;
Insufficient coordination between the Bank's sovereign and non-sovereign operations;
The need to ensure a better balance between the Bank's objectives and risk management; and
The need for greater attention to the development of the financial sector and financial intermediation.

NSD approvals amounted to UA 4.8 billion, accounting for 30 percent of the Bank's total new commitments.

While the independent Evaluations Department has not evaluated all Bank Group private sector development activities, it recently assessed its non-sovereign operations (NSO)⁴ from 2006 to 2011⁵. The assessment found that through its NSOs, the Bank Group has generally achieved good alignment of its operations with the private sector strategy, particularly in infrastructure and the catalytic effect of its non-sovereign operations in mobilizing additional investment and funding. The Bank has also adopted industry best practices for measuring and managing risk in its private sector portfolio and has remained within defined exposure limits. The Bank has also done well in aligning staff resources to private sector operations and in developing a wide array of skills across the sectors and functional disciplines that are central to its strategy.

4 The Bank Group's NSOs include (i) private sector operations (PSOs) including the private dimension of Public-Private Partnerships (PPPs); (ii) operations by government-owned (or parastatal) enterprises, including utilities, with autonomous character and independent legal identity; and (iii) 'enclave' projects sponsored by RMCs.

5 African Development Bank. 2013. *Fostering Private Sector Development in Africa: An Independent Evaluation of Non-Sovereign Operations, 2006-2011*. Operations Evaluation Department (OPEV).

At the same time, the evaluation identified areas for NSOs requiring additional attention and made a series of recommendations. These include better handling of competing priorities; greater attention to financial sector intermediation operations, particularly through lines of credit and equity funds; widening the Bank's range of instruments; reviewing the Bank's equity portfolio to address its underperformance; and ensuring proper balance between the Bank's core strategic objectives and its risk management guidelines.

The key recommendations from the evaluation are summarized in Figure 3. It should be noted that of the eight OPEV recommendations in this evaluation, four were specific to the financial sector. Indeed, actions in the financial sector are suggested under each of the strategic pillars of this Strategy—something unsurprising given that the financial sector including banks, other intermediaries, and capital markets serve the real sectors of the economy.

Furthermore, Annex I includes several other key lessons from other reviews of the Bank Group's PSD activities, and how they have informed this Strategy.

6 For details, see management response to the Independent Review of the Bank's Private Sector Operations (PSO), 2013.

Figure 03 | Key OPEV Recommendations on NSOs⁶

Recommendation to review Bank's strategy, policies and procedures for financial sector investments, particularly intermediation through lines of credit.
Recommendation to be more selective in approving new equity investments, increase the Bank's underwriting restrictions and reduce the overall rate of growth of new interventions.
Recommendation to examine options to further refine the Bank's risk management framework without jeopardizing its financial integrity.
Recommendation to utilize a wider range of instruments at the project-level, including guarantees and trade finance.
Recommendation to adopt a more systematic approach to capacity building in client financial institutions.
Recommendation to review the Bank's ADOA framework.
Recommendation to adjust NSO strategic choices in recognition of constraints imposed by prudent portfolio risk management, to achieve a balance between core strategic objectives, strategic priorities, and risk management guidelines;
Recommendation to monitor the Bank's overall capital adequacy and the consequent headroom for further growth in private sector operations.
Recommendation to streamline NSO approval process.



The AfDB Private Sector Development Strategy (2013-2017)

Certain conditions must be in place for the private sector to thrive, encourage inclusive growth, and cut poverty by creating jobs. These conditions include rule of law; good 'hard' and 'soft' infrastructure; a stable macroeconomic environment; an educated, skilled and healthy workforce; and access to financial services. Africa's private sector also needs deeper financial markets, more access to higher education and training, and more gender equality if it is to be globally competitive, and for this to result in significantly more intra-African and external trade.

2.1 Vision and Objectives

The private sector now generates 70 percent of Africa's output, 70 percent of its investment and 90 percent of its employment. That sector, though, is still largely composed of mostly informal micro and small enterprises, with limited capacity to contribute to accelerated development.⁷ Large differences among African countries persist – much of formal employment comes from government jobs. Africa's private sector also has to contend with limited public sector capacity to regulate it effectively, a generally restrictive business environment, poor infrastructure (particularly in power and transport), serious skills shortages and mismatches, and difficulties in gaining access to finance. While the extractive industries sector has been an important driver of economic growth, such growth has not resulted in equally impressive job creation and poverty reduction. This highlights the urgent need for RMCs to transform and diversify the structure of their economies in order for such growth to be sustainable and inclusive.

This strategy envisions a competitive private sector that will be an engine of sustainable economic growth, generating a decent work environment that offers productive employment in Africa in the next decade and beyond.

Its main objective is therefore to contribute to sustainable African development and poverty reduction by promoting broad-based economic growth through effective private sector development. To help meet the objectives of

inclusive growth and transition to green growth, AfDB will aim to catalyze and leverage private sector resources. This objective is consistent with:

- the Bank's 1964 Charter, which calls for the Bank "to promote investment in Africa of public and private capital in projects or programs designed to contribute to the economic development or social progress of its regional members"⁸; and
- the Bank's 6th General Capital Increase (GCI-6) and the 12th replenishment of the African Development Fund (ADF-12) strategic goal of fostering development through the private sector.

The AfDB Group will achieve this objective by increasing as much as possible the development impact of its private sector activities by capitalizing on its track record, its comparative advantages, its unique business perspective, and lessons it has learned from previous strategies in a way consistent with its institutional goals.

2.2 Bank Group Positioning

The Bank Group has a unique position as an African organization serving Africans. Its main source of comparative advantage is its African character and its central place in the African development institutional architecture.

Established fifty years ago by independent African states to contribute to "the sustainable economic development and social progress of its regional members individually and jointly"⁹, the Bank has delivered on its mandate with over US\$100 billion in financing of projects for Africa's development, an increasing number of which focus on private sector development. The Bank Group is majority African-owned and completely focused on the continent. Through its analytical products and the knowledge of its staff, it has deep understanding of Africa's institutional history and political economy. In addition to its African

⁷ African Development Bank. 2011. *African Development Report (ADR)*. AfDB. Tunis.

⁸ Article 2, "Agreement Establishing the African Development Bank"; signed August 4, 1963 (Khartoum, Sudan).

⁹ Ibid., Article 1.

character, which ensures privileged access to, and support by, regional member states, the Bank serves as an important forum for interaction among these 54 RMCs and its 24 non-African member countries.

The Bank Group needs a clear definition of its role in assisting its RMCs if it is to contribute meaningfully to efforts to achieve broad-based economic growth, inclusive social development and gradual transition to green growth through an effective private sector. As Africa's leading development institution, the Bank has a unique business perspective based on the areas of its comparative advantage and core operational priorities, as summarized in Figure 1.

Since private sector development has to take place on a vast scale in Africa, the Bank has to refine its business model to ensure that its efforts are aligned with market forces to create conditions that support private initiative. Likewise, the Bank must systematically assess how its projects are helping private sector development, especially in coordination with other development partners in Africa.

2.3 Operational Principles

The proposed private sector strategy is anchored in the five underlying operational principles of the 2013 Private Sector Development Policy¹⁰:

- Ultimate ownership of the PSD agenda lies with RMCs;
- The Bank is selective in its interventions;
- The Bank demonstrates 'additionality' in its intended interventions;
- The Bank aims to attract other partners in its interventions; and
- Bank interventions do not compromise its financial integrity.

The PSD Strategy specifies Management's intended directions for the Bank Group on the PSD agenda over the medium term. The Strategy is guided by the PSD

Policy, but also by the Bank Group Strategy 2013-2022, evaluations by OPEV, lessons learned from past strategies, and strategic advice from Senior Management. It includes strategic pillars and operational priorities to guide Country Strategy Paper (CSP) and Regional Integration Strategy Paper (RISP) development teams, intended results and approaches to attain them, and is notably informed by Bank Group stakeholder demands. While strategic directions in it are not expected to change in the short or medium term, their progress is monitored and they may be fine-tuned or updated periodically to adjust to changing conditions. The Strategy also benefits from business plans and specific directional guidelines to guide staff in specific areas in which they work, where necessary.

2.4 Pillars and Priorities

The strategy focuses its resources on the biggest opportunities for job creation across the continent, and is built around three pillars of activity (Figure 4):

- (i) improving Africa's investment and business climate;
- (ii) expanding access to social and economic infrastructure; and
- (iii) promoting enterprise development.

In deploying interventions across these three pillars, Management knows Bank financial resources will always be a small fraction of Africa's requirements. Given Africa's enormous needs, the Bank will seek new ways to mobilize resources to support Africa's transformation, especially by leveraging its own resources. It will continue to build on and expand the size and the practical operations across both its windows of support, while exploring options for attracting new investment from emerging economies and from new funders and donors, including sovereign wealth and pension funds. The Bank Group will also use its existing instruments better, while developing new ways to ensure that each dollar it invests unlocks significantly more from other investors. Wider use of public-private partnerships, co-financing arrangements and risk-mitigation instruments will also draw in new investors.

10 The PSD Policy (ADB/BD/WP/2011/85/Rev.3 and ADF/BD/WP/2011/46/Rev.3) presents the highest level of mandatory principles proposed by Management on the Bank Group's private sector development agenda approved by the Board. The Policy also helps define the universe of acceptable areas for Bank interventions through its delineation of unacceptable areas such as speculative activities, commercially unviable projects and projects deemed illegal under host country rules or international conventions and agreements, etc. All these guide PSD strategy. However, because staff may need more specific guidance to be able to comply with the Policy in the specific areas in which they work, other types of directional statements (e.g., guidelines) may follow from the Policy, again focusing on key principles and mandatory rules. The PSD Policy is not expected to change much over time although it can be adjusted with Board approval.



Figure 04 | The AfDB Private Sector Development Strategy

VISION			
A competitive private sector, which will play a significant role as an engine of sustainable economic growth and poverty reduction in Africa, in the next decade and beyond			
OBJECTIVE			
To contribute to sustainable development and poverty reduction in Africa by promoting broad-based economic growth, employment and inclusive development through effective private sector development.			
STRATEGIC PILLARS	Pillar I: Investment and business climate	Pillar II: Access to social and economic infrastructure	Pillar III: Enterprise development
EXPECTED OUTCOMES	An enabling business climate supporting investment and the development of socially responsive enterprises	Increased access to social and economic infrastructure	A diverse, dynamic, entrepreneurial, innovative, and broad-based enterprise sector, producing goods and services for domestic and foreign consumption
OUTPUTS			
Private sector development capacities to support Regional Member Countries achieve more inclusive and environmentally sustainable economic growth, improved access to social and economic infrastructure, and enhanced competitiveness of the private sector across Africa.			
MAJOR ACTIVITIES	Support for enabling policy, legislative and regulatory environment ("soft infrastructure") for private sector development.	Assistance to regional member countries to address known and targetable "hard" infrastructure constraints to private sector development, particularly in transport and energy. Select activities in skills improvement and education.	Assistance to countries to address specific enterprise-level challenges to private sector development, including skills shortages, difficulties in accessing finance, lack of scale, value chain gaps and weakness.
KEY INSTRUMENTS	<ul style="list-style-type: none"> • Program-based operations • Technical assistance and capacity building • Economic and sector work • Project loans and grants • Policy dialogue and advisory services • Donor coordination 	<ul style="list-style-type: none"> • Project loans and grants • Technical assistance and capacity building • Economic and sector work • Program-based operations • Policy dialogue and advisory services • Donor coordination 	<ul style="list-style-type: none"> • Direct financing assistance: long-term debt, equity, guarantees, loan syndications, and underwriting • Advisory services • Technical assistance and capacity building

PILLAR 1 - Investment and Business Climate

The opportunities and incentives to invest productively, create jobs, and expand are shaped by the costs and risks associated with the business and investment environment, and other non-physical barriers to competition. Efficient and well-regulated public services, effective law enforcement, and transparent procurement practices all contribute to a better investment and business climate, and faster growth and development.

