CHAPTER 4 COMPARATIVE ANALYSIS OF SUB-REGIONAL DEVELOPMENT BANKS IN AFRICA AND THE WORLD.

4.01 In considering the possibility of establishing a SRDB for SADC, the ToR for this study required an evaluation of experience with SRDBs elsewhere. Several sub-regions in Africa and other parts of the world have established their own SRDBs to facilitate the process of economic integration. This measure was rooted in the belief that dedicated SRDBs were essential to co-ordinate and finance regional infrastructure projects as well as cross-border trade and trade-related investment.

4.02 This chapter examines the experience of SRDB's in Africa, the Caribbean and the EU. Its analysis relies on published information that was readily available. The budget and time constraints for this study precluded direct visits to the SRDBs and primary evaluative investigation. Of the sub-regions looked at, the experience of SRDBs in Africa is perhaps the most relevant in considering the prospects of a SRDB in SADC.[1]

The Experience of Sub-regional Development Banks in Africa

4.03 The SRDBs analysed in sub-Saharan Africa[2] included:

- The *COMESA* (formerly PTA) *Trade and Development Bank* (CTDB)
- The *East African Development Bank* (EADB).
- Banque de Developpement des Etats de L'Afrique Centrale (BDEAC) translated as the *Development Bank for the Central African States*
- Banque Ouest Africaine de Developpement (BOAD) also known as the *West African Development Bank.*

4.04 The genesis of all these SRDBs lay in treaties that established the respective integration arrangements involving the countries concerned. They were created to fulfil a strongly felt (if never properly tested) sense that: (i) definite sub-regional development financing needs existed that needed to be met; and (ii) such needs could only be met by a special purpose sub-regional institution created to mobilise resources for that purpose. In none of these instances was the case examined for exactly what these 'sub-regional' development financing needs were, and how they were distinct from either *national* needs or from *regional* development finance of the kind that the AfDB was created to provide.

4.05 In retrospect, it is evident that these SRDBs were seen to be necessary adjuncts to other sources of finance at a time when: DFIs were in vogue, private financing options were limited, and 'development finance' from sources like the World Bank, AfDB and bilateral donors was the only type of funding available for infrastructure and other large projects in developing countries at the time. It was also the type of finance that was felt could best be mobilised for specific sub-regional purposes through special purpose vehicles such as SRDBs.

1 In analysing the African SRDBs, this report has relied heavily on information gleaned for a previous report commissioned by the DBSA. That Report, entitled 'Report on a Background Investigation into a sub-regional Development Bank for Southern Africa' was authored by Thomas J. Beale and Jean P. Snijders of Beale & Associates CC (November 1994). The authors gratefully acknowledge their debt to that work in preparing this chapter.

2 Another SRDB for the Great Lakes States - the Banque de Developpement des Etats des Grand Lacs (BDEGL) - also exists but, as no useful information was readily available on that institution, it was omitted from the analysis.

4.06 By and large, the African SRDBs had relatively broad mandates. They could provide finance for reconstruction and development (generally defined) and were intended to foster economic integration in their respective sub-regions. They did so by: (i) helping to co-ordinate national development plans; (ii) providing member governments with technical assistance; and (iii) ensuring, through their operations, the equitable distribution of regional welfare gains across member countries, especially gains derived from intra-regional investment co-operation and trade promotion.

4.07 Specifically, member governments saw these SRDBs as instruments to implement publicly guided industrial policies, especially location policies across member states. The emphasis was on the role that SRDBs were to play in the industrialisation of the sub-region they served. Their charters required them to focus on meeting the needs of smaller, less developed economies in their sub-regions, and to focus on projects and programmes involving participation by two or more members. In only one instance, the CTDB, was the financing of intra-regional *trade* a specific function of a SRDB.

4.08 The following paragraphs convey briefly, the lessons that might be learned from the experience of each of the four African SRDBs evaluated. In evaluating these institutions the latest up to date information was generally not available. References to information for years earlier than 1996 indicate that unfortunate reality. Nonetheless, that absence of recent data does not invalidate the lessons that can be learnt from these examples. These lessons focus on three themes:

- institutional issues involved in the creation and operation of SRDBs;
- perceived versus actual demands made on SRDBs for financial products and services; and
- the overall economic impact of SRDBs on their sub-regions in terms of resource mobilisation and the outcomes of projects they financed.

The COMESA Trade & Development Bank (CTDB formerly PTAB)

4.09 CTDB was the last SRDB to be established in sub-Saharan Africa. It was created in 1985 as the PTA Trade & Development Bank (PTAB), under the Preferential Trade Area for Eastern and Southern Africa (PTA-ESA) Treaty provisions. That Treaty was succeeded by the 1992 Treaty converting the PTA-ESA into the Community of Eastern and Southern Africa (COMESA). CTDB's development (project) financing activities got off to a slow start with approvals of only US$ 7 million in 1990-91. They averaged less than US$ 10 million annually between 1992-94. Disbursements against these approvals were US$ 0.7 million in 1991, US$ 1.9 million in 1992, and US$ 3 million in 1993-94. In total, CTDB financed eight projects in as many years between 1985-92 for a total of US$ 18 million.

4.10 Given the development financing needs of its member states, these amounts were insignificant. They invalidated estimates made by the PTA Secretariat in 1985 which suggested a pipeline of *priority* projects in need of *urgent* financing in ESA amounting to US$ 12 billion including US$ 1.3 billion for industry; US$ 3.2 billion for transport and communications and US$ 1.6 billion for agriculture and food production.

4.11 Retrospectively, it is apparent that CTDB (if it was necessary at all) was established at an unpropitious time when the macroeconomic and financial conditions in Africa and ESA were at their nadir. Its location in Bujumbura, decided upon as a political compromise, also contributed to the prolonged dormancy of the institution. CTDB had to cope with the acute difficulties of operating from a war-torn capital with very poor transport and communication linkages with the rest of the sub-region. It suffered for a prolonged period from the self-inflicted tragedies of internecine conflict between Burundi and Rwanda in the 1990s.

4.12 CTDB attracted membership support from only 13 of the 20 members of COMESA, with the AfDB as a non-state member. From the outset, it experienced the following problems:

- It took an inordinately long time to appoint an effectively functioning management team. A CEO was not appointed till 1987. The staff complement of 31 comprised only 12 professionals and 19 support staff in 1990, five years after establishment. By March 1993, professional staff had increased to 25 and support staff to 27.

- Member countries were invariably late in subscribing and paying-in their capital contributions. Paid-in capital contributions amounted to US$ 9 million by 1987, US$ 40 million by 1990, and US$ 70 million by 1992. These contributions carried a 'callable' obligation in the ratio of 2:1.

- The slow pace of capital contributions affected the rate at which CTDB was able to build up staff, create a pipeline of financeable development projects, and mobilise other resources leveraged on its capital base.

- Between 1987-93 most of CTDB's income was derived from the investment of its capital in commercial bank time deposits and purchases of high-grade bonds issued by OECD governments and multilateral development banks rather than from project or trade financing loans to member countries. Its early operations thus resulted in a net capital transfer to the rest of the world from the sub-region.