KEY CHALLENGE – RESTRICTIVE BUSINESS ENVIRONMENT

Africa's investment and business climate is characterized by a wide range of regulatory and labor, trade and business obstacles that reduce competitiveness and constrain the private sector. These obstacles are seen in two ways: first, through inconsistent policies at the macro and sector levels and in each sector (regulation and taxation, stability and security, finance, labor skills development, infrastructure); and second, through diminished credibility, public trust and legitimacy for governance institutions, and an absence of channels for wide participation in policy formulation. Despite wide variations across Africa, these structural deficiencies often result in bureaucratic red tape, poor control of rent-seeking and lack of transparency, all of which significantly reduce the credibility of public policy and administration, and hinder governments' enabling role (see Figure 5). Where corruption is a threat, businesses prefer to remain unregistered to escape what they see as predatory policies. This makes for a difficult business

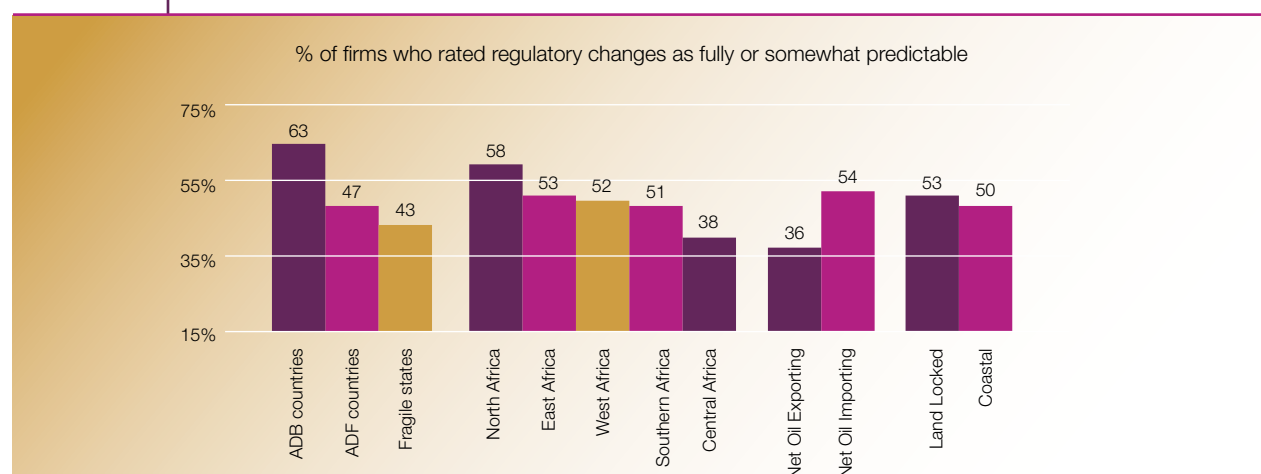
environment across Africa for large and small enterprises alike, compared with other parts of the world.

Africa's underdeveloped financial markets present further investment and business barriers to private sector development. African formal financial systems and capital markets are embryonic and face problems of scale, volatility, long-term liquidity, and macroeconomic and regulatory stability, and are perceived as risky by outsiders. Current global financial uncertainty is a complicating factor, as are increasing economic risks in the wake of the 2008-2009 global financial turbulence, which have led to much more expensive short-term commercial financing, especially in trade finance. Access to long-term credit is even scarcer on the continent. The flow of credit to the private sector also remains below other developing regions' levels. Close to half of Africa's small businesses report that gaining access to financial services is a major constraint. Only 22 percent of African companies hold a loan or a line of credit from a financial institution, compared to 31, 47, and 48 percent in developing parts of Asia, America and Europe, respectively.¹¹


Furthermore, Africa's financial infrastructure is generally in nascent stages of development. Financial infrastructure comprises a set of market institutions, networks and shared physical infrastructure that enable the effective operation of financial intermediaries, the exchange of information and data, and the settlement of payments between wholesale and retail market participants. Credit bureaus, collateral registries and credit rating

11 African Development Bank, 2011. *African Development Report (ADR)*. AfDB. Tunis.

Figure 05 | Predictability of Regulatory Changes



Source: Staff calculations based on enterprise survey data, 2010.



systems are only beginning to be developed in several African countries. On a cross-regional comparative basis, sub-Saharan Africa has the least developed payment and settlement systems, with many economies predominantly cash-based, and several countries still using manual check processing and clearing houses.

Finally, Bank research reveals an acute mismatch between the skills young people bring when they leave the education system, and those that are sought in labor markets, particularly in the private sector.¹² This points to the poor quality of education, and a disconnect between education systems and employers. At the tertiary level, young Africans are confronted with university systems that have traditionally focused on educating for public sector employment, with little regard for private sector needs.

GOING FORWARD – OPERATIONAL PRIORITIES

The Bank will work with partners (government, development partners, the private sector, civil society, and others) to help RMCs address key structural business and investment climate challenges. Specifically, it will:

- Support policy initiatives that champion reducing the attraction of informal-sector activities by supporting improvements to increase the ease of doing business and reduce the cost of business creation, expansion and closure. In particular, it will support initiatives promoting greater transparency, predictability and accountability in business and investment regulatory frameworks¹³, particularly in tax policy and administration; strong property rights; and sound corporate governance;¹⁴
- Support initiatives to deepen and expand financial and capital markets, including those that encourage creation of a diversity of financial institutions and services (e.g. insurance, leasing), development of financial instruments (e.g. bonds, equities, guarantees) that can mobilize term finance, and efforts aimed at increasing local currency borrowing to fund private sector projects;

12 African Development Bank et al. 2012. *Africa Economic Outlook* (AEO). AfDB. Tunis.

13 See, joint AfDB-OECD report that focused on legislation, policies and practices to combat bribery of public officials in business transactions in 20 African countries, "Stocktaking of business integrity and anti-bribery legislation, policies, and practices in twenty African countries," OECD. Paris.

14 This also includes Anti Money Laundering/Combating the Financing of Terrorism initiatives, for which the Bank has a strategy. (see *Bank Group Strategy For The Prevention Of Money Laundering And Terrorist Financing In Africa* ADB/BD/WP/2007/70 and ADF/BD/WP/2007/46).

- Support initiatives to improve Africa's financial infrastructure including collateral registries, credit bureaus, credit ratings, and payment and settlement systems, all of which are necessary to foster financial stability and the successful operation of modern integrated financial markets;
- Support initiatives to improve innovation, entrepreneurship, knowledge and skills, particularly through providing assistance to more effective vocational training;
- Facilitate policy dialogue between regional, national, and, where necessary, sub-national private sector stakeholders;
- Support initiatives that improve the institutional and operational frameworks for public-private partnerships (PPPs); including strengthening the analytical capacity for their selection, evaluation and monitoring, as well as transaction-level project preparation; and
- Assist in strengthening regional economic communities and national authorities to encourage and support regional financial sector integration, cross-border investments, elimination of non-tariff trade barriers, the harmonization of investment and engineering codes, and quality assurance and certification standards

Under this pillar, the most significant Bank instruments are Policy-Based Operations (PBOs), through which the Bank supports policy reforms in RMCs. In the spirit of the Paris Declaration, these policy reforms are agreed upon in conjunction with governments and other development partners. Accordingly, the relatively wide range of operational priorities under this pillar reflect the impracticality of identifying ex-ante which aspects of PSD-related policy reforms the Bank will support and which it will not as part of a collective effort to support reforms.

Accordingly, the set of operational areas outlined above will allow the Bank's Sector Departments and Country Teams to tailor Bank interventions to country and sub-regional circumstances in cooperation with other development partners and stakeholders. The Bank will take a leadership role where it has a comparative advantage, while letting others lead elsewhere.

Another significant instrument for use under this pillar will be the Bank's Institutional Support Projects (ISPs),

which provide capacity building and technical assistance to institutions that support private sector development in RMCs. The ISPs complement policy reform measures supported under PBOs and allow the Bank to deploy more focused resources at the request of RMCs.

PILLAR 2 -

Access to Social and Economic Infrastructure

‘Efficient economic infrastructure’ means the facilities with which a country or a region makes business activity possible (communication, transportation and distribution networks, financial institutions and markets, energy supply systems, etc.). This is critical to tackling some of the greatest impediments to private sector development in Africa. It includes social infrastructure – a subset of the infrastructure sector, which typically deals with assets that accommodate social services such as health and school facilities, as well as the systems that underpin them. Since Africa is one of the world’s fastest-growing economic hubs, meeting the demand for, and increasing access to, key infrastructure is a priority in increasing market size, deepening regional integration, and lowering prices through economies of scale.

KEY CHALLENGE – LIMITED ACCESS TO PHYSICAL INFRASTRUCTURE

One of the main impediments to development of Africa’s private sector and to its socioeconomic transformation is the lack of physical infrastructure. Moreover, existing infrastructure is often outdated and poorly maintained. African markets are still largely inaccessible because of poor infrastructure and connectivity. Poor road, rail and harbor infrastructure adds 30 percent to 40 percent to the costs of goods traded among African countries (see Figure 6).¹⁵ In transport, there are specific, logistics-related challenges continue to generate costly inefficiencies above physical infrastructure, including: the efficiency of customs and border management clearance; the ease of arranging competitively priced shipments; the competence and quality of logistics services; the ability to track and trace consignments; and the frequency with which shipments reach consignees within scheduled or expected delivery times. The bad state of Africa’s electricity, water, road and information and communications technology (ICT)

infrastructure imposes high costs on industries, reduces competitiveness, and restricts access to local and international markets. In so doing, it reduces national economic growth by two percentage points every year, and cuts business productivity by as much as 40 percent.¹⁶ In energy, at least 30 countries report regular power shortages and many others face power outages with varying frequency. This limits growth prospects for firms of all sizes. However, MSMEs are particularly affected because they usually cannot invest in their own electricity generation. Africa has 15 percent of the world’s hydro-power potential, and less than 10 percent of the continent’s share is currently tapped. There is also significant potential in renewable sources of power such as solar, wind, biomass and geothermal energy.

The lack of infrastructure is a significant obstacle to the growth and development of the private sector, and results in a low level of intra-African trade and trade with the rest of the world. Africa accounts for 12 percent of the world population, but generates only insignificant proportions of global GDP and world trade.

Infrastructure development is closely tied to the story of the continent’s resource and commodity endowments. Significant resource discoveries in recent years – for example, oil and gas in East and South-East Africa, as well as the huge demand, particularly from Asia, for agricultural and natural resources including minerals such as iron ore, platinum, coal and copper – are driving the need for infrastructure. In turn, Africa’s economic growth continues to be driven by the investment in the infrastructure needed to extract and transport these resources to global markets (rail and port infrastructure). Some RMCs have begun to consider ways of linking new infrastructure connected to these endowments with other markets, for instance in dual-purpose railways for transporting both ore and agricultural produce.

Africa’s rapid population growth also places enormous strains on existing, and often outdated and poorly maintained economic and social infrastructure. In fact, in many countries, infrastructure limitations constrain productivity at least as much other institutional challenges as weak governance, complex regulation, and lack of access to financial services. This is especially true in the power and logistics industries as well as physical infrastructure for the delivery of healthcare and basic education.

¹⁵ Infrastructure Consortium of Africa (ICA). 2005. *Africa’s Infrastructure: A Time for Transformation*. World Bank. Washington, DC.

¹⁶ Ibid.



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In addition to the lack of physical connection between countries, there is also very limited integration of regional markets for infrastructure services, particularly, in power, energy, telecommunications, transport, water and sanitation. This is in part due to weak regional economic communities that are not structured to make necessary regional investments. More significantly, governments have also not worked enough with the private sector and others to develop and upgrade regional infrastructure (particularly in communications and transport); improve policies for industries that fit the productive capabilities of countries in Africa (for example, in agriculture and food security); and fully implement protocols of the Regional Economic Communities that governments have signed.

In addition, significant obstacles remain to the mobilization of private financing and investment in infrastructure.

The costs of overhauling Africa's infrastructure needs are estimated at about US\$100 billion a year over the next decade.¹⁷ Two-thirds of that is required for entirely

new infrastructure, and the rest for the maintenance of existing infrastructure. Only about US\$25 billion a year is currently being spent on capital expenditure, leaving a substantial shortfall. New and innovative financing will be needed to address this gap.¹⁸

GOING FORWARD – OPERATIONAL PRIORITIES

Support to Africa's infrastructure – the essence of this pillar – is at the core of the Bank's work and is an area where it has a comparative advantage. The Bank Group's Strategy 2013-2022 envisages scaling up infrastructure investments substantially via both its sovereign and non-sovereign windows, and particularly in the areas of transport, energy, water and sanitation, all of which have been identified by African companies and governments as posing the biggest challenges for the continent's transformation.

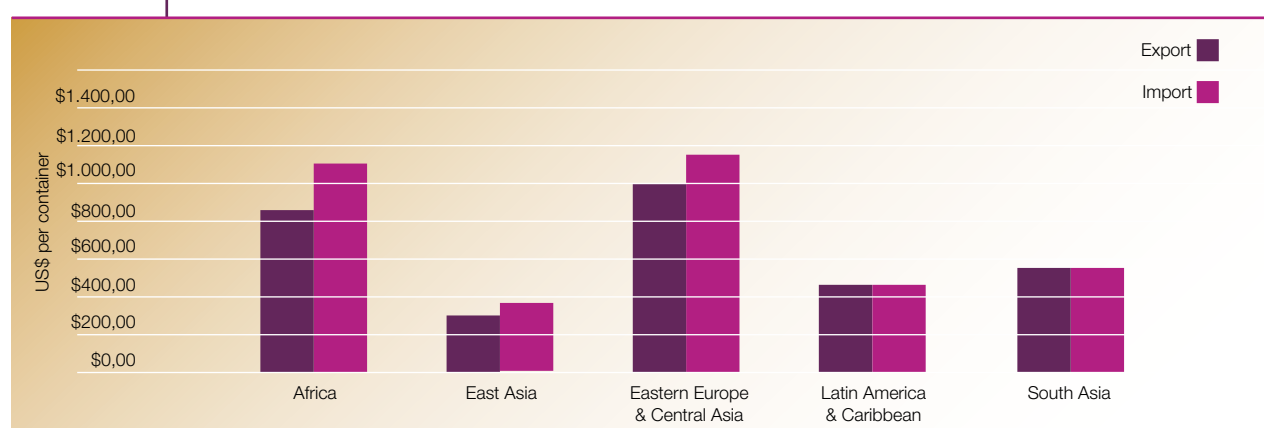
Under this pillar, the Bank will support RMCs mainly in their infrastructure development priorities as expressed in their long-term development strategies and, at the regional level, as expressed in the African Union/New Partnership for Africa (NEPAD) Program for Infrastructure Development in Africa (PIDA). Bank interventions will help RMCs increase their productivity and competitiveness, deepen physical, economic and social integration, and create greater opportunities for promoting inclusion and contributing to sustainable economic transformation. Specifically, it will:

- Support new infrastructure or rehabilitation initiatives aimed primarily at improving long-term and comprehensive reforms and investments across transport and logistics chains, reducing travel time

17 World Bank. 2005. The African Infrastructure Country Diagnostic. World Bank. Washington DC.

18 African Development Bank 2011, 'Closing Africa's Infra-structure Gap: Innovative Financing and Risk', AfDB Economic Brief.