- Instead of delivering on project financing, the CTDB undertook trade financing (limited to using 25% of its resources) and the issuance of PTA Travellers cheques to circumvent the problems created by closed capital accounts in member states.

4.13 The history of the CTDB was characterised by two phases. The first was an *institution-building* phase that lasted eight years up to 1992, although even then it was still debatable that an institution had been created with sufficient capacity to do what it intended. The second was an *operational* phase that began in 1992, although there is little evidence of anything significant having been accomplished since then. During the first phase, the slow rate of capital subscriptions compromised CTDB's progress towards achieving its initial objectives. Most surprisingly, despite its being created as a PTA Treaty organisation, private economic agents at the ground level in most PTA member states were unaware of its existence or its intended functions.

4.14 Contrary to the assumptions of the PTA Secretariat, there were few projects and project sponsors applying to the CTDB for finance, deterred both by lack of knowledge about the Bank and by the difficulty of dealing with it in Bujumbura. Weak institutional capacity and insufficient staff made it difficult for CTDB to identify suitable projects, undertake preliminary project feasibility studies, or pre-appraisal and appraisal work and post-loan monitoring and supervision. When projects did get into the pipeline, it was often found that project sponsors either did not comply with essential conditions and/or had failed to get the necessary approvals from their governments. Member states were unwilling to guarantee loans made by CTDB for financing projects in their countries.

4.15 CTDB did not undertake leasing or equity investment operations (up to 1993) because it did not have the internal capacity to do so. Its lines of credit to national DFIs in member states were unutilised because it had no surveillance or monitoring capacity to supervise such use. The institution decided it could not finance infrastructure or agriculture projects with ordinary resources because it felt that these required long-maturity concessional funds of the type it could not mobilise. Its project financing was thus often limited to co-financing operations with the AfDB.

4.16 To a limited extent, CTDB arranged trade financing facilities through the central and commercial banks of member states. It succeeded in mobilising a US$6 million credit line from the Indian Exim Bank and raised a total of about US$20 million in external facilities for trade finance, collateralised against deposits. Along with facilities provided by the central banks of member states, CTDB had, by the end of 1993, financed a total volume of just over US$ 45 million in pre- and post-shipment advances and letters of credit. Over a period of nine years, that was not particularly large given the trade volume of its member states. At the end of 1992 its outstanding trade loans amounted to about US$25 million in contrast to the outstanding project loans of under US$4 million.

4.17 In contrast to its intentions, the CTDB did not discount bills of exchange, nor did it provide export credit guarantees. It did not launch a revolving export credit fund nor enable forward exchange cover. It sold between US$8-12 million of PTA traveller's cheques annually between 1989-92; with Zimbabwe, Zambia and Malawi accounting for two-thirds of sales. But these instruments were not readily encashable in many member states due to limited convertibility arrangements. On that score, as well as in its trade and project financing operations, CTDB took large (potentially debilitating) exchange risks relative to its balance sheet. At the end of 1992, its total assets were about US$85 million. Over 60% of those assets were in the form of cash and time deposits with banks and less than 30% represented loans for trade and project financing.

4.18 In late 1992, the CTDB (or PTA Bank as it was then known) developed an operational plan for 1993-97. That Plan attempted to draw on experience from the weak performance of 1986-92 and tried to make the PTAB a more relevant institution for its membership. The Plan recognised explicitly that it was difficult to differentiate between the roles of national, sub-regional, regional and global DFIs when it came to financing projects in member states. It was cautious about delineating the role of a sub-regional DFI in relation to that of DFIs at other levels. The key features of the Plan included:

- Concern about not crowding out the role of the AfDB or of national DFIs and usually ending up co-financing projects put forward by these institutions;

- Focus on rehabilitation investments and those which added value to raw commodity exports;

- An emphasis on regional industrialisation, private sector investments and providing forex to industrial units for imports of spare parts and intermediates;

- Support for the reform of public sector enterprises;

- Technical assistance support but no direct lending for infrastructure projects;

- A target of US$265 million for mobilising lines of credit for project financing between 1993-97;

- An annual project lending target of US$85 million coupled with targets for co-financing mobilisation (US$70 million); equity investments (US$15 million) loan guarantees (US$15 million); buyers' credits (US$25 million); lines of credit to national DFIs (US$40 million) and technical assistance grants of US$15 million; and

- Expansion of trade finance and travellers cheques operations. The target for annual trade financing volumes by the end of 1997 was US$370 million with a widening of instruments used to include bankers acceptances, forfeiting, suppliers' credits, performance guarantees and bonds, debt swaps and a revolving export credit fund. A commercial paper programme providing US$500 million in pre-and post-export financing was launched in 1993.

4.19 Seen against CTDB's experience of 1985-92, the plan put forward for 1993-97 was ambitious. But, in the context of ESA's financing requirements, it was modest. Detailed information on CTDB's operations and finances after 1992 was not readily available and it was difficult to establish conclusively whether the plan's targets were achieved. The little information that was available suggests that CTDB succeeded in mobilising a line of credit for project financing from the AfDB for about US$20 million in 1994, but was not successful in meeting its project financing targets.

4.20 ***Lessons for SADC to Consider*:** With the membership of COMESA overlapping with that of SADC, the experience of CTDB should provide SADC members with cause for careful reflection. Contrary to expectations, CTDB has been unable to perform a substantive value-added project-financing role since it was created. It has played only a limited trade-financing role, largely because of exchange control constraints. From the viewpoint of *institutional development* and its value as an addition to the array of sub-regional institutions in COMESA, the CTDB experience showed that:

- It is difficult and costly to create a functional, effective new sub-regional DFI from scratch in an environment as difficult as that in ESA when other established national and sub-regional DFIs (i.e. the EADB) are already operating in the same domain.

- The slow rate of capital contribution by members retarded CTDB's capacity to build up its internal capacity as well as its capacity to establish an independent reputation as a credible borrower.

- The lack of credibility behind CTDB's 'callable' capital, underwritten by countries with limited creditworthiness, hindered its resource mobilisation efforts.

- Direct exposure to foreign exchange risk on the balance sheet of an SRDB can be financially destabilising and should, if possible be avoided or actively managed with sophisticated in-house financial expertise.

- There was no clear-cut case for a mezzanine level of sub-regional DFI between national DFIs and the AfDB (as a regional DFI) when it came to meeting project finance needs in PTA-ESA.

- Sound management and professionalism in staff is critical to the effectiveness of any DFI but was lacking in the CTDB.

- Active political support and will are required for the success of any sub-regional DFI; especially when it is established on political rather than economic grounds.

4.21 The CTDB case also demonstrates the disparity between *a priori* demand estimates by sub-regional secretariats (they have a vested interest in exaggerating demand) and the ground level realities, which SRDBs confront. That disparity immediately creates a credibility problem for them in establishing their role and viability when such estimates of demand prove to be unreal or impractical or, from their viewpoint, irrelevant. Despite sub-regional demand for *urgent* development financing being estimated by the erstwhile PTA Secretariat at US$12 billion in

1985, the CTDB was unable to finance projects for even US$20 million (or 0.4% of that amount) in the eight years between 1985-93.

4.22 That does not automatically suggest that demand estimates in PTA-ESA were overstated. It may suggest that a SRDB may not have been the right vehicle for meeting such demand even if it had been more accurately estimated. Indeed, the CTDB played a greater role in meeting demand for trade finance than for project finance. But even that role emerged for artificial reasons, reflecting the impact of exchange controls on intra-regional trade and the shortage of foreign exchange in ESA economies during stabilisation and structural adjustment. Under more normal circumstances - of the kind now evolving throughout SADC - such a trade-financing role is best left to commercial banks, and specialist trade financing institutions (such as discount houses, forfaiting specialists etc.) to play without let or hindrance from individual national authorities.

4.23 There is no *ex post* evaluation information available to facilitate an informed and accurate judgement about the overall economic and financial impact that the CTDB has had on the economies of its member countries. CTDB has lent minuscule amounts for trade and project finance over its life so far. That has been inevitable given the limitations of its capital base and internal institutional capacity. It would be difficult to make the case therefore that it has had any discernible impact on the economies of its member states or on achieving closer integration among them.

4.24 During its tenure, six COMESA members have become economically dysfunctional as a result of internal conflict and war. Another six have gravitated to SADC. Three have decided to revive the East African Community. These developments are not of CTDB's making. But they underline how difficult it is for a SRDB to succeed under such circumstances. Unfortunately, these have been the rule rather than the exception in Africa. The experience of COMESA with CTDB has not been encouraging. Given the lack of clarity about what different members want to get out of SADC, the main lesson for SADC may therefore be that, it would make little sense to replicate the CTDB experience by creating a new SRDB and risking a similarly desultory outcome.

The East African Development Bank (EADB)

4.25 The EADB has an unusual history in the context of the particular regional integration arrangement it was intended to support. It was established immediately after the Treaty for East African Co-operation - establishing the East African Community (comprising Kenya, Tanzania and Uganda) - was signed in mid-1967. The EAC was dissolved in 1977. But the EADB continued to function with its constitutional status suspended in limbo between 1977-80. In July 1980, its existence was confirmed with independent legal status on the basis of a special treaty unrelated to earlier regional integration objectives. Thus this particular SRDB survived the break-up of its original raison d'être and operated through two decades after which, ironically, the EAC may now be revived.

4.26 The main reason for EADB's survival and durability was the foresighted inclusion of *non-regional* members as minority shareholders in its capital structure. They included official financial institutions such as the AfDB (multilateral), FMO of Holland and DEG of Germany (bilateral) as well as private (international) commercial banks. The non-regional shareholders had Board representation that they used with members of stature. An international Advisory Panel that included people of exceptionally high calibre from the international financial community complemented the Board.

4.27 Like other SRDBs and RDBs, the EADB had a reasonably broad development finance mandate within its member states, spreading across all sectors. Operationally it narrowed that mandate down to financing industry and infrastructure. Its charter initially aimed at promoting regional economic integration. But, after the break-up of the EAC, that clause was modified to 'promoting the development of the region' in which it operated.

4.28 EADB's initial *authorised* capital stock was SDR 40 million. That was increased to SDR 80 million in 1986 and to SDR 200 million in 1992 (or about US$275 million at current exchange rates, although the SDR has fluctuated between US$ 0.98 to $1.49 between 1967-97). Of this amount 90% is Class A stock (with a 1:5 paid-in to callable capital ratio - i.e. requiring one-sixth of the value of each Class A share to be paid-in), and 10% is Class B stock with a requirement that the full value of the share should be paid-in. Of that amount nearly SDR 124 million had been subscribed by the end of 1992 including SDR 118 million in Class A shares (with a paid-in component of SDR 20 million) and SDR 5.76 million of Class B shares. Under the terms of its Charter, sub-regional member states are required to hold at least 51% of the total equity base of the EADB.

4.29 Among the first SRDB's to be established in independent Africa, with support from the World Bank and later the AfDB, the institution-building phase of EADB lasted five years. By 1972, it had established a complement of about 70 staff, with offices in each member country, more than half of whom were professionals. With political support, the EADB employed an exceptionally competent management team supported by expatriate advisors, provided by the World Bank. Considerable emphasis was placed on continuous internal staff training and professional development. EADB was managed prudently and conservatively from the outset, being profitable in every year from its inception up to 1977, when its operations were disrupted by political events beyond its control.

4.30 In its first 20 years of operation (i.e. 1967-87)[3] the EADB approved a cumulative US$ 200 million in loans and disbursed about US$ 140 million, mostly to industrial enterprises in both the public and private sectors. At the end of 1987, its outstanding loan and equity portfolio stood at about US$66.5 million. It lent mainly long-term forex loans largely because its own sources of funds were of this nature from official multilateral and bilateral lenders. But it arranged local currency and working capital funding for these projects through co-financing with local (domestic and foreign) commercial banks that it had established close working relationships with in each of the three member countries.

4.31 The EADB applied firm exposure guidelines to its lending and equity investment operations and insisted on adequate collateral being provided to secure its commercial interests. It also insisted on obtaining government guarantees when lending to parastatal enterprises. EADB operated profitably in all but one of its first 20 years. Its record was the consequence of choosing to finance only 'economically sound, technically feasible, and financially viable, projects'. Its position as a lender of forex resources led it to attach priority to forex generating export enterprises in order to reduce its own repayment risk.

4.32 Over the first 20 years of its existence, EADB established itself as a resilient SRDB, which outlived the EAC mainly because it operated on sound commercial principles. It focused its lending on the private sector. It also developed an internal institutional tradition of having a sufficiently credible, competent, independent, and professional management and staff to withstand the shocks of unwarranted political intervention in its operations but still able to muster the necessary political support to guarantee its survival when it was needed. The cumulative financial and economic impact of its lending over 20 years, given the amounts

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[3] Information quoted here is from the *East African Development Bank - 20 Year Report*, EADB, Nairobi, 1987.

involved (approvals averaging US$10 million and disbursements US$7 million annually) could not have been that substantial.

4.33 The EADB estimates that the projects it financed generated *total* investment of US$1 billion and more than 100,000 new jobs over the 20 year period. A shift in emphasis between 1977-87 towards infrastructure lending, and for projects involving at least two countries, also led the EADB to believe that it had contributed to enhancing integration; through backward and forward linkages in cross-border infrastructure and improvements in the flow of goods across the borders of its three founding member states. Further, the EADB estimated a net positive effect of its cumulative operation's on the sub-region's overall balance of payments because of its emphasis on financing forex-generating or forex-saving projects. These estimates are difficult to corroborate independently without primary evaluative research.

4.34 By its admission, but not through any fault of its own, the EADB failed to foster closer integration among its member states or to achieve more balanced economic development through the sub-region it was created to serve. The reason was that two of its three member countries (Kenya and Tanzania) opted for diametrically opposed economic regimes. Kenya chose a mixed-market capitalist model for economic development, while Tanzania opted for extreme socialism. Uganda descended into an economic abyss under the rule of Idi Amin and was later engulfed by a debilitating war. When the EAC broke-up, because its internal political tensions had become too great to accommodate, these 'integration' objectives were dropped from the revised EADB Treaty and Charter in 1980. There is a clear lesson to be learnt by SADC from EADB's experience in this respect. It is that SRDBs cannot achieve integration or equity objectives across sub-regions, or even achieve any significant economic impact in the absence of political commitment. That holds true no matter how strong the institutional sinews of SRDBs might be. Their role is inevitably diminished and vitiated when there is no political will to ensure peace and stability, pursue a common economic agenda, or co-ordinate investment and macroeconomic policies within a coherent framework.