Figure 06 | Inland Transport Costs



Source: Larossi, G. 2009. "Benchmarking Africa's Costs and Competitiveness". Africa Competitiveness Report 2009. World Economic Forum, AfDB

between regions, improving access and delivery of social services, integrating national markets and connecting them to regional markets and markets outside Africa¹⁹;

- Support to initiatives aimed at strengthening access and capacities to deploy efficient and/or climate-proof infrastructure systems, including multi-modal transport systems, which can also offer ways to manage urban growth, while reducing the overall ecological footprint;
- Support initiatives for meeting Africa's rising demand for energy, with an emphasis on clean energy and energy efficiency, or other types of projects that can help RMCs exploit 'green' opportunities;
- Support private infrastructure and public-private partnerships through direct and indirect financing instruments, and through provision of technical assistance and transaction advisory services;
- Support initiatives for strengthening the potential for RMCs to take advantage of the opportunities to benefit from export-oriented growth based on the development of effective export processing zones (EPZs) based on coordinated packages of non-distortionary incentives, infrastructure and services attractive to investors; and
- Boost the Bank's analytical and advisory capabilities in maintaining its leadership role in continental infrastructure initiatives, such as the NEPAD and the Infrastructure Consortium for Africa.

In order to accelerate progress in all the areas mentioned, there is need for a more systemic and partnership approach to increase private investment, create more sustainable jobs, transfer new technologies and skills, and realize Africa's true economic and human potential over the next few decades.

PILLAR 3 - Enterprise Development

Further challenges relate to issues directly affecting the operations and growth of private enterprises, and

especially MSMEs. Under this pillar, the Strategy restricts its focus on three broad priority areas – access to finance and financial services; entrepreneurial and business operation skills; and access to technology, innovation, and value chain linkages – all of which present challenges for African enterprise-level PSD.

KEY CHALLENGE – ACCESS TO FINANCIAL SERVICES AND THE SUPPLY OF LONG-TERM CAPITAL

Africa's private enterprises – including an estimated 70 percent of Africa's approximately 50 million MSMEs – are severely hampered by insufficient access to long-term finance (see Figure 7).²⁰ Even large African enterprises routinely experience financing constraints.²¹ Such underfunding has led to significant underinvestment, particularly in capital goods such as machinery and equipment, as well as in research and development. In turn, this has contributed to low levels of innovation, productivity and competitiveness.²²

African traders, particularly current and potential exporters, face severe difficulties securing trade finance. When financing is available, costs are often prohibitive and duration is often short, especially for MSMEs. Despite Africa's trade having more than tripled in value in the last decade (US\$1.2 trillion in 2010), there is an acute shortage of trade finance in Africa, mostly because of local financial institutions' lack of financial and technical resources and an incomplete perception of risk by international banks.

Financing constraints vary within countries and across Africa, as well as by firm size. The differences reflect difficulties in gaining access to funding from formal financial institutions, either because of companies' inability to present bankable proposals, or financial institutions' reluctance to extend credit to MSMEs.

Deep and durable solutions to the challenges of access to financial services and the supply of medium- and long-term capital in Africa need to incorporate all available instruments, including lines of credit, equity and related

¹⁹ This includes regional initiatives such as the Program for Infrastructure Development in Africa (PIDA).

²⁰ T. Beck, S. Munzele Maimbo, I. Faye, T. Triki. 2011, *Financing Africa, Through the Crisis and Beyond*, African Development Bank. Tunis.

²¹ Ibid.

²² World Economic Forum, World Bank, and African Development Bank. 2011. *The African Competitiveness Report 2011*. World Economic Forum: Geneva; Gebreeyesus, M. 2009. "Innovation and Microenterprises Growth in Ethiopia." UNU-WIDER Research Paper No. 2009/51; and Onyeiwu, S. 2011. "Does the Lack of Innovation and Absorptive Capacity Retard Economic Growth in Africa?" UNU-WIDER Working Paper No. 2011/19.

instruments, agency lines, risk-sharing, guarantees, and technical assistance. Action should be taken at all relevant levels, in firms and in financial institutions, nationally and globally.

GOING FORWARD – OPERATIONAL PRIORITIES

The Bank will develop a more holistic approach to financial sector competitiveness and inclusivity in ways that align with country contexts and the capabilities of the local financial sector in deploying interventions that encompass:

- Partnering with financial institutions (commercial and development finance institutions including banks, private equity funds, etc.) to facilitate intra-Africa investment and trade and also, to enable them to give better service to MSMEs, traders (see Box 1) and women;
- Working with governments and the private sector to establish technology-based business models to help the ‘unbanked’ and the ‘under-banked’;
- Supporting initiatives that involve working directly with individual MSMEs to improve their creditworthiness, financial literacy and growth potential;
- Support for direct financial assistance to enterprises through catalytic, long-term debt and equity, guarantees, loan syndications and underwriting, particularly initiatives in agribusiness, industrial modernization, extractive industries (mining, oil and gas) as well as regional integration and support mechanisms (social infrastructure, financial instruments, etc.) for local communities;

- Support for initiatives to increase the responsiveness of private financial institutions to the increasing demand for long-term debt, by continuing to extend credit lines and risk-sharing instruments to enable FIs to on-lend to their clients;

- Attracting global leaders’ attention to the issue of strengthening the financial sector in Africa; and

- Developing specific guidelines to support MSMEs and to ensure that financial intermediaries are accountable for the deployment of Bank funds for purposes intended.

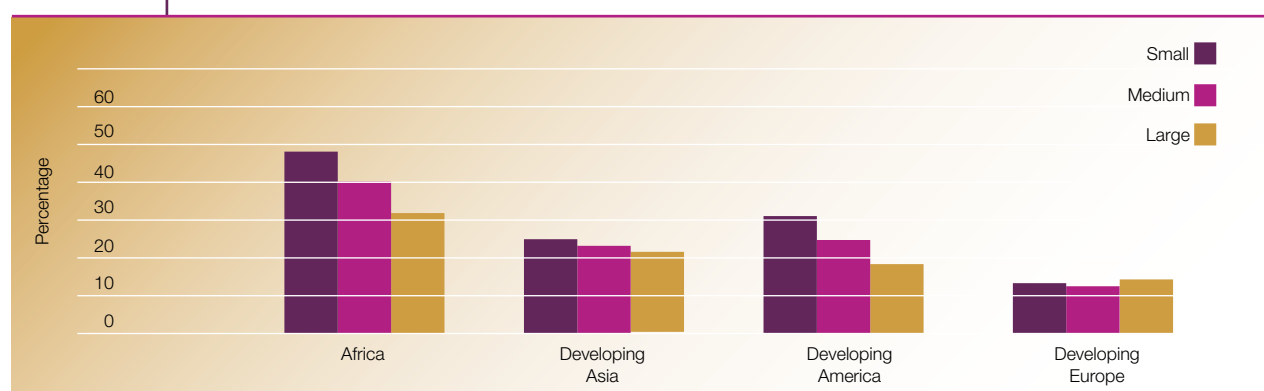
In light of the importance of the financial sector in both the Bank’s overall Strategy for 2013 – 2022 as well as in this Strategy, the Bank is undertaking a comprehensive review of its approach to the financial sector, which will lead to the preparation of a new Financial Sector Development Policy and Strategy to replace the 2003 Financial Sector Policy.

KEY CHALLENGE – SPECIFIC OBSTACLES FOR MICRO, SMALL, AND MEDIUM-SIZE ENTERPRISES

Africa’s private sector is largely comprised of MSMEs, with people becoming small-scale entrepreneurs out of both desperation and aspiration. MSMEs are often very small, informal, family-based enterprises, or sole proprietorships, which can terminate quickly. Many are run by individuals with no other opportunity for gainful employment, and who rely on these activities to survive or supplement in-kind earnings from subsistence farming.²³ Such entrepreneurs are often untrained, and they lack crucial market information. All entrepreneurs,

23 African Development Bank. 2011. *African Development Report*. AfDB. Tunis.

Figure 07 | Percentage of Firms Identifying Access to Finance as a Major Constraint



Source: Staff calculations using enterprise survey data, 2010.

however, face obstacles to growth, such as under-capitalization and capital structures, lack of collateral, a severe skills shortage (including financial literacy), weak market linkages, as well as the widespread lack of business development services and networks. Women entrepreneurs also often have to contend with legal impediments, and restrictions on access to institutions, and using and owning property, which inhibit their access to credit, gaining employment or dealing with taxes.

Between 2008 and 2012, 34 percent of all approved Bank Group NSD financing targeted MSMEs directly and the Bank intends to scale up support to MSME development in Africa. At the same time, it recognizes the constraints of retail-type operations, which may not be cost-effective and in the Bank's comparative advantage. Its approach will be aimed primarily at strengthening skills and business linkages, as well as the provision of financial assistance. It will also further specify the objectives, business models and resource requirements associated with financial inclusion (micro and self-employment enterprises), and enterprise development (growth and opportunity-driven entrepreneurs).

To be more effective in its interventions in this area, the

Bank will develop a robust definition of MSMEs that would be included in its Guidelines for Non-Sovereign Operations (currently being drafted) so as to better classify and monitor interventions intended for MSMEs as well as maximize their development impact. This would be done in consultation with the country authorities.

GOING FORWARD – OPERATIONAL PRIORITIES

Specifically, the Bank Group will:

- Review, and where necessary adjust the framework for supporting micro-finance investments and programs, particularly those aimed at entrepreneurship development. Under its Microfinance Policy²⁴ and in line with the Strategy 2013-2022, the Bank Group is committed to supporting the development of improved access to financial services across Africa, particularly for small-scale economic operators and low-income households that are not well served by the conventional banking system;

24 African Development Bank Group (2006): *Microfinance Policy and Strategy of the Bank Group*; Board document codes ADB/BD/WP/2006/06/Rev.1/Approved, and ADF/BD/WP/2006/08/Rev.1/Approved; June 12, 2006; Executive Summary, paragraph 9.4, and Sections 4.4 and 4.5.

Box 01 | Scaling Up Work in Trade Finance

The Bank's new Trade Finance Program (TFP) will address persistent market constraints in terms of the availability of risk limits and liquidity for trade in Africa. These are exacerbated by the continued stress in the global banking markets, particularly in Europe, as well as the conservative impact of the Basel III banking regulations. Because there is relatively low risk – and historically low default rates – in the trade finance sector, the TFP is expected to be the lowest-risk capital-consuming instrument in the Bank's private sector operations, and to have a positive overall impact on the risk profile of the Bank's portfolio by balancing other higher-risk operations.

The Bank will also focus on business-enabling environment issues that are primarily targeted at trade facilitation by collaborating with Africa's regional economic communities (RECs) to harmonize financial policies and regulations at the national and regional levels, as a way of facilitating cross-border financial transactions and enhancing cross border trade. Key activities include:

- non-operational aspects of trade finance (to address the challenges of access to finance faced by African financial institutions and MSMEs);
- export promotion and investment support services (to address some of the major challenges of inter- and intra-regional trade, cross border investment and domestic investment); and
- commodity market/exchange support activities (to address problems hindering development of profitable agricultural value chains).

From a development perspective, the Bank's trade finance program is expected to help the growth of African economies. The TFP will use a number of instruments to help the Bank support small and medium-scale enterprises, sectors such as agriculture and manufacturing, and low-income countries.

Over the initial 4-year business-plan period, the TFP aims to support over US\$11 billion of African trade, involving about 8000 SME transactions covering more than 110 local financial institutions in at least 30 RMCs.



- Fine-tune its support to MSMEs through financial intermediaries (Box 3), especially given the OPEV evaluation which concluded that the Bank could do more;
- Enhance its support to technical assistance initiatives aimed at the provision of financial services to the MSME target markets, as well as those meant to ensure that the non-financial needs and requirements of MSMEs are addressed. The latter include measures to enhance the enabling environment and capacity-building support to local intermediaries that provide assistance to MSMEs, such as Business Development Services and linkages to markets;
- Support initiatives that systematically create opportunities to link local enterprises into the supply chain of international enterprises through subcontracting, licensing, franchise arrangements and public sector and development partner procurement policies;
- Support initiatives that provide enterprises, including MSMEs, with incentives for promoting technologies and knowledge leading toward greener industrial products; and
- Deepen its partnerships with others involved in MSME development in Africa, including co-financing technical assistance programs with the International Finance Corporation, L'Agence Française de Développement, USAID, DFID, AMSCO, PEP-Africa, UNIDO, ILO, IFAD and others.