4.35 The EADB's fortunes have been more mixed in the last decade (1988-97) although the erosion of its financial base began as early as 1982. It has suffered progressively from the cumulative effects of misguided domestic economic policies and poor governance in its member countries through most of the 1970s and early-1980s, and of the adjustment programmes later imposed to correct them in the late-1980s and 1990s. The forex risks passed on to its clients have rebounded on it since many of its clients have gone into sustained default or receivership. These clients have been severely affected by the combined effects of sudden import liberalisation, acute forex shortages to keep their plants running at acceptable utilisation levels, sharp and sudden increases in domestic interest rates coupled with spiral devaluations of domestic currencies. Moreover, even the government guarantees which were meant to have protected the EADB from arrears and defaults by parastatals have not been honoured on time due to strict budget constraints.

4.36 The level of EADB's lending operations have declined due to both its worsening portfolio performance as well as a reluctance on the part of borrowers to borrow in foreign currency and assume forex risks. It has been unable to mobilise long-term domestic currency resources for lending in its member states. Markets for such funds are only just emerging in its member states and the EADB would be competing with governments and national DFIs in thin and volatile markets for mobilising such funds. Consequently the EADB has shifted to deploying more equity resources from its international shareholders and Special Funds from donors (especially the Nordic donors such as Denmark, Norway and Sweden) for special purposes such as the rehabilitation of Ugandan industry.

4.37 For a relatively prudent and conservative institution which attempted to cover its risks in every way it knew, it was a reflection of EADB's helplessness in the face of circumstances beyond its control, that its provisions for doubtful debts in 1991 amounted to over 25% of its portfolio. In that year, 54% of its loans were in non-accrual status: i.e. in arrears for so long that income from affected loans could not be accrued and the principal outstanding had to be provided for to insure against the increasing likelihood of non-repayment. EADB's financial situation deteriorated from 1987 onwards and became so serious that it virtually suspended operations between 1989-91 until a financial restructuring exercise undertaken by independent international auditors was completed.

4.38 Contrary to the unblemished record of its first two decades, EADB incurred net losses between 1989-91 because of increasing provisioning requirements. It reverted to a small profit in 1992. However, income from project loans kept declining till 1994 as a result of a slowdown in lending. At the end of 1992, EADB's loan and equity portfolio amounted to about US$140 million with net assets at US$ 117 million and 80% of its portfolio not providing a satisfactory yield. Fifty per cent of the portfolio was not performing (with interest and principal in arrears), while a further 30% represented projects at various pre-operating stages of implementation. Completion of these projects was delayed for a variety of reasons, mainly a shortage of funds on the part of sponsors. In the mid-1990s the portfolio situation had improved but not as rapidly as might have been hoped earlier.

4.39 The Plan to revive the fortunes of the EADB, which followed the financial restructuring exercise, recognised that, in the 1990s, the EADB would have to adjust to changes in its operating environment resulting from adjustment programmes. It would also need to adapt to changes in local financial systems and markets reflecting changes in domestic economic policies and different priorities of the multilateral and bilateral donor community. Accordingly the revival plan recommended:

- emphasis on improved collection and recovery and a consequent reduction in the need for provisions;
- a shift from forex to domestic currency lending with implications for greater reliance on increasing equity resources and on special funds provided on concessional terms without forex risks being passed on;
- improving profitability through greater reliance on fee income and further diversification of EADB's range of technical assistance and financial advisory services;
- capturing opportunities presented by privatisation programmes in its member states; and
- a programme of internal institutional strengthening and capacity-building.

4.40 In the long-run, the revival plan pointed to EADB's gradually converting itself into a European-model 'universal bank' combining investment and commercial banking functions. During the 1990s, the EADB has implemented parts of that plan with a measure of success. It has succeeded in increasing its capital base and diversifying its sources of special funds. It has mobilised more resources from the AfDB (through a US$ 20 million loan in 1994) and Japan Exim Bank (US$ 7 million) specifically to support the rehabilitation and expansion of SMEs in the three member states. The latter task could have been performed just as easily by the national DFIs in the countries concerned.

4.41 EADB has made less progress with implementing some of the more far-reaching and imaginative recommendations of the revival plan. These included:

- mobilising and lending short and long-term domestic currency resources;
- increasing venture capital and equity financing;

- structuring internationally funded debt-swap programmes for a variety of purposes;
- leasing and securitised lending;
- providing privatisation advisory services and regional financial services; and
- playing a key role in the cross-border initiative for ESA sponsored by the AfDB, EU and World Bank.

4.42 Arguably, the economic impact of EADB on its sub-region between 1987-97 was less than in the previous two decades. This was mainly because: (i) the impact of its lending was vitiated by the consequences of adjustment programmes; and (ii) the first half of the 1990s was taken up by emergency measures to ensure its survival. The EADB has proved beyond any doubt that a robust DFI, once created, generates its own dynamic for survival (especially if it a relatively competent institution) regardless of whether a real economic role exists for it or not. EADB's institutional capability, resilience and 30-year history notwithstanding, its experience still raises questions about whether its establishment as a SRDB for the EAC was really necessary. It is difficult to assert that the EADB made a unique contribution at the sub-regional level that could not have been achieved either by national DFIs or the AfDB without this mezzanine level of intermediation.

4.43 But EADB's survival in an environment where such institutions are difficult to create in the first place is an accomplishment that should not be dismissed too easily. EADB's experience in surviving, even when its main raison d'être (the EAC) had disappeared, is a curious phenomenon in the annals of SRDBs. It is a strong testimonial to the competence and quality of management of the institution, and of its will to survive in the face of formidable odds. But it provides no valuable pointer confirming the utility or necessity of the economic functions it performed. Nor does it serve to change the reality that, at the end of it all, the EADB - though an indisputably worthwhile institution in its own right - had a limited impact in achieving the economic, financial, development and sub-regional objectives it was established for.

4.44 ***Lessons from EADB's Experience:*** Clearly the *first* broad lesson to be learnt from EADB's experience is that it is not necessary for a regional integration arrangement to exist in order for a sub-regional DFI to survive; even though it may be necessary for such an arrangement to exist to justify setting up a SRDB in the first place. The *second* broad lesson is that once a publicly-funded inter-governmental institution is established it is virtually impossible to terminate it, providing it has strong enough management and sufficient external support, even if the main reason for its role disappears.

4.45 Apart from those two odd lessons, the EADB provides other lessons as well as warnings in considering whether SADC needs its own SRDB. These include:

- The value of involving, in a productive manner, *non-regional* shareholders from donor countries, or of a multilateral hue, who are able and prepared to work with a competent management to defend the interests of the institution under difficult political circumstances. Generally in Africa there is reluctance to involve non-regional shareholders on the grounds that this ultimately results in loss of sovereignty and control. On the other hand it also results in usable sources of funds being excluded from participation in institutions which only they have the financial capacity to keep going.

- The importance of having, credible, competent and professional top executives, management and staff with the courage to withstand counter-productive political intervention yet able to muster political support for the right reasons at the right time. Most African DFIs, whether sub-regional, national or even regional have not usually been blessed with such executives and management.

- The value of having SRDBs and DFIs lend mainly to the private sector and not put all their eggs in the parastatal basket.

- The dangers of unmanageable forex risk exposure in the financial operations of SRDBs. It is not enough to be sanguine about passing these risks on, especially in circumstances of systemic collapse and high-pressure adjustment, under which the exchange rate undergoes spiral devaluation. The EADB example clearly demonstrates that even a soundly managed institution can be brought to the brink of insolvency by relying too heavily on intermediating forex loans from other sources of official finance and not diversifying its sources and uses of funds.

- The limitations of providing *development finance* as the main financial product from the viewpoint of an institution's evolution and growth. As time goes by that limitation becomes increasingly evident.

- The inherent weakness of relying on the guarantees of governments (to cover borrowing by their parastatals) whose creditworthiness is being eroded.

- The spectacular 'own goals' that governments can score in debilitating their DFIs through sustained policy default as well as those that MDBs can score in debilitating their DFI borrowers through adjustment programmes whose negative consequences are not adequately provided for in their design. Both involve *moral hazard* on the part of government shareholders and MDBs that are not admitted by either.

- Managing a non-performing portfolio and extracting residual value from such portfolios is an expensive process requiring special skills which most SRDBs and African DFIs do not have and find it difficult to develop.

- Development finance is not simply a matter of mobilising resources from foreign donors and MDBs. It requires mobilising domestic savings and devising financial securities that offer sufficiently attractive inflation-proof returns to local and institutional investors and individuals.

- Even well-managed SRDBs are not good vehicles for implementing industrial location policies, which are inconsonant with underlying economic fundamentals, location comparative advantages and infrastructure imperatives. Thus the objective of dispersing industrial investment across poorer parts of African sub-regions is a task which even the more capable SRDBs have failed at.

- In situations of continuing political flux, strong regional institutions such as the EADB can not just survive the breakdown of their founding regional integration arrangements. They can help to create conditions that result in the resurrection of defunct or dormant integration arrangements. This is especially true when such arrangements are conceived for the right reasons, break down for the wrong ones, and have ripened for revival as circumstances changed. But the corollary is that such institutions also involve a cost that needs to be properly counted and assessed.

4.46 What is surprising is that when the PTA was formed, its member governments did not consider the possibility of utilising a strong extant institution like the EADB as the central pillar around which a PTAB, that served more countries, could be built. This lapse of rationality afflicted the donor community as well; in particular the AfDB, which was a shareholder in both institutions. It is difficult to discern from available historical records whether this rather obvious option was ever considered. If not, it would be interesting to know why. If it was considered it would be instructive to learn why PTA members opted for setting up a new SRDB, which did not have any prospect of developing even a fraction of the institutional capacity that the EADB already had and that was being under-utilised.

4.47 Had that option been taken, the outcome might have been quite different for the PTA and EADB. One strong SRDB with proper capitalisation, a wider operating ambit, and a clearer sub-regional mandate, might have succeeded - all other things being equal - as BOAD did in Francophone West Africa. Instead the creation of a new SRDB resulted in two SRDBs operating in the same sub-region and both being compromised. That step resulted in the extant institution (EADB) being weakened and the new institution (PTAB/CTDB) never getting off the ground. Answers to these questions are important in understanding some of the issues, which the SADC membership faces in considering the possibility of setting up a new SRDB instead of building around one that already exists.

Banque de Developpement des Etats de L'Afrique Centrale (BDEAC) or The Development Bank for the Central African States

4.48 BDEAC was established eight years after the EADB by the Central African Customs and Economic Union (UDEAC) and about eleven years after UDEAC was formed under the Brazzaville Treaty in 1964. Cameroon, Central African Republic (CAR), Chad, Congo, Equatorial Guinea and Gabon were its members. Complementing UDEAC (in much the same way as the MMA complements SACU), the Central African Monetary Union (UMAC) was established in 1972 with the Reserve Bank of the Central African States (BEAC) at its centre. Under UMAC, the Central African States adopted the CFA franc (CFAF) as a common currency throughout the sub-region, underpinned by arrangements with France aimed at protecting its stability, value and convertibility. The CFAF was also the common currency of the countries of francophone West Africa under a similar monetary union, UMOA. Till January 1994 it was freely convertible into the French franc at a rate of 50 CFAF to 1 FFR and through the FFR convertible into any other hard currency as well. In January 1994 the CFAF was devalued to 100 CFAF = 1 FFR.

4.49 In retrospect the failure to adjust the parity value of the CFA franc early enough was a major error of judgement on the part of all governments and economic authorities involved. The lapse occurred despite repeated warnings and pressures applied by the IMF and World Bank for over two years. The value of the CFAF was maintained at an unrealistically high level for too long. Surprisingly, that happened with French Treasury and Banque de France support!

4.50 It was a policy failure that resulted in all francophone African economies becoming progressively uncompetitive for three years. That unfortunate reality encouraged large-scale smuggling across borders of much cheaper basic goods imports from anglophone West African states. It resulted in the progressive de-industrialisation of francophone Africa. It also triggered sustained capital expatriation by the UDEAC's private and public sectors, through entirely legal channels. That inflicted considerable damage on all member economies unable to use the exchange rate as a tool for economic adjustment. Denied that possibility, UDEAC countries had to rely instead on fiscal and monetary contraction to bring about necessary demand adjustments which eventually led to inevitable economic implosion and a long delayed re-acquaintance with economic reality.

4.51 The common currency, customs union and *taxe unique* - levied on industrial enterprises exporting within member states to fund compensatory transfers from the richer to the poorer countries of the sub-region - combined to form a much closer regional integration arrangement in UDEAC than was the case in the EAC or ESA. Internal transfers from the *taxe unique* were made directly through budgets (as with SACU customs revenues) rather than via a SRDB. It was felt, in keeping with the ethos of the times, that a SRDB would nevertheless be useful in further enhancing sub-regional integration. Accordingly, the BDEAC was created to promote the economic and social development of member states by: (i) financing *multinational* and *integration* projects; (ii) helping member states to mobilise financial resources for projects important to their national economies; and (iii) financing feasibility studies of *regional* projects. The shareholders of BDEAC included all UDEAC members (as well as the Reserve Bank, the BEAC) as sub-regional shareholders and the AfDB, France, Germany and Kuwait as the *non-regional* members. The participation of non-regional shareholders, capable of providing sustained financial support, made BDEAC's capital structure similar to that of the EADB.

4.52 BDEAC's 20-year history can be divided into three phases. Its institution-building period between 1977-81 saw the gearing up of its operational capability. BDEAC lending in those four years averaged nearly CFAF 1.4 billion (about US$ 5 million) for 3-5 projects per annum. The next decade, covering its first two 5-year plans (between 1982-91) saw BDEAC enter a second phase of steady (if not dramatic) expansion. Annual lending approvals rose to an average of about CFAF4.85 billion (about US$20 million) for about 6-8 projects each year. Between 1982-86, BDEAC benefited from the effects of surplus oil revenues generated by the coastal UDEAC states (especially the Congo and Gabon) until their profligacy caught up with them. The 1986-91 period was more difficult as the consequences of adjustment became reflected in its portfolio.