In addition, the Bank will explore other options aimed at scaling up and leveraging financing and services for MSMEs, supplemented by guarantees and insurance mechanisms, such as the African Guarantee Fund and the Bank's Trade Finance Initiative, to encourage the continent's financial institutions to increase their exposure to MSMEs.

The Bank will also explore ways to support new initiatives that can promote inclusive economic growth and social development. Of significant potential are social enterprises and social businesses.²⁵ These companies

can be an effective way of fostering social innovation, entrepreneurship and value chain development. They can also be combined with microfinance to broaden effectiveness, development impact and sustainability.

However, because social businesses are still largely untested in Africa, Bank assistance will focus on providing demonstration effects, and on helping to incubate the first wave of African social businesses, such as the pilot programs in Tunisia, Togo and Uganda. These pilots will deepen understanding, help foster institutional environments and help establish financial vehicles (e.g. revolving funds) to assist social enterprises. The Bank will also consider direct financing, funding for incubators, awareness raising, technical assistance and capacity building to commercially viable social business schemes.

Lastly, the Bank will ensure that its actions stress equitable distribution of risk and reward among private sponsors, governments and communities; encourage technology transfers and industrialization; and foster the involvement of home-grown enterprises in these sectors, including through joint ventures and by using local suppliers of goods and services in the enterprise supply chain.

KEY CHALLENGE – WEAK VALUE-CHAIN LINKAGES

Sweeping economic changes during the last half century have provided a huge opportunity for Africa to emerge as a global economic power. To unleash its potential, especially given the new spirit of an Africa on the rise, African countries must embark on a bold transformation driven by massive industrialization to address youth unemployment, poverty, and gender disparities. There is a real opportunity, for example, for African countries to create jobs and promote economic transformation through a commodity-based industrialization process, capitalizing on the continent's resources, high commodity prices, and opportunities presented in the changes in the structure of global production. Exploiting Africa's commodities for industrialization involves adding value to soft and hard commodities and developing forward and backward linkages to the commodity sector.

Value chains allow widely separated producers, processors, buyers, sellers, and consumers to add value to products and services as they pass along the chain. The African private sector is mainly concentrated in the chain's less lucrative segments, with limited scope

²⁵ The main difference between social businesses and social enterprises is that, while they both may make profits, the former is created for a social benefit rather than private profit. Lenders and creditors in a social business may recoup their initial investment, but all further profits are re-invested into that or other social businesses targeting particular social objectives. Social enterprises, meanwhile, may or may not re-invest further profits.



for economic diversification. This is especially the case in agriculture and extractive industries.

Value chain development is critical for strengthening Africa's ability to capitalize on its resources, for integrating African enterprises into regional and global production value chains, and for African industrialization and agricultural transformation. By understanding the

interactions between the different players, it is possible for private and public agencies (including development agencies) to identify ways to increase efficiency and thereby value, and to strengthen the ability of those along the chain to increase their share of the total value.

In supporting agro-industrial and other value chains, the Bank will take care not to substitute for local

Box 02 | Fine-Tuning Interventions via Financial Intermediaries


A substantial proportion of the Bank Group's direct private sector lending is channeled through financial intermediaries (FIs) including commercial banks, micro-finance institutions, private equity funds, regional and national development banks, and insurance and leasing companies. The Bank utilizes FIs as channels to reach projects and entities that are either too small for the Bank's originating and supervision capacity or whose financing needs are better addressed by private intermediaries. This also contributes to the strategic objective of building the depth and breadth of the financial system. Under current financing arrangements, the Bank does so along the following lines:

- It provides capital, in the form of debt or equity or risk cover in the form of guarantees to an FI, which invests the funds in multiple sub-projects;
- It appraises eligibility for Bank financing on the basis of a pre-identified pipeline of projects;
- It does not predetermine the exact use of funds beyond requiring broad geographic, enterprise segment or type, and sectoral parameters;
- It does not select, appraise, or monitor the private firms that ultimately receive its funds, but rather delegates this function to respective FIs; and
- It requires FIs to periodically report on the financial performance of sub-projects, on development results and the enterprises/projects supported, and to report serious contraventions of environmental and social standards, as part of its legal agreement.

Delegating most operational decisions to the respective FIs and relying on an ex ante pipeline of projects, without necessarily clearly defining the development objectives of the Bank Group's investments, has meant institutional procedures have sometimes not been sufficiently adapted to intermediary financing. This is partly reflected in weak self-reporting by FIs and has often meant inadequate monitoring of the Bank's investment portfolio, which does not adequately capture the development results that are sought by the Bank.

As stipulated in the PSD Policy, the Bank Group will fine-tune its guidelines to investments which are channeled through financial intermediaries by:

- Conducting a thorough evaluation of institutional models that support the various target groups and sectors to determine what works, what lessons have been learned, and how to measure the impact of interventions. In this regard, Management will examine the prudence of, and where necessary, adopt specific guidelines by some Development Finance Institutions (DFIs) that either target or exclude certain sectors, require FIs to match the tenor of the financing provided, restrict the minimum and maximum size of sub-loans to ensure access for specific beneficiaries, or even require FIs to apply certain environmental and social standards.
- Developing better definitions for its areas of support, to be included in Project Appraisal Reports, and including specific requirements on support for strong, locally and regionally owned institutions; having a clear and credible strategy for under-served segments, regions and sectors (including having clear mandates with a focus on sustainable development and finance for the poor); having strong socio-economic safeguards in line with the Bank's Integrated Safeguards System (ISS); and acting as responsible taxpayers.
- Strengthen the capacity of FIs (particularly, local and regional ones) by scaling up technical assistance packages to FIs aimed at strengthening their business and financial management practices (e.g. portfolio management, risk management, environmental policies, and corporate governance). In this regard, the Bank will work with client FIs to build up their compliance with environmental and social standards.
- Develop adequate mechanisms to ensure that the Bank group support actually reaches intended beneficiaries (e.g., MSMEs) in order to ensure that FIs are accountable for the deployment of Bank funds for purposes intended.



entrepreneurs, will work within existing commercial initiatives and will avoid establishing new marketing channels that are unsustainable, even if they offer fairer terms for target beneficiaries during the project life span. Care will be taken to avoid creating competition with existing business and other services, unless their viability and sustainability is certain. In addressing market imperfections, particular emphasis will be paid to changing uncompetitive and inefficient processes and behavior. The Bank will support new initiatives aimed at the development and strengthening of value chains particularly in extractive industries, agriculture, forestry and fisheries, but also in other niche areas such as education and medical research hubs, pharmaceuticals, and medical devices.

GOING FORWARD – OPERATIONAL PRIORITIES

Working with other organizations where possible, Bank assistance will focus on:

- Intra-regional investments and export value chains to promote the full benefit of regional supply chains, while taking into account country and regional differences;
- Improvements in market access for small farmers and MSMEs, as well as those aimed at developing their skills as agribusiness entrepreneurs with an eye toward becoming venture capitalists;
- Improving the capacity of Africa's producers, particularly manufacturers and related industries, to compete with imported products in local markets, and helping to link them to regional and international markets;
- Ensuring access to information and knowledge;
- Developing local skills and technological capabilities among firms linked together as part of a value chain; increasing the depth of local linkages by targeting skills development, technological capabilities, access to capital, and buyer–supplier cooperation along the value chain; engaging lead commodity firms to promote local linkage strategy, including procurement, sourcing, and processing, and promote the emergence of local lead firms;
- Supporting technology and skills transfer, as well as the movement of skilled labor within Africa, by facilitating private investment across borders;
- Capitalizing on the Bank's significant direct and indirect financing of large-scale enterprises and projects – including to state-owned entities, joint public-private ventures, and foreign and domestic entrepreneurs – to demonstrate how their operations can spur the continent's industrial transformation, and in turn, create socioeconomic benefits for a large number of Africans; and
- Linking value chain development with green growth criteria (resource use efficiency/sustainability/resilience) and promoting public private partnerships, particularly in upstream dialogue on enabling conditions for private sector development as well as in promoting particular private sector investments, e.g. by helping to lower investment risks.

2.5 Areas of Special Emphasis

The Bank Group's Strategy 2013-2022 highlights three cross-cutting priorities which are crucial to the ultimate success of the Bank Group's PSD agenda: *fragile states*, *agriculture and food security*, and *gender*.

Fragile States

As part of its inclusive growth agenda, the Bank has made strong commitments to the continent's fragile and conflict-affected states, central to Africa's development agenda in the Bank Group Strategy 2013-2022. Based on the experience of the Bank Group's Fragile States Facility (FSF), which provides supplementary resources for sovereign operations in those fragile states that otherwise receive smaller ADF Performance-Based Allocations (PBAs)), international good practice and commitment to the New Deal for Engagement in Fragile States (Busan 2011) the Bank Group aims to transform the way it engages with Africa's fragile and conflict-affected states on private sector development issues. It seeks to ensure that these countries can also benefit from resources in the Bank's non-sovereign window, taking into consideration its risk management framework. These changes are part of a broader agenda to improve the absorptive capacity of these countries while maximizing results.

The current review of the Bank's Group's strategy for Fragile States provides a strong entry point to refine the institution's approach to PSD through a fragility lens. For both sovereign and non-sovereign operations, supporting PSD in fragile states presents significant operational challenges, which require adjustments

by the Bank Group of its generic approach to fragile countries. In practical terms, this will involve more informed risk-taking, nimbler operational responses including the development of innovative instruments by the Bank Group, more hands-on implementation support, and new approaches to measure results in fragile and conflict-affected states – all based on the accumulated experience of the Bank.

To this end, the Bank will make greater use of the wide range of instruments to better tailor operational support to be effective in these situations. These include strengthening support toward better business- and investment-enabling environments, taking into account the challenges and opportunities in each of these states (Pillar I). They also include greater innovation in undertaking Bank-financed private sector operations through use of innovative risk mitigation instruments such as partial risk guarantees that provide private sector investors with comfort on the contractual undertakings of governments or state-owned entities (Pillar III).

As part of the ADF 13 replenishment, and at the request of Deputies, Management has received endorsement for two new financial instruments for the ADF to enable the Bank to prudently stretch its risk capital in more risky countries – and notably fragile states.²⁶ Elsewhere, the Bank will also make greater use of multi-donor trust funds to mobilize and align donor support; support to non-sovereigns and sub-national entities that may have capacities (and trust) that central governments are still developing; greater use of existing programmatic instruments to finance infrastructure rehabilitation and basic service delivery (such as joint sector support and multi-year program-based operations).

Agriculture and Food Security

In Africa, the agriculture sector is essential for growth, poverty reduction, and food security. More than half of rural employment in Sub-Saharan Africa consists of self-employed farmers, many of whom are women. Agriculture contributes 13 percent to Africa's GDP, and GDP growth originating in agriculture is about four times more effective in reducing poverty than GDP growth originating outside the sector. It is also the largest source

of foreign exchange, accounting for about 40 percent of the continent's hard currency earnings; and the main generator of savings and tax revenues. The sector also remains the dominant provider of industrial raw materials with about two-thirds of manufacturing value-added in most African countries being based on agricultural raw materials. Agriculture supports some 70-80 percent of the total population in Africa, including 70 percent of the continent's extreme poor and undernourished. This means labor-intensive growth in the sector holds much promise for poverty reduction. Long-term investments aimed at boosting agricultural productivity will contribute to inclusive growth by creating employment opportunities for women and youth. Likewise, the agricultural sector is crucial for finding paths to development that will ease pressure on natural assets while managing environmental and socioeconomic risks better.

The Bank, by investing in rural infrastructure (rural roads, irrigation, storage facilities, access to markets, conservation systems and supply networks), its areas of comparative advantage, will help improve agricultural productivity, which is one of the most effective ways to drive inclusive growth, reduce poverty, and increase employment. Wherever possible, the Bank will also support initiatives for building resilience to climatic shocks like droughts, promoting efficient and sustainable use of land, forest, water and other natural resources, and providing sustainable infrastructure. Unlocking Africa's agricultural potential and tackling food insecurity will require sustained coordinated investment using an integrated value-chain approach. While these interventions may be initiated by the public sector, there is need for increased linkages with the private sector, by promoting PPPs in agricultural projects and programs. The Bank will therefore continue its support as a financier of private investment in agriculture agribusiness and agriculture value chains (working both directly and indirectly with private sponsors in the sector).

Gender

The Bank Group's Strategy for 2013-2022 reaffirms the Bank's commitment to gender equality as essential for economic progress and sustainable development. It states that gender equality is not only part of an inclusive growth strategy but also an area of special emphasis for the Bank, particularly as related to private sector development.

Learning from past successes and failures, the Bank

26 The two new instruments endorsed by ADF Deputies to proceed to detailed design and proposals for consideration by the Bank's Boards are (i) a Partial Credit Guarantee (PCG) and; (ii) a Private Sector Facility (PSF). Both instruments are designed to leverage the Fund's scarce resources and crowd in commercial sources of financing for transformational development projects in low income countries (LICs).





proposes to intensify efforts to reduce gender disparities by focusing on three key strategic areas during ADF-13. These include promoting women's economic empowerment, strengthening women's legal status and property rights, and improving knowledge management and capacity building. The Bank is developing the Gender Strategic Framework 2013-2017, which seeks to align the strategic areas for the promotion of gender equality to the areas of focus of the Bank. As part of this framework, the promotion of gender equality must be strengthened in the area of private sector development.