4.53 But, after 1991, BDEAC entered its third phase of dissipation and portfolio collapse. Worsening economic conditions throughout the sub-region, the increasing indebtedness of UDEAC countries including its oil-rich economies, and the impact of structural adjustment programmes, had their inevitable impact on BDEAC's portfolio. The negative consequences were the same as those afflicting every DFI in Africa and hitting the SRDBs particularly hard. In BDEAC's case, average lending approvals between 1991-93 plummeted to CFAF2 billion (or about US$7 million) for one project each in 1991 and 1992 with operations coming to a halt in mid-1993. In that year, BDEAC was restructured with a halving of its staff complement to a total of 46, remaining with only 22 professional staff.

4.54 Between 1977-93, BDEAC had cumulatively financed about 85 projects in all for a total of about US$ 230 million equivalent. Of these only six could be classified as *sub-regional* projects with the rest being national projects, which could have been financed by national DFIs. A club of national DFIs, working with the AfDB under co-financing arrangements, could have financed even the sub-regional projects. Thus the need for a SRDB to finance sub-regional projects was not borne out by BDEAC's operating experience. Most of its lending (nearly 80%) was in the form of loans to sovereign governments or to their instrumentalities mainly with government-backed guarantees constituting the only effective collateral which BDEAC had. Private sector loans backed by adequate 'real' collateral accounted for just 20% of its total loan portfolio.

4.55 BDEAC loans were concentrated in infrastructure (transport, communications and electricity). Its largest loan (CFAF1.5 billion or US$7 million) was for Air Afrique, the regional airline for francophone west and central Africa. BDEAC managed a number of concessional special funds to finance feasibility studies and technical assistance. These were financed by the EIB and by the Swiss and German governments. Cumulatively it financed technical assistance amounting to nearly CFAF 1 billion, mainly for rural development projects. Only five of the feasibility studies it financed were for sub-regional projects. It also provided an umbrella for the Basic Rural Development Fund for UDEAC which was founded in 1989. That Fund had its own administrative structure and management committee presided over by the Director-General of the BDEAC.

4.56 In 1992, the recovery rate on principal and interest payments due from all clients dropped from over 85% in 1991 to less than 20%. By mid-1993 it was below 7%. The non-performing portfolio accounted for over 75% of the total portfolio with 50% representing sovereign loans or loans backed by sovereign guarantees which, as in the case of the EADB, were not honoured on time. Thus, an institution that was profitable for most years between 1978-89 began to make operating losses from a deteriorating portfolio. The deduction of provisions for bad loans from income resulted in BDEAC incurring a loss of CFAF 1.5 billion (or about US$ 6 million) in 1992, despite cutting its operational costs in half through radical retrenchment.

4.57 In mid-1993 BDEAC's total assets were equivalent to effective capital employed (i.e. total liabilities) of CFAF 35.5 billion (or about US$130 million) against an authorised capital base of CFAF 57.25 billion (about US$210 million). The paid-in component of BDEAC's capital amounted to CFAF 22.9 billion (US$ 85 million). Of this amount CFAF 2.1 billion (US$ 8 million) from sub-regional shareholders was in arrears. A further CFAF 1.1 billion due from France and Germany was also in arrears at the time, resulting in available paid-in capital of CFAF 19.7 billion (or about US$70 million). The balance of CFAF 15.8 billion (or about US$60 million) in resources (liabilities) represented funding from long-term loans extended by the AfDB and others. There was also a callable component of CFAF 34.35 billion (US$125 million) attached to the capital base that represented implicit regional shareholder guarantee support for BDEAC's borrowings.

4.58 For BDEAC, the CFAF was its unit of account. It was a convertible currency whose value had held against the FFR for over 15 years. Yet, BDEAC's loans were often denominated in foreign currencies (FFR or USD or a basket of currencies) depending on the nature of its own borrowings. It passed these on without (supposedly) taking any exchange risk on its own books. However, the period between 1978-93 saw at least three cycles of fairly large and volatile movements in the FFR (and therefore the CFAF) exchange rate versus the USD, which resulted in large exchange risks materialising for BDEAC's clients.

4.59 These risks were unhedged. Unable to bear them when they materialised, its clients passed them back to BDEAC via arrears and default. Where exchange risks were concerned, the devaluation of the CFAF in January 1994 was the final straw. BDEAC's effective paid-in capital was halved in USD terms from US$70 million to under US$35 million since there were no maintenance-of-value provisions. At the same time its liabilities in CFAF terms doubled. The sudden change in its gearing resulted in BDEAC's liabilities no longer being fully covered by the callable part of its authorised capital.

4.60 In its capital structure, the principle of equal contributions was applied to the four larger, richer countries, i.e. the Cameroon, CAR, Congo and Gabon. They held equal shares of 13.92% each, requiring capital subscriptions of CFAF 7.97 billion (US$30 million). The poor countries - i.e. Chad and Equatorial Guinea - joined later. They contributed CFAF 7.08 billion (12.37%) and CFAF 2.85 billion (4.98%), respectively. Thus the sub-regional members held 70.9% of BDEAC's total shares. Of the other shareholders, the BEAC held a further 11% with the total sub-regional shareholding thus amounting to nearly 82%. France was the next largest non-regional shareholder with a shareholding of 6.55%, leaving the remainder of about 11.65% of the shares being divided between the AfDB, Germany and Kuwait. The regional shareholdings had paid-in to callable obligations in a ratio of 1:2 while the non-regional shareholding was entirely paid-in.

4.61 In 1993, its serious exchange risk and portfolio problems resulted in BDEAC undertaking a radical restructuring financed by the World Bank. The restructuring measures recommended were almost identical to those recommended for EADB and included:

- stern actions to improve debt recovery and collection of arrears and upcoming dues especially from member states and their parastatals;

- writing down the portfolio to realistic values, taking into account genuine recovery possibilities from the portfolio, i.e. marking-to-market the value of the residual portfolio and writing down the rest through reductions of net income, accumulated provisions, reserves and capital in that sequence;

- cancelling undisbursed balances of loans committed for unviable projects;

- cancelling disbursement of loans to governments or parastatals whose debt service to BDEAC was late by more than six months;

- searching for other sources of funds to finance BDEAC's undisbursed commitments to projects which could be restructured and 'saved';

- switching to a policy of making loans in CFAF, supported by borrowings in CFAF;

- reducing reliance on sovereign loans and guarantees to back its portfolio;

- abandoning its 'quota system' in hiring management and staff from member states and relying more on merit criteria to guide recruitment and staffing policies;

- participating pro-actively in restructuring client enterprises; and

- matching its assets and liabilities more carefully (in terms of currency structure, maturity, duration, cost and risk).

4.62 In 1994-95, BDEAC implemented a restructuring plan incorporating these measures and is now emerging from its problems as a smaller, leaner institution. Its balance sheet had shrunk to under US$60 million in 1996 against a total of over US$130 million in 1993. How relevant it remains to meeting the development financing or even external financing needs of its sub-region is a matter of argument. On balance, it is neither significant nor relevant except to the very smallest economies in UDEAC whose own financial condition would not permit them to mobilise the incremental resources that the BDEAC is still capable of raising for them.