The role of women in creating, running and expanding businesses is recognized as fundamental for growth and poverty reduction, but women do not have private sector opportunities equal to those of men in Africa. Although roughly equal numbers of men and women are engaged in African commercial activity, women are predominantly found in informal, agriculture sector-related activities. Female entrepreneurs also face disproportionate obstacles in obtaining credit, training,

access to networks and information. They also face additional legal and policy obstacles.

Going forward, the Bank Group will support initiatives to increase women's human capital – skills, management training, business mentors and networks; to expand awareness of women's success as entrepreneurs; to improve the voice of women in investment climate policy circles; and to leveling the playing field for women and improving their economic opportunities. This last point will emphasize improving access to finance and education, eliminating gender bias in labor policies, land tenure and administration, and building skills in science, technology and entrepreneurship.

The three broad implementation modalities will include finalizing the Bank Group's Gender Strategic Framework to guide Bank activities in gender mainstreaming, improving the effectiveness of gender mainstreaming in operations and improving the monitoring of results.



Implementing the Strategy

Many good strategies do not achieve the intended results due to inadequate attention to implementation. Although a Bank-wide mandate, private sector development has at times been seen as the exclusive preserve of a few departments within the organization. Implementation of this strategy will therefore require a mindset shift that will mainstream private sector development issues throughout the institution. (Annex III). In this regard, Bank Management will pay particular attention to a number of *leadership*, *ownership*, and *partnership* issues. Likewise, Management will pay special attention to *monitoring and evaluating* the Strategy.

3.1 Leadership

The Strategy has broad implications that will affect the operations of the Bank Group as a whole, not simply private sector operations. Work is underway to explore institutional options to more effectively deliver on the strategic thrust of the PSD agenda. Management recognizes that there might be need for fine-tuning the organizational and incentive structure. Senior management will lead this process by ensuring adequate staffing and resourcing of the Bank's Operational units, particularly Field Offices. Several specific actions in this regard, will include:

- ***Fine-tuning the organizational and incentive structure.*** A challenge for the Bank's structure is the absence of a dedicated department that oversees the overall PSD agenda. This has meant that the agenda is fragmented across the Bank without centralized and permanent accountability. A high-level Private Sector Development Steering Committee (PSDSC) will be set up to ensure effective implementation of the Strategy. Its very creation signals that private sector development is more than private sector operations and hence, supersedes the organizational responsibility of a single complex. The PSDSC will play a key role in transforming the organization, whose activities have been dominated by public sector interventions, to one increasingly focused on seeking private sector solutions and promoting public-private partnerships. As part of its mandate, the PSDSC will:

- i. Ensure that the Strategy is translated into a consolidated, results-focused organizational business plan, with a clear timeline that matches Bank activities for implementation of the Strategy;

- ii. Provide guidance to harmonize other strategy and policy documents that might impact the effective implementation of this Strategy; and oversee the effective implementation of recommendations from various OPEV evaluations affecting the Bank's PSD and NSO agendas (Box 3);

- iii. Ensure that the overarching goal of private sector development is inculcated into the Bank's culture, its KPIs and incentive structure agreeing on commonly defined targets, development outcomes, and striving for optimal contributions from each unit across the Bank;

- iv. Consolidate and update the Bank's policy framework for NSO, including (a) greater coherence between the Bank's Risk Management Framework and its strategic objective of supporting more NSOs in low income countries; and (b) ensuring that NSOs are not merely opportunistic, but are part of CSP and RISPS programming, particularly by strengthening the PSD and NSO orientation of CSPs and RISPS as mentioned in Section 3.2;

- v. Fine-tune Bank's business processes as related (but not limited) to its PSD agenda, to strengthen their effectiveness and value for money, as well as have oversight over resource and quality assurance in all PSD-related work; and

- vi. Develop plans to effectively communicate the Strategy both within and outside the Bank.

- ***Consolidate the Bank's work on the financial sector.***

In light of the importance of the financial sector in both the Bank's overall Strategy for 2013 – 2022 as well as in this Strategy, the Bank is undertaking a comprehensive review of its approach to the financial sector, which will lead to the preparation of a new Financial Sector Development Policy and Strategy to replace the 2003 Financial Sector Policy. The PSDSC will play a crucial role in guiding this process. In this regard, the President has constituted a working group chaired by the Chief Economist and Vice President, with high-level representation from several Complexes to:

- i. Re-express the operational priorities for financial sector

operations into measurable objectives linked to the PSD Strategy pillars and the Bank Group's overall strategy for 2013-2022;

- ii. Prioritize activities associated with those objectives that tackle long-term, seemingly intractable problems, (e.g. access to finance, increased and faster take-up of needed harmonized regulatory reforms) and which, if proven successful, have potential to achieve transformative scale;
- iii. Identify needed resources, preferred partners and milestones for prioritized actions; and
- iv. Consider how organizational structures, budgets, processes and skills of financial sector operations can be best aligned to implement prioritized activities for key objectives.

The working group will fast-track, near-term priorities before modified approaches are fully implemented institutionally. That will begin with considering which sectors and markets (e.g. extractive industries, agriculture, and power) should prioritized actions be tackled.²⁷

27 Illustrative prioritized actions will include the following: (i) sustainable, i.e. commercially viable, approaches to mitigating risk of lending to SME's; (ii) linked policy/regulatory reforms with investments in financial sector infrastructure, e.g. payments systems, agent networks that are associated with mobile solutions that are at the heart of more inclusive, deepened financial services; and (iii) capital market investment products that support increased origination of a variety of credit assets (leasing receivables, infrastructure bonds, real estate mortgages) for local and international institutional investors.

• **Clarifying links to programming and budget.** Under Steering Committee guidance, the Bank will develop a PSD business plan and address the issue of the Strategy's implications on the Bank's administrative budget. In the short term, proposed changes will be primarily implemented through a shifting of existing staff into any new structures that are created; and where necessary, through the creation of a limited number of new positions. The budgetary impact of these recommendations will be examined in the annual Program and Budget (PBD) discussions, in close consultation with the Board. In addition, the Bank's ADF and ADB windows will systematically aim to actively mobilize co-financing from other development partners or commercial Banks for both its lending and non-lending program. The Bank will also explore greater efficiencies in the use of concessional and grant financing to deliver its catalytic potential. Further, it will seek to enhance the capacity of local and regional financial intermediaries through which some of its PSD programming is delivered.

3.2 Ownership

To ensure that private sector development is everyone's business and not the concern of only select Bank units, and also that the Bank's various Complexes are aligned to the Strategy, management will focus on the following:

• **Strengthening country and regional strategy and programming.** Implementation of the PSD Strategy in each RMC will require a clear understanding of

Box 03 | Implementation Schedule of Key Recommendations by OPEV

Action	Completion date
Private Sector Risk Sharing framework	December 2013
Update of the ADOA framework	December 2013
Update of Bank's capital adequacy policy	December 2013
Consolidated PSD Business Plan	December 2013
Equity Investment Policy	December 2013
Equity Investments operational Guidelines	December 2013
NSO Policy	January 2014
NSO Guidelines	January 2014
Financial Sector Strategy	March 2014
Enclave Projects Policy	June 2014
Enclave Projects Operational Guidelines	June 2014
Lines of Credit Policy	September 2014
Lines of Credit Operational Guidelines	September 2014

the situation on the ground, including the legal and regulatory environment as well as constraints and opportunities for the private sector to thrive. In this regard, more effective appraisals of the private sector will be done for each RMC on a regular basis. Such assessments, which will be carried out by Country Teams, will leverage the Bank's decentralized staff in Regional Resource Centers as well as its Field Offices and will complement CSPs and RISPs to form the backbone for deciding possible interventions by the Bank. Another point of entry will include private sector development related knowledge products that would support effective policy dialogue on private sector development issues, structural transformation issues, development of capital markets and financial services, and leveraging both public and private investments.

- **Selectivity.** This Strategy emphasizes that Bank assistance to RMCs will be largely determined by country circumstances as enshrined in CSPs and RISPs, the Bank's basic business plan for RMCs. CSPs/RISPs, both aligned to national or regional development strategies and priorities. This will ensure that the Bank's PSD activities will optimize additionality, reflect sound analysis, consultation and ownership. This will also help build collaboration with other donors in advancing private sector development in RMCs and ensure that Bank country-level activities reflect the Bank's core competencies, sound analysis, consultation, and ownership
- **Fostering 'One Bank' teamwork in the preparation and implementation monitoring of PSD interventions in RMCs and RECs.** The Bank will foster greater collaboration between the Bank Group's sovereign and non-sovereign windows. In this regard, the PSDC will promote enhanced sharing of "development intelligence" on what works well and what does not in individual RMCs or RECs, and foster multi-sector and multi-skilled analysis of opportunities and constraints to realizing successful Bank interventions. This will be done primarily by aligning the Bank's non-sovereign operations with country and regional strategies. Second, new efforts will be made to strengthen the PSD orientation of sovereign operations through the fostering of more systematic review of the Bank's public sector operations to consider how they facilitate private investment and private enterprise participation.
- **Strengthening the Bank's capacity in private sector development support.** The Bank will roll out a program for capacity building for Bank staff, as well as RMCs officials, covering subjects including: PSD-responsive CSPs; investment climate issues; systematic analysis of the state of the financial sector in RMCs or sub-regions. Such capacity building programs, conducted by the Bank's African Development Institute (EADI) and others, will also train cross-sectoral Bank staff in the identification of potential areas of Bank support to deepen and broaden access to financial services for enterprises and/or capital market development opportunities; greater effectiveness in-country dialogue on PSD with various stakeholders in the respective RMCs or sub-regions.
- **Improving the PSD and NSO dimension at sector level.** Sector operations departments, with advice from the PSDSC and other relevant departments will jointly work to strengthen the Bank's sector strategy papers so that they better describe interventions needed for effective private sector participation. This will particularly be the case for the sectors highlighted in this strategy, such as transport and energy. At the same time, Management will devote particular attention to the need to recruit and maintain staff with the right skills mix to effectively manage the Bank's rapidly growing non-sovereign portfolio.
- **Using decentralization for greater operational effectiveness.** The Bank will implement an institutional capacity-building program to equip decentralized staff with the requisite tools, skills and budget to deliver effectively on the PSD agenda and, if necessary recruit new staff for this purpose. The Bank's Business Opportunity Seminars (BOS) will continue to strengthen the participation of local African enterprises in Bank-financed projects.

3.3 Partnership

A key instrument for implementing this Strategy will be strategic partnerships with other development partners, including DFIs that work directly with the private sector, policy research institutions and universities, governments, and of course, the private sector. The Bank intends to ratchet up engagement with the private sector through such vehicles as CEO fora, regional, national and sub-national business trade groups. Special focus will be given to:



- **Knowledge generation, management and brokerage.** The Bank will seek to position itself as a more visible, effective and relevant knowledge broker on private sector development in Africa issues. It will intensify its approach to its PSD knowledge products and advisory services, as part of an update to its knowledge management strategy. Bank Management will redouble efforts to mobilize resources to fund PSD-related analytical work, in partnership with various other organizations.

- **Strategic initiatives.** The Bank will seek to extend its cooperation and co-financing with a wider range of partners at the national, regional, and global levels. Such partnerships include the Fund for African Private Sector Assistance (FAPA), African Management Services Company (AMSCO), the Multi-Donor Governance Trust Fund (GTF), the Enhanced Private Sector Assistance (EPSA) initiative, the Investment Climate Facility for Africa (ICF), the Infrastructure Consortium for Africa (ICA), the Extractive Industries Transparency Initiative (EITI), AfriTAC, and the Making Finance Work for Africa (MFW4A). It will also scale up support for special initiatives such as the African Legal Services Facility (ALSF).

- **New Partners.** New partnerships will be developed with, for instance, Brazil, China, India, Russia, Turkey and Singapore, as well as global funds, Islamic funds, private foundations, African and other Sovereign Wealth Funds and central banks. Elsewhere, the Bank will work closely with the AU, UNECA, the World Economic Forum, and other fora to support Africa's private sector. The Bank will also explore ways of leveraging the resources of Africa's Diaspora (US\$20 billion of annual remittances), including using diaspora bonds and other innovative financing.

3.4 Monitoring and Evaluating Results

The effectiveness of the Bank's private sector development assistance to RMCs will largely depend on its ability to monitor, measure and evaluate its work and, where necessary, to make adjustments.

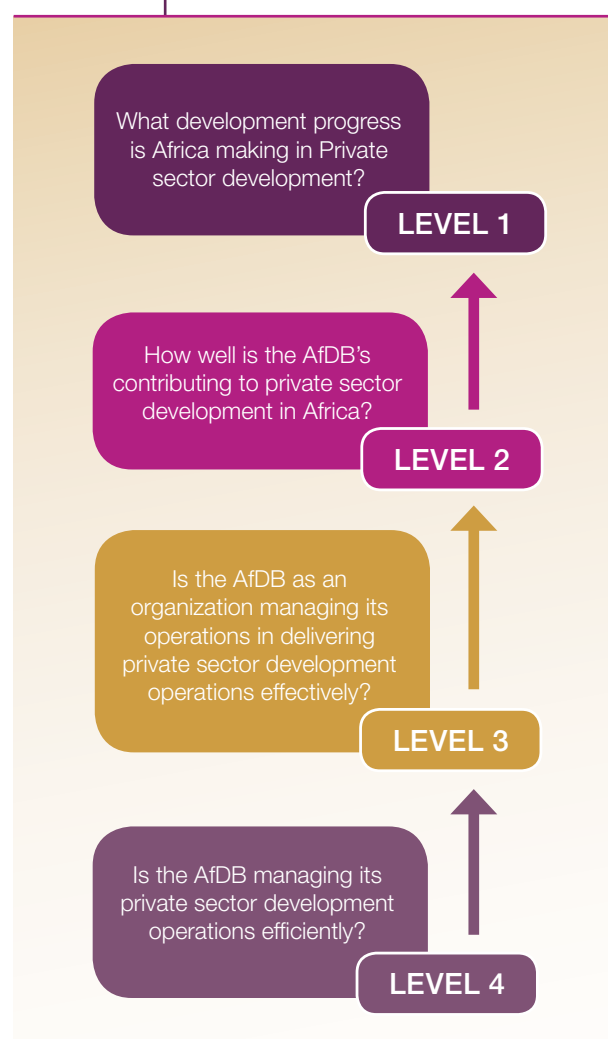
The PSD Strategy is aligned with the Bank's existing, four-level results monitoring framework (Figure 8). The RMF, a draft of which is summarized in Annex IV, will allow the Bank's shareholders and stakeholders to monitor private sector activities to ensure that they are making significant contributions toward helping

the Bank Group to achieve developmental and other mandates.

Bank Group departments will work closely with its Results Department (ORQR) to revise Bank-wide public sector development indicators to reflect the PSD strategic priority. These will then be applied across the organization.

Given the rapidity of changes in the regional and international social and economic landscapes, it is proposed that this strategy cover a period of five years, with a mid-term review in the third year of the strategy.

Figure 08 | PSD Results Monitoring Framework



Risks and Mitigation Measures

There are several risks that could adversely impact the effective implementation of this Strategy. The major ones are summarized below, along with suggested mitigation measures. In general, risk management will be an iterative process during the Strategy's duration, with new risks identified, assessed, prioritized, and dealt with throughout the Strategy's duration. And in line with the Bank's Strategy for 2013-2022, Management will examine the prudence of innovative risk evaluation and mitigation methods.

Inadequate Financing and Capacity to Deliver.

This Strategy is premised on several key assumptions including that there will be no significant reduction in the Bank Group's ADF window resources in real terms over the next two replenishment cycles, and that the Bank Group will maintain its Triple-A rating in the absence of any significant economic or other shocks. However, the resources available to deliver on this Strategy may still be insufficient. Given the size of most infrastructure and industrial projects, prudent risk limits, particularly for low-income countries (LICs) and fragile states, may limit the Bank's ability to constantly undertake significant volumes of NSO in these countries. The Bank may also fail to mobilize the necessary skills for the strategy within budget constraints.

As a mitigation measure, implementation of the Strategy will place high emphasis on defining and executing ways to stretch the Bank's risk capital, notably through risk participation and sharing measures. Moreover, the Strategy is designed to leverage existing Bank Group resources while attracting those of other partners, including African governments, the private sector, and non-traditional development partners including emerging countries and philanthropic organizations.

The Bank will redouble efforts to make more effective use of bilateral and multilateral trust funds (Special Funds). The proposed PSD Strategy Steering Committee will also serve to mitigate the particular delivery capacity risks internal to the Bank.

Strategic Alignment and Reputational Risk. Parties to the Bank Group's transactions may not share the Bank's pro-poor focus. The business model for the Bank's

allocation of funds to the private sector focuses both on the commercial potential of enterprises within the Bank's risk framework and on amplifying development benefits, but private parties might focus only on the former. The tension between the two objectives could lead to a drift toward financing lower-risk activities in areas mostly favored by investors but which may not provide the most development benefit.

As mitigation measures, the Bank Group will continue to emphasize promotion of private sector development in areas where development benefits are high but which financial markets regard as too long term or risky, or not profitable enough. The Bank is developing corporate governance guidelines to steer its engagement for partnerships, particularly from the private sector. Additional mitigating measures include Bank support to sovereign and non-sovereign clients on preparing operations (including environmental and social safeguards); using results-based analytical frameworks as a basis for the preparation, implementation, and monitoring of Bank-financed operations; and systematic attention to sustainability issues (institutional viability, operations and maintenance; and financial viability) as well as environmental/social sustainability issues. Bank guidelines for project teams on corporate governance and corporate social responsibility (CSR) will also be developed, to ensure the promotion of good practice across the windows of AfDB Group activity.

The Bank will also continue to fine-tune its Assessment of Development Outcomes and Additionality (ADOA) procedure for all private sector operations. An ex post facto evaluation of the accuracy of ADOA will be undertaken in 2014. Projects for which assessed ADOA ratings are unsatisfactory will not be eligible for presentation to the Board. This may mean: developing new ways of appraising project risks, moderating the approach of always following the market, and not being overly dependent on a project-driven model by addressing all three PSD strategic pillars concurrently.

Governments' Commitment to PSD. Whereas most African governments now recognize the vital role of the private sector in economic development and poverty reduction, many have yet to make sufficient practical

progress, including by making critical institutional and governance reforms. Substantial risk could arise in following an unforeseen erosion of Africa's current credibility and growing reputation as a preferred investment destination.

Mitigation measures would primarily revolve around stronger high-level policy dialogue with Governments, particularly through the dialogue mechanisms with other development partners, or via General Budget Support and Sector Budget Support operations. Steps could also be taken to boost public awareness and popular support, including strengthening the demand for PSD-related reform. Other mitigation measures would involve dissemination of quality knowledge products as part of Bank Group analytical and advisory services.

Portfolio Growth and Concentration: Another risk that the Bank faces is the monitoring of the growth of its young private sector portfolio. This is particularly true as most loans are expected to reach the end of their grace period in 2013/2014, and some borrowers' credit profiles have deteriorated, and so the limit of risk capital utilization allocated to high-risk transactions in accordance with the Bank's risk appetite? statement

is about to be reached. Consistent with the GCI commitments, the Bank has increased its exposure in LICs, which use risk capital faster than similar projects in middle-income countries (MICs). Similarly, projects sponsored by Africa's emerging entrepreneurs are also perceived to be more risky than counterparts with a global presence and track record. This is most evident with regard to the Bank's equity investments. (See Box 4)

In order to build resilience and to protect the Bank's AAA rating, the rapid growth of the non-sovereign portfolio over the last years may need to be balanced with more efforts in consolidation and portfolio management particularly to address the potential risk of portfolio concentration. To that end, Management is adopting mitigation measures. Continuing to strengthen institutional credit risk governance through undertakings by the Bank's Credit Risk Committee (CRC) will continue to reinforce institutional focus on credit risk governance and prudential limit management. Through its exclusive

28 See, in this regard, *Equity Investment Policy Guidelines* (ADB/BD/WP/94/125) and *Review of ADB Financial Policies* (ADB/BD/WP/93/86).

29 See, *Equity Portfolio – Risk Capital Utilization and Performance* (ADB/BD/IF/2012/238).

Box 04 | Equity Investments

The Bank Group has been making equity investments since the 1970s, the main goal of which has been to leverage more capital by attracting more investors, and consequently to contribute to the development of Africa's private sector. That development objective, though, must be accompanied by satisfactory financial returns. Because equity investments are not primarily held by the Bank for income-generating purposes, current guidelines also require their eventual sale to private investors when enterprises become self-sustaining.²⁸

In recent years, the Bank's equity investment portfolio has recorded significant growth while expanding the scope of investments with additional instruments, notably private equity funds. As a portfolio designed to increase development results as much as possible, it still manages to achieve positive financial returns and is already realizing capital receipts from dividend payments and sales of certain underlying investments. Nevertheless, this growth has resulted in rapid risk capital posing particular challenges, given statutory caps on the use of these instruments.²⁹

Bank Group Management is fully aware of the need to reconcile the Bank's operational objectives with its risk management framework for equity investments. Going forward, the Bank will continue close monitoring of its portfolio, carefully selecting investments to balance the Bank's risk/return while revisiting guidelines and processes to address the inherent riskiness of these types of transactions, including exit mechanisms, all as part of updated Guidelines for Private Sector Operations (currently under review).

In line with the recommendations by the Bank Group's independent Evaluation Department (OPEV), Management will apply existing screening and selection methods, bolstered with revamped development impact assessment, to all new equity investments. This will allow greater selectivity by the Bank and better management of the growth rate of its equity investment portfolio. Bank Management will also examine the levels of risk capital charges for equity investments to ensure they reflect the Bank's experience with these types of instruments, international requirements (including those from International Financial Reporting Standards) and practices used by fellow IFIs and bilateral development agencies. Furthermore, the Bank will recruit additional investment and legal officers and provide more specialized training to staff on equity investments.

focus on credit risk issues, the CRC will continue to be instrumental in strengthening the credit risk culture across the institution and will closely monitor growth of the Bank's portfolio, notably for private sector operations. Management is also reviewing the Bank's capital adequacy policy toward an economic capital framework in line with the best banking practices.

At the same time, Management is increasing use of alternative instruments, as well as seeking risk-sharing partners to leverage the Bank's NSO portfolio and pipeline, while keeping its risk levels within prudential limits. These measures are intended to enable the Bank to allocate more headroom to its strategic priorities, while protecting its financial profile.

In addition, the Bank is improving management of concentration risk, particularly in the public sector portfolio, by pursuing geographic diversification and increasing sovereign lending to creditworthy countries to which the Bank is underexposed. The current review of the Bank Group's broader lending landscape is also expected to pave the way for additional diversification opportunities. Concentration of risk by sectors or instruments in the non-sovereign portfolio, particularly in the financial sector, is also subject to strong monitoring.

Credit Risk. The Bank's rating reflects its intrinsic financial strength, its prudent financial management and policies, and its strong shareholder support. These strengths offset the relatively high risk profile of its overall portfolio, which results from its challenging regional operating environment. However, the Bank's own Weighted Average Risk Rating (WARR) of its portfolio remains within the limits defined by its risk appetite statement.

In recent years, the Bank Group has considerably increased lending to sovereign and private sector

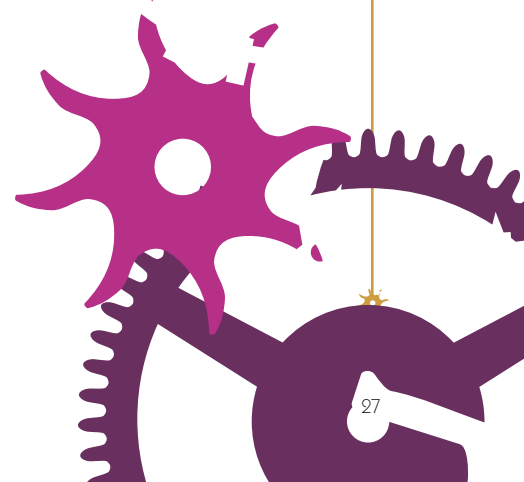
counter-parties. However, the its strong capitalization, liquidity buffers and risk-management framework help to offset risks it carries on its balance sheet, and create substantial headroom in risk-bearing capacity to expand its lending further. Moreover, the Bank's private sector operations in its low-income RMCs are an obvious avenue to achieve greater geographic diversity to compensate for the concentration of its sovereign portfolio in a few countries (some of which have recently been downgraded because of domestic and external political and economic factors), and hence are an element of a Bank-wide portfolio risk mitigation strategy.

Business Process Risk. In an effort to strengthen internal review, the Bank has, at times, made its approval process too long and onerous relative to the Bank's processing capacity. This makes the Bank less competitive than other IFIs and limits the potential productivity of the teams processing NSO.

The Bank's new NSO guidelines will propose a streamlined approval process, benchmarked with other IFIs, to ensure that each step retained in the process presents "value for money" for the Bank and its clients.

Operational Risk. Since the Bank began to originate non-sovereign guaranteed transactions, the body of statutory documents that guide and regulate the its NSOs has developed incrementally, leading to an accumulation of policy and guideline directives that now need to be consolidated and updated.

The PSO portfolio review, the new PSD Policy and this Strategy establish the foundation for a new PSO guidelines policy to supersede the numerous existing policies.



05

Conclusion

The private sector drives Africa's economic growth. Economic growth drives Africa's development. African countries recognize these facts and are determined to harness the tangible benefits of development for their people: socioeconomic opportunity, human capital, critical infrastructure, regional competitiveness, environmental sustainability, social inclusion and poverty reduction, health, safety, literacy, happiness.