4.63 Like EADB (but unlike CTDB), BDEAC started out as a promising institution. It might have achieved much more had it not been reversed in its own tracks by circumstances beyond its control. First, its prospects were blighted by the misguided economic policies of member governments. Later its balance sheet was impaired by the consequences of the inevitable corrective structural adjustment programmes that ensued. EDB had to cope with the same problems. But BDEAC did not have the same quality or capacity of management or the same professionalism in its staff as EADB. Instead it applied quotas to achieve nationality representation in its staff instead of pursuing policies that made staff competence and capacity the overriding priorities in its recruitment and selection practices, relegating the pursuit of having a representative staff to secondary status.

4.64 ***Lessons to be learnt from BDEAC's experience:*** The lessons from BDEAC's experience for SADC are similar to those from the EADB with perhaps the following additional ones to be taken note of:

- Governments in Africa have been enthusiastic about establishing SRDBs in various sub-regions. But they have not shown the same enthusiasm for meeting their capital and guarantee obligations to these institutions.

- Priority on having representative management and staff through quota-based hiring has resulted in the subordination of efficiency and capability criteria, compromising the institutional ability and prospects of the SRDBs created.

- Assets and liabilities need be matched with SRDBs undertaking pro-active risk management to ensure that their exposure to currency risk, term transformation risk, interest-rate risk and volatility risk is contained within manageable bounds.

- UMAC has tighter integration arrangements than hold in SADC. Its arrangements are similar to SACU-MMA. Yet BDEAC's role was found not to be justified or vindicated; there was no special niche which only a SRDB was needed to fill.

- Lending to member governments and parastatals is a risky business for SRDBs and has proven to be their undoing. Such institutions, if they are needed at all, need to focus their lending mainly on the private sector and avoid lending to the public sector for non-commercial projects which do not have independent cash-flow streams which can be attached or escrowed for debt servicing purposes.

- In current circumstances, where SRDBs exist they should help governments to privatise rapidly and encourage the development of sub-regional cross-holdings in post-privatised enterprises.

- SRDBs are particularly vulnerable to the pressures of adjustment and structural change in member economies. These often compromise the financial viability of their client bases and its portfolios. Whereas national DFIs are exposed to the risks of economic deterioration and adjustment in one economy, SRDBs are exposed to such risks in several.

Banque Ouest Africaine de Developpement (BOAD) or the West African Development Bank.

4.65 BOAD is the mirror image of the BDEAC in Francophone West Africa, although its operating history suggests that it has been more successful; perhaps even the most successful of the African SRDBs established so far. It was founded under the West African Monetary Union (UMOA) arrangements of 1962 (revised in 1973 and again in 1994) with the Central Bank of the West African States (BCEAO) at their centre. The members of UMOA are Benin, Burkina Faso, Cote d'Ivoire, Niger, Senegal, Togo and Mali. Like UMAC, UMOA also uses the CFAF as its common currency under similar arrangements with the French Treasury and the Banque de France.

4.66 BOAD's mandate is to promote the balanced development of member states and ensure the economic integration of West Africa by financing priority infrastructure projects (in transport, telecommunications, and electric power) as well as projects in industry, agro-industry, rural development, tourism and other commercial services. Although empowered to operate in non-member states (with the anglophone West African states in mind) BOAD has not yet done so. The principal shareholders of BOAD include the seven (Class A shareholder) members of UMOA and the BCEAO as the sub-regional members whose shareholdings carry callable capital obligations along with their paid-in portions in a ratio of 2:1. The non-regional (Class B) shareholders whose full share values have to be paid-in include Belgium, France, Germany (DEG), the AfDB and the EIB. The total non-regional share is limited to one-third of the total number of Class A shares in order to ensure sub-regional dominance of the institution.

4.67 The single largest shareholder of BOAD is the BCEAO (the sub-regional central bank) with 46% of subscribed and 35% of paid-in capital; making BOAD an affiliate of BCEAO, an unusual arrangement among SRDBs. BCEAO is represented on BOAD's Management Committee (the institution's key policy-making organ) but has a frequent and continuing dialogue with BOAD at operating management and staff levels as well.

4.68 Reflecting the strong political support that BOAD receives from its member states, the President of BOAD is appointed by the Council of Ministers of UMOA. The presidency of BOAD is regarded as a key executive position of stature in the sub-region. The Management Committee comprises the President of BOAD and the Governor of BCEAO, as well as statutorily appointed representatives (and alternates) nominated by UMOA governments. Non-regional shareholders are also represented on the Management Committee in proportion to their shareholding. *Prima facie* the influence and involvement of member governments in determining the make-up of BOAD's management and board may appear to be overbearing for a SRDB. But in practice such involvement has been translated into constructive support. That has been a key ingredient in assuring BOAD's relative success and continuing relevance in its sub-region.

4.69 The other factors contributing to BOAD's relatively better performance include:

- The stature and calibre of the senior executives appointed to head BOAD and BCEAO and their closeness in working together on sub-regional integration issues;

- The close operating relationship between the sub-regional central (BCEAO) and development (BOAD) banks,

- The clear delineation of functions and operational responsibilities between BOAD and the national DFIs (where BOAD acts as a funds wholesaler and the national DFIs act as retailers especially for lending to SMEs and rural enterprises), and

- The relationship between BOAD (sub-regional) and the AfDB (regional).

4.70 BOAD commenced operations in 1976, almost at the same time as BDEAC. But it has undertaken a wider range of activities. Lending for infrastructure accounted for 42% of cumulative lending up to 1995, while lending for agro-industrial and industrial projects accounted for 12%. BOAD also participated in the equity of public and private enterprises (3% of total loans/investments) and of DFIs in member countries. These, in turn, financed SMEs via BOAD lines of credit to them. Loans and investments to DFIs accounted for 9% of total loans/investments while loans for rural development projects, at subsidised interest rates, accounted for 34% of cumulative lending. Country-wise, Senegal received 24% of BOAD's total loans; the Cote d'Ivoire 20%; Benin, 17%; Burkina Faso, 17%; Niger, 12%; Mali, 5%; and Togo, 5%.

4.71 About 76% of BOAD's financing was for national projects while 24% was for 33 *sub-regional* projects. BOAD found that invariably sub-regional projects were poorly prepared, rarely harmonised with national policies or cleared by national institutions. External sponsors usually promoted them, because there was a scarcity of sub-regional sponsors with adequate skills or capital, and with insufficient co-ordination between other sub-regional organisations involved in project design or implementation.

4.72 Complementing its lending operations BOAD, like BDEAC and EADB, has managed a number of special funds which have been financed by: endowments from member states and non-regional governments and institutions, and contributions from the BOAD budget after profits, user levies and charges. These funds include: an Interest Subsidy Fund, the Fund for Financing Feasibility Studies, a Backing Guarantee Fund, a Redemption Guarantee Fund, a Fund for Participation and Assistance, an Exchange Risk Cover Fund and a Private Sector Investment Guarantee Fund for West Africa; which was set up in co-operation with BCEAO and the Caisse Francaise de Developpement. The BOAD's technical assistance grant funds have been supported by contributions from the Belgian and Swiss governments while co-financing arrangements for projects have been entered into with the AfDB as well as the EXIM Bank of Japan.