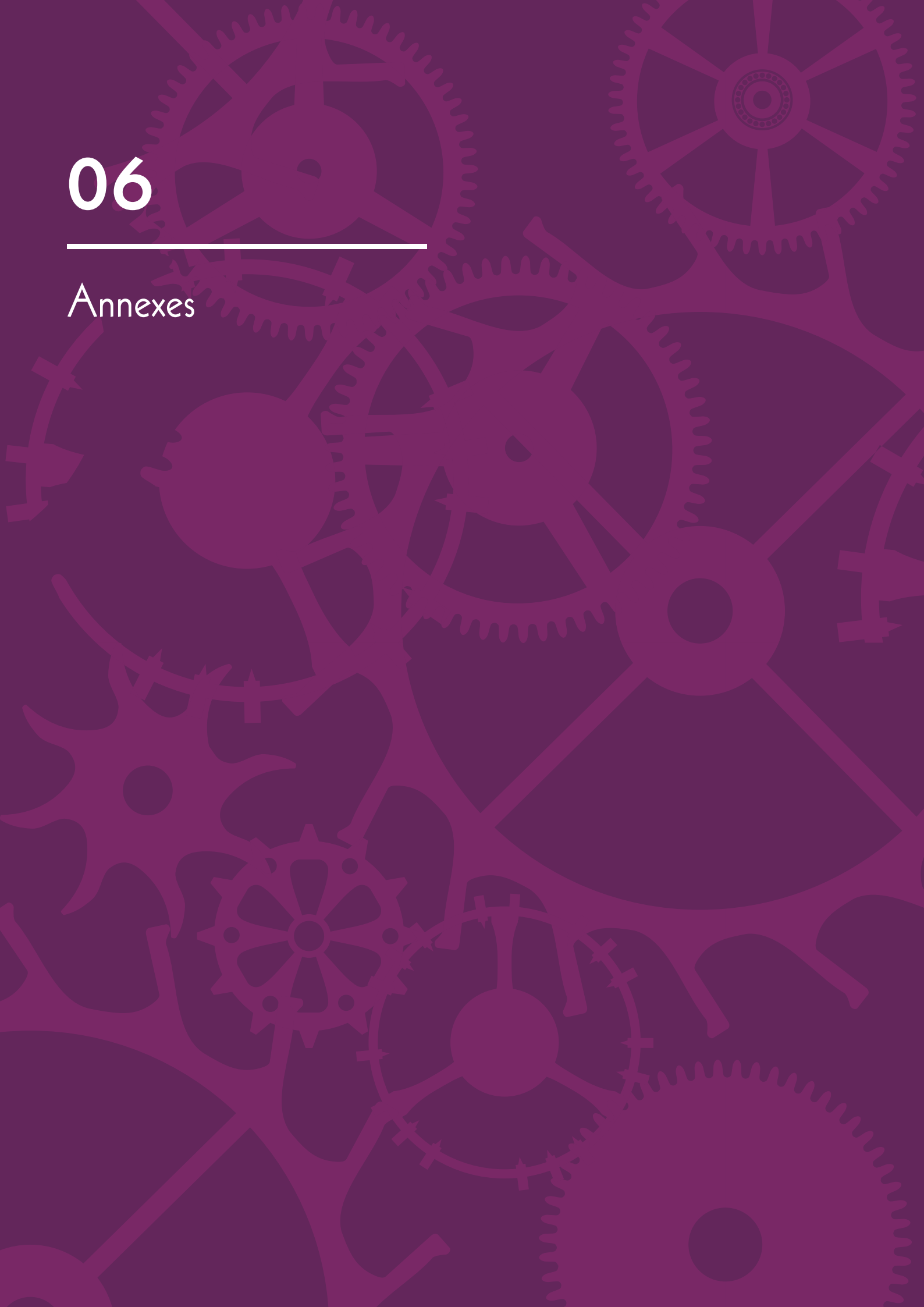
This Strategy sets out the framework for the Bank Group's private sector development activities across Africa for the medium term. The Strategy affirms the role of the private sector as an agent of Africa's development, and as a partner in delivering on the Bank's agenda of inclusive growth and the transition to green growth.

In line with its Strategy 2013-2022 and its operational policies, the African Development Bank will use resources at its disposal to support private sector development, not as a distinct sector or instrument, but as a priority to which all Bank operations can and must contribute.



06

Annexes



6.1 Annex I: Lessons from Previous Activities³⁰

CHALLENGE	SOLUTION (Private Sector Development Strategy)
Strategy Alignment	
Operational instruments including regional, country and sector strategies and business plans inadequately reflect PSD as a Bank-wide priority.	<ul style="list-style-type: none"> Proposed PSD SC to play key role in ensuring that new regional, country and sector strategies, as well as related business plans, fully capture Bank priorities. New guidelines to be developed to ensure that revamped regional, country and sector priorities better reflect PSD as a Bank-wide priority.
Institutional Buy-In	
Institutional buy-in on PSD not broad enough across Bank Group operations to allow internalization of, and responsiveness to, institutional PSD objectives.	<ul style="list-style-type: none"> Proposed PSD SC to oversee, monitor and report on Bank's overall PSD agenda. New guidelines to be developed to ensure that revamped regional, country and sector priorities better reflect PSD as a Bank-wide priority.
PSD Prioritization	
Unclear Bank Group PSD priorities often contribute to strategic misalignment in project selection.	<ul style="list-style-type: none"> Greater clarity in Bank Group PSD priorities and principles guiding them.
Operations	
Insufficient knowledge-based activities inform Bank Group business-enabling environment (BEE) operations.	<ul style="list-style-type: none"> Revamped and strengthened approach to knowledge-based operations and activities to be developed to better inform Bank Group's PSD operations, including BEE operations.
Insufficient local content in Bank Group's procurement of operations to promote PSD.	<ul style="list-style-type: none"> Fine-tuning of Bank Group's communication strategy on PSD opportunities for local providers in Bank-financed projects, including expansion of its Business Opportunity Forums.
Insufficient engagement of non-state actors in the Bank's PSD agenda.	<ul style="list-style-type: none"> Revamped guidelines for country and regional strategies to emphasize sustained engagement with non-state actors in informing PSD priorities and strategy.
Results and Accountability	
Weak corporate PSD Results Monitoring Framework (RMF) focuses primarily on non-sovereign operations at the expense of the rest of the Bank Group's PSD interventions.	<ul style="list-style-type: none"> Revamped and strengthened PSD Results Monitoring Framework to be developed by Results Department in collaboration with various Complexes and overseen by proposed PSD SC.
Poor results and accountability when targeting support to MSMEs, particularly through financial intermediaries.	<ul style="list-style-type: none"> Bank Group's approach to working with financial intermediaries to be fine-tuned.
Lack of measurement framework for catalytic effect of Bank Group's sovereign and non-sovereign lending.	<ul style="list-style-type: none"> Where appropriate, staff performance indicators to be adjusted to reflect PSD goals.
Skills Mix	
Deficient skills mix across the Bank Group to deliver effectively on its PSD agenda.	<ul style="list-style-type: none"> Bank Group to adjust existing gaps in current human resource skills mix in light of PSD agenda, through capacity-building and other means.
Safeguards	
General lack of use of Bank Group safeguard measures a dialogue platform for country portfolio improvement.	<ul style="list-style-type: none"> The proposed PSD SC will be the place to bring this issue and propose solutions in conjunction with ORPC and other relevant units.
Long and onerous approval processes relative to the Bank's processing capacity, leading to lack of competitiveness compared to other IFIs.	<ul style="list-style-type: none"> Streamlined approval process, benchmarked with other IFIs, to ensure that each step retained in the process presents "value for money" for the Bank and its clients.
Proliferation of NSO policy and guideline directives that now need to be consolidated and modernized.	<ul style="list-style-type: none"> The NSO portfolio review to lay the foundation for streamlined guidelines to supersede numerous existing policies.

³⁰ See Annual Development Effectiveness Review 2012 and Mid-Term Review of the Medium-Term Strategy 2008-2012 (Ref. ADB/BD/WP/2011/52/Rev.1 and ADF/BD/WP/2011/30/Rev.1), the 2008 Strategy Update for Private Sector Development, and the 2008-10 Business Plan for Non-Sovereign Operations; and "Fostering Private Sector Development in Africa: An Independent Evaluation of Non-Sovereign Operations, 2006-2011". Operations Evaluation Department (OPEV).

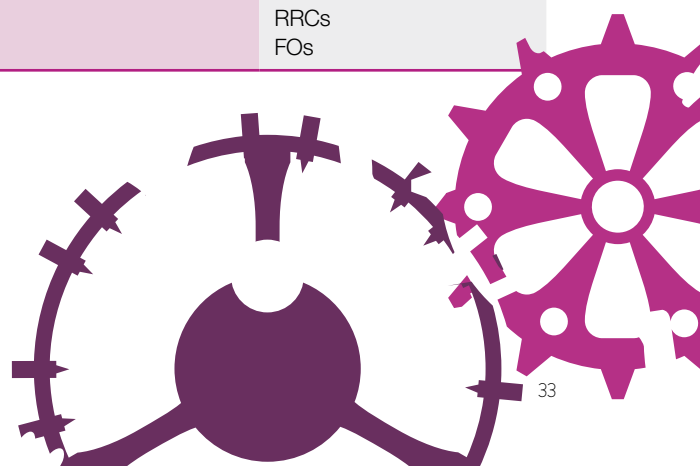
6.2 Annex II: Pillar-Related Operational Areas

PILLARS	TARGET OUTCOMES	OPERATIONAL AREAS	KEY UNITS
PILLAR I: Investment and Business Climate	1.1 Improved investment and business climate in RMCs	1.1.1 Macroeconomic policy reforms, taxation, fiscal incentives to seize green opportunities as well as to promote more inclusive growth; institutional strengthening	RDs OSGE
		1.1.2 Rule of Law: Legal and regulatory reforms (e.g. simplification of business registration or investment licensing, construction permits, enforcing contracts, handling business insolvency, etc.) Business enabling environment for industrial services and manufacturing enterprises Business enabling environment for agribusiness, agro-industry, and rural enterprise	RDs OSGE OITC, ONEC, OWAS, OSAN, OSHD African Legal Support Facility
		1.1.3 Anti-Corruption institutional reforms and capacity building	RDs OSGE
		1.1.4 Property Rights: Improvement of land tenure and property registration systems ensuring rights for equal access for women (and their implementation)	RDs African Legal Support Facility
	1.2 More efficient national and regional factor and product markets	1.2.1 Labor market reforms, vocational training, youth technical skills development and entrepreneurship promotion	OSHD
		1.2.2 Regional market integration: - Financial infrastructure broadening and deepening - Trade policy and related institutional reforms - Labor mobility across regions - Tax systems harmonisation - Standards (including quality assurance and certification) harmonisation - Investment and engineering codes harmonisation	ONRI OSGE
		1.2.1 Public-Private Partnership frameworks	OSGE OPSM African Legal Support Facility
	1.3 Strengthening corporate responsibility	1.3.1 Corporate good governance	OSGE OPSM African Legal Support Facility
		1.3.2 Environmental and social impact management (including capacity to implement the Extractive Industries Transparency Initiative)	ONEC ORQR OSGE

PILLARS	TARGET OUTCOMES	OPERATIONAL AREAS	KEY UNITS
PILLAR II: Access to social and economic infrastructure	2.1 Improved physical infrastructures and increased access to services: Transport, Communications, Energy, Water supply and Sanitation	2.1.1 Transport: Infrastructure and Services	OITC OPSM ONRI
		2.1.2 Communication: Infrastructure and Services	OITC OPSM ONRI
		2.1.3 Energy: Infrastructure and Services (including renewable energy)	ONEC OPSM ONRI
		2.1.4 Water Supply and Sanitation	OWAS OPSM ONRI
		2.1.5 Infrastructure improving agriculture production and food security (irrigation systems, rural roads, etc.)	OWAS, OSAN OPSM ONRI
	2.2 Improved social infrastructure and increased access to services: Education, Health care	2.2.1 Higher education, science and technology	OSHD, OPSM
		2.2.2 Vocational training	OSHD, OPSM
		2.2.3 Health-related: Infrastructure and services	OSHD, OPSM
	2.3 Improved regulatory frameworks in socio-economic infrastructure sectors	See 1.1.2 and 1.3.2	See 1.1.2 and 1.3.2

PILLARS	TARGET OUTCOMES	OPERATIONAL AREAS	KEY UNITS
PILLAR III: Enterprise development	3.1 Small, Medium and Micro Enterprises (MSMEs) and Social Business	3.1.1 Micro, Small and Medium Scale Enterprises (MSMEs) - Scaling up and leveraging financing and services for SMEs : - Proposal to create a standalone Facility for SMEs - Establishment of local systems and institutions to facilitate micro-enterprise creation - Support for business development services - Capacity building, including in financial literacy - Creation and coordination of business clusters and network - Support to Microfinance Institutions	OPSM OSGE OSHD
		3.1.2 Social Enterprises: - Support to RMC authorities to prepare or strengthen policy and institutional frameworks conducive to social business - Partnerships with selected social businesses	OSHD OPSM
	3.2 Value Chain Development and Catalytic Investments	3.2.1 Lesson-sharing between countries	EADI
		3.2.2 Strengthening value chains, particularly in extractive industries, manufacturing, agriculture, forestry and fisheries	OPSM, OSHD, OSAN
		3.2.3 Support to the deepening and expansion of financial and capital markets	FNVP, AFMI, MFW4A, ONRI, OPSM
		3.2.4 Catalytic investments with a focus on technology transfers, industrialization agribusiness, agro-industry, and rural enterprise	OPSM, OSHD, OSAN
	3.3 Trade Finance	3.3.1 Implement the 2012 Trade finance initiative	OPSM, ONRI

ADDITIONAL ACTIVITIES	INSTRUMENTS	OPERATIONAL AREAS	KEY UNITS
PSD mainstreaming	Coordination	All areas	Proposed PSD Steering Committee
Integrated or mutually complementary sovereign and non-sovereign operations, including Public-Private Partnership (PPP)	Sovereign and non-sovereign guaranteed loans, guarantees	All Pillars	RDs, Sector Departments, OPSM
Support to Fragile states	Policy dialogue, policy-based assistance, and sector operations	All Pillars	OSFU, RDs, Sector Departments, OPSM
Support in project design and institutional support operations	Analytical, Advisory, and Advocacy Activities	All Pillars	EDRE, EADI, ESTA, ORPC
Project support	All instruments	All pillars	GECL, ORPF, EDRE (ADOA), FFMA, ONEC, ORQR and Sector departments.
Business Opportunity Seminars	Internal	All pillars	ORRU RRCs FOs



6.3 Annex III: Summary of Bank-Wide Institutional Arrangements

Regional Departments (RDs) and Field Offices (FOs) will lead in the following activities:

- conducting dialogue with active and potential investors and business operators to identify RMCs' strengths and weaknesses, opportunities and threats, and the perceptions of investors and business operators;
- overseeing policy dialogue with RMCs and RECs on private sector development;
- mainstreaming private sector development in CSPs and RISPs, incorporating business enabling environment operations and non-sovereign operations while ensuring synergies;
- identification and preparation of integrated or complementary sovereign and non-sovereign operations, including public-private partnership (PPP) opportunities in collaboration with Sector Departments; and
- monitoring the private sector development performance of the Bank Group's country and sub-regional operations. RDs and FOs will advise Sector Departments and the Private Sector Department on national and regional development priorities.

Sector Departments (SDs) will lead in:

- mainstreaming private sector development in the preparation of Sector Strategies of the Bank Group, in collaboration with the Private Sector Department;
- conducting sector-specific policy dialogue with RMC and sub-regional stakeholders;
- preparing and managing the Bank Group's financing operations – including policy-based and investment operations – contributing to improving the enabling environment for business. In addition, the SDs will provide the Private Sector Department sector-specific expertise on project design and implementation monitoring;
- providing technical support to SDs in the design of and management of catalytic transactions including PPPs.

Governance, Economic and Financial Reforms Department (OSGE) will lead in:

- conducting dialogue and providing advisory services and technical assistance to RMCs and RECs on good governance, macro-economic stewardship and financial sector reforms;
- management of policy-based and institutional support financing operations. The department will also provide technical support to other operations departments, on governance aspects of operational strategies, projects and programs.

- **Operations support departments** will take the lead in mainstreaming private sector development issues in their areas of focus.
- **The Fragile States Unit (OSFU)** will collaborate with RDs and Field Offices in programming policy dialogue, policy-based assistance, and sector operations toward improving the business environments of post-conflict and other fragile countries.
- **NEPAD and Regional Integration and Trade Department (ONRI)** will conduct diagnostic studies on the performance of regional integration initiatives on key goals (including market integration and trade development) and advise the RDs, SDs, and the Private Sector Department on the regional cooperation, integration and trade issues of private sector development. Also, ONRI will lead in policy dialogue, on private sector development issues, with regional economic communities (RECs) and specialized regional organizations.

Private Sector Department (OPSM) will take the lead in interactions with local and foreign investors, business operators, parastatal enterprises, and financial intermediaries. The department's activities will include:

- Leading in the financial structuring of catalytic transactions not covered by sovereign guarantee, and in the management of their execution, in collaboration with RDs and SDs (the Department may also be asked to lead transactions covered by sovereign guarantees, at the request of the RDs);
- Collaborating in operations supporting the development of micro, small and medium scale enterprises (MSMEs);
- Leading the mobilization of domestic, regional and external investors and business operators through underwriting of privatization, syndication of large-scale financing operations, and participation in equity funds and special trust funds targeted at specific private sector development objectives, such as microfinance, MSMEs and agri-business;
- Collaborating with ECON, OSGE and ONRI in supporting RDs in the identification and assessment of impediments in the business environments in RMCs and sub-regions and proposing improvements; assisting SDs in identifying and appraising private sector development opportunities and proposing approaches their sustainable management and prudent use; and collaborating with ECON in knowledge generation and dissemination on private sector development and business interaction with other regions of the world.

Chief Economist's Complex (ECON) will be responsible for:

- analytical, policy advisory and dissemination activities, including knowledge generation and dissemination on private sector development and enabling environment, in collaboration with SDs and RDs;
- serving as the Bank's key knowledge broker on PSD; and
- assessment of the expected impact and value added by the private sector development aspects of Bank Group operations, including assessment through ex-ante additionality and development outcomes assessment (ADOA) of financing operations. The Complex will play a leading role in generating differentiated knowledge products on PSD and a supportive role in conducting policy dialogue and in the design and implementation of policy-based financing operations, including institutional support.

Financial Complex (FNVP) Departments will continue to lead in:

- the mobilization of financial resources for Bank operations and the management of liquidity through treasury operations;
- use of such operations to support the development of national/sub-regional capital markets;
- developing operational guidelines for the Bank's financing products and instruments;
- exercising risk management and prudential oversight on Bank sovereign and non-sovereign financing operations; and
- providing fiduciary management of Bank financing operations.

Procurement and Fiduciary Management Department (ORPF) will continue to oversee:

- implementation of the rules and procedures on the procurement of goods and contracts for works financed by the Bank Group;
- the fulfillment of fiduciary safeguards by the beneficiaries of Bank's financing. To increase the use of country systems, ORPF will support capacity-building of RMCs and business sector clients with inadequate institutional competence for procurement and fiduciary management; but the department will provide oversight until country systems are assessed to be sufficient. ORPF will advise on effective application of the rules and procedures to increase local firms' participation in the supply of goods, services and works procured from Bank Group financing.

On a decentralized basis, and working with Regional Resource Centers (RRCs) and Field Office (FOs), the **Partnerships and Cooperation Unit (ORRU)** will expand the Business Opportunity Seminars (BOS) program for African companies. The aim of these seminars is to increase the participation of companies from RMCs in Bank-financed projects. Generic BOS will also continue to take place at the Bank's HQ twice a year.

The General Counsel and Legal Department (GECL) will continue to review legal issues affecting, or arising from, Bank Group operations, including non-sovereign operations, and advise OPSM and other SDs.

Environment and Social Departments will provide guidance and oversight on the fulfillment of environment and social safeguards in the preparation and implementation of sovereign and non-sovereign operations financed by the Bank Group, including policy-based operations. The units will rely on countries' and private clients' environmental and social oversight institutions, where these have adequate monitoring and evaluation capacities. The Bank's Environment and Social units, therefore, will support capacity-building for RMCs, financial intermediaries, and private business operators on environment and social impact assessment, mitigation planning and implementation, and safeguards monitoring and evaluation.

Specialized Support Departments and Units: A number of organizational units provide back-office support to Bank Group sovereign and non-sovereign operations.

6.4 Annex IV: Indicative Results Monitoring Framework (RMF)

This RMF is indicative, and will be developed further in 2013. The proposed set of indicators will be reviewed to ensure that they are regularly measured, with a thorough methodology from credible sources. Level 1 indicators are mainly inspired by the RMF for the Bank Group's Long Term Strategy and by the Annual Development Effectiveness Review (2012). Some Level 2 indicators are taken from ADOA indicators. Missing Level 3 and 4 baseline and target data will be addressed in the revised version of this indicative RMF. Wherever possible, data will be gender disaggregated.

LEVEL1 - Private Sector Development in Africa	Unit of measurement	All African Countries	Source
		Baseline (2011)	
LIST OF INDICATORS			
General Indicators			
Index of unemployment rate (including rates among youth and women)	index	11.3 (15.6 and 17.4) (2008)	ILO, AfDB
Private sector share of employment	%	90	WB
Global competitiveness index score	index	3.6 (2009-2010)	WEF
Business start-up costs	% GNI per capita	77	WB
Africa; s share of global trade	%	3.1	AfDB
Share of African countries with credit ratings of B and above	%	33	S&P
Transparency International's Corruption Perceptions Index rating	Index 1-10	2.9	Transparency International
Country Policy and Institutional Assessment (CPIA) score for property rights and rule-based governance	Index 1-6	3.11	AfDB
Business start-up time	days	23	AfDB
Total intra-Africa trade	US\$ billion	112.4	IMF-DOTS
Foreign direct investment inflows (% of GDP)	%	2.3	AfDB/ UNCTAD
Exports of goods and services (% of GDP)	%	37	DCS
Ease of access to loans	1-7	2.76	WEF

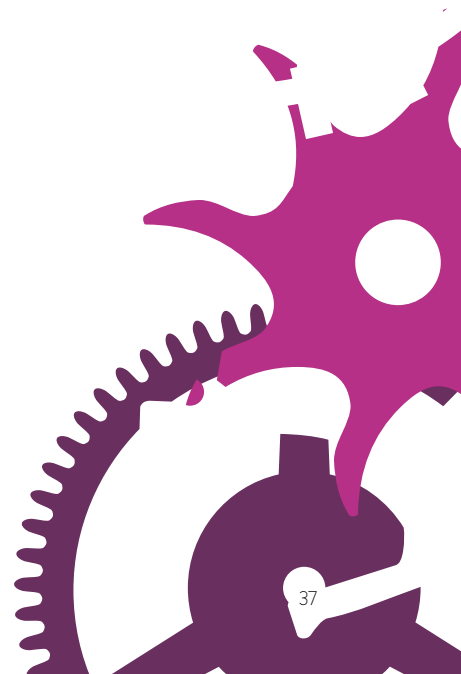
LEVEL2 - AfDB's contribution to Private Sector Development in Africa	Unit of measurement	All African Countries	Source
		Baseline (2011)	
LIST OF INDICATORS			
Production of energy – power capacity installed by Bank Group interventions	MW	1,110 *	AfDB
Transport – Km of roads constructed, rehabilitated or maintained by Bank Group interventions	kilometer	18,777 *	AfDB
Local and regional suppliers of goods, works, and services of total financing volume	%	43%	AfDB
Bank Group private sector projects' contribution to government revenue	US\$ million	12,528 *	AfDB
Total number of microcredits granted by Group via FIs	Number	330,660 **	AfDB
Credit to MSMEs as share of total balance sheet of FI operations****	US\$ million	TBD	AfDB
People benefiting from Bank Group-funded microfinance and social activities	Number	12,829,000 **	AfDB
SME effect (turnover from Bank Group investments)	US\$ million	650 **	AfDB
Total number of jobs created for women through Bank Group investee projects and sub-projects/total number of jobs created	number	28,664/349,886 **	AfDB

... 6.4

LEVEL3 - AfDB efficiency as an organization in delivering Private Sector Development operations	Unit of measurement	All African Countries Baseline (2011)	Target year	Source
LIST OF INDICATORS				
Multiplier effect of US\$1 AfDB resources to US\$ more invested by the government or other donors	US\$	2	TBD	AfDB (2009)
Multiplier effect through NSO of US\$1 value of AfDB resources to USD\$ value of total investment	US\$	TBD	TBD	AfDB
Volume of non-sovereign financing arranged by the Bank	UA million	959	TBD	AfDB
% of Bank Group operations contributing to Private Sector Development rated satisfactory	%	93.80%	TBD	AfDB
Average time required for Bank Group NSOs from exploratory review to Board approval	months	13.6	TBD	AfDB
Share of CSPs which include a financial sector diagnostic****	%	TBD	TBD	AfDB
Number of sovereign guarantee public sector operations by the Bank Group supporting PPPs****	Number	TBD	TBD	AfDB
Bank Group non-sovereign portfolio loan impairment ratio	%	1.36	TBD	AfDB
Weighted Average Risk Rating (WARR) of the NSO portfolio	%	3.48	3-4	AfDB

LEVEL4 - AfDB management of Private Sector Development operations	Unit of measurement	All African Countries Baseline (2011)	Target year	Source
LIST OF INDICATORS				
Share of private sector officers (FOs) based in the field offices or the regional resource centers	%	15	TBD	AfDB
Number of business- and investment-enabling environment (Pillar I) specialist professionals	Number	2	TBD	AfDB
Share of private sector operations (NSO) task-managed from field offices	%	60	TBD	AfDB
Global vacancy rate - Private sector operations (NSO) process professional staff***	%	17.13	TBD	AfDB

* data 2010-2012,** data 2009-2011, *** covering personnel primarily involved in the Bank's NSO business process: EDRE1, GECL2, FFMA2, FTRY4, ONEC3, OPSM 0,1,2,3,45. **** data currently unavailable but being developed for future monitoring



About the African Development Bank Group

The AfDB Group is a multilateral development bank whose shareholders include 54 African countries and 24 non-African countries. The AfDB Group's primary objective is to contribute to the sustainable economic development and social progress of its regional members, individually and jointly. It does this by financing a broad range of development projects and programs through public-sector loans, including policy-based loans, private-sector loans, and equity investments; by providing technical assistance for institutional support projects and programs; by making public and private capital investments; by assisting countries with development policies and plans; and by supplying emergency assistance.

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