4.73 BOAD began with annual approvals of US$5.2 million for three projects in 1976, with fewer than 15 staff. By the end of 1995 it made cumulative commitments in excess of CFAF 220 billion (over US$370 million) with disbursements exceeding CFAF 150 billion (US$ 250 million) over those 20 years. By then it had a total staff complement of about 100, two-thirds of whom were professionals. It had financed a total of 135 projects and made 15 equity investments, with the commitment rate (for loans and investments) between 1990-93 (before the CFAF devaluation) running at about US$ 20 million for 10-12 projects per year. In 1994-95 the amount of lending nearly doubled in CFAF terms, but remained the same in dollar terms, although the number of projects financed annually increased marginally to between 12-15. About 18% of its portfolio represented loans to, and investments in the private sector especially in the private financial sector. BOAD has also been successful in mobilising funds from the domestic sub-regional capital markets with bond issues of about CFAF 5 billion.

4.74 The overall increase in approvals between the second half of the 1970s (averaging CFAF 2.5 billion annually) and the first (pre-devaluation) half of the 1990s (averaging CFAF 5 billion annually) did not represent a significant compound increase in annual operations. It represented no increase at all in real terms. Like BDEAC and EADB, the BOAD was hit by a worsening operating environment with most of its member states in the grip of crisis-induced adjustment programmes between 1991-94. But, unlike the other two SRDBs, it was not so badly affected by a deteriorating portfolio as to make losses or require radical capital and organisational restructuring although it was severely affected by the CFAF devaluation of 1994.

4.75 Since 1992, the BOAD has concentrated on three priorities: (i) improving and extending sub-regional infrastructure linkages in transport, telecommunications and energy; (ii) financing projects aimed at helping the sub-region to achieve food self-sufficiency; and (iii) working with BCEAO to strengthen the sub-region's banking systems and financial markets. BOAD was actively involved in financing and participating in a study on the feasibility of creating a sub-regional capital market within UMOA in the context of its desire to achieve full economic and monetary union by the end of the present century.

4.76 BOAD's involvement in bolstering the financial systems of member countries has widened and deepened considerably between 1992-96. It has financed and provided technical assistance to local commercial banks. It has purchased equity in them and played a direct, strategic policy-making role on their Boards as well as on the Boards of national DFIs. It has also acted as a trustee and fiduciary agent for some of the national central banks in the sub-region. BOAD acquired substantial stakes in private sector banks in Benin and Mali to which it also extended refinancing facilities. Unfortunately, BOAD also played a leading role in acquiring a large stake (of CFAF 3 billion or US$ 6 million) in a private commercial bank with a sub-regional network (Meridien-BIAO SA Holdings) on behalf of UMOA members. That bank, promoted and built-up by investors from Zambia, eventually failed, leaving BOAD and other shareholders with a serious financial crisis to clean up.

4.77 At the end of 1995, BOAD's balance sheet showed total assets of CFAF 250 billion with total loans outstanding of CFAF 130 billion, equity investments of CFAF 10 billion, and with provisions of about CFAF 7 billion against doubtful loans. Its liabilities included CFAF 40 billion in long-term borrowings, special fund liabilities of CFAF 35 billion and statutory reserves of CFAF 25 billion. Although an increasing number of accounts had fallen into arrears between 1991-94, BOAD took early corrective action. Consequently it did not face the same problems as those faced by BDEAC and the EADB in collecting on government guarantees and on ensuring that member states made capital calls and contributions on a timely basis.

4.78 Despite the salutary experience of BOAD over its 20-year operating life, the basic question still remains as to whether a sub-regional institution like BOAD was needed in francophone West Africa. Did it do anything unique which neither national DFIs nor the regional RDB (i.e. AfDB) could have done? It managed to lend only an average of less than US$ 20 million for about 9 projects each year throughout its operating life; hardly the kind of amount that would make it worthwhile creating a sub-regional SRDB for. Yet, remembering that the financing alternatives (especially for the private provision of infrastructure) which exist today did not exist then, BOAD probably did play a useful sub-regional role, but then for very particular reasons.

4.79 To begin with BOAD carved out a niche for itself as a provider of wholesale funds to national DFIs which they retailed on its behalf but at their risk. BOAD also took up equity stakes in these national DFIs and played a role in their internal policy-formulation and decision-making processes. Thus it helped to create a sub-regionally inter-linked network of DFIs, with itself at the hub, in a financial, institutional and technological sense. This action immediately delineated the role of BOAD vis-à-vis national DFIs in terms of areas of activity and size of projects financed; leaving SME and rural enterprise financing to national DFIs and concentrating its own lending operations on larger infrastructure and industrial projects whether sub-regional or national in nature.

4.80 At the other end of the scale, BOAD co-opted and co-financed projects with the AfDB, relying on its project identification, appraisal and supervision capacities. Moreover, as a credible regional institution BOAD, in an era when international development financing was still in vogue, became the vehicle of choice for bilateral and multilateral lenders wishing to channel their funds to that region for a variety of development purposes more efficiently than they could have done. It therefore fulfilled a useful resource mobilisation and financial unbundling role for its sub-region for development funding from official sources in a manner that would be difficult to replicate in present circumstances.

4.81 ***Lessons to be learnt from BOAD:*** From the relatively better experience of BOAD, the lessons for any other sub-regional arrangement wishing to set up its own SRDB would include the importance of:

- Strong political support and constructive government involvement (rather than counter-productive political interference) in supporting the SRDB's policy and decision-making mechanisms and protecting its financial status.

- Establishing appropriate institutional connections with other key sub-regional financial institutions at the outset. In BOAD's case its unusually close relationship and shareholding linkage with BCEAO was critical to its success as a SRDB.

- Making the SRDB an institution of considerable stature within the sub-regional institutional framework (comprising the secretariat, the central bank and BOAD).

- Delineating clearly at the outset the roles of national DFIs, the SRDB and the RDB (AfDB) to avoid unnecessary overlap while ensuring seamless co-operation across these institutions to cover all sectors of activity and all sizes of projects.

- Establishing a co-operative rather than competitive ethos across DFIs at these three operational levels (i.e. the national, sub-regional and regional).

- Involving the SRDB in wider efforts aimed at financial system development and in the sub-regional co-ordination of commercial banking and other financial markets.

- Moulding the functions and activities of the SRDB around the core integration concepts being pursued with all members subscribing to a common view of what such integration concepts and efforts involved. That ensured that its shareholders and clients saw the SRDB's financial products and activities as relevant to their needs and to the integration enterprise as a whole.

- Involving the SRDB intrinsically in the overall integration effort.

Overall Lessons to be learnt from the Experience of African SRDBs

4.82 The specific lessons learnt from the experience of each of the four SRDBs examined above have been distilled at the end of each section. The main observations are pulled together and recapitulated hereunder. Three of the four African SRDBs failed to fulfil their promise, while the fourth met expectations to a modest extent, at least from an activity if not from a financial transfer point of view. On closer examination of their history and evolution, this generally desultory record of African SRDBs might be attributed to the following reasons (and where the record was better, i.e. in the case of the BOAD, because these reasons did not apply):

- A lack of clarity about the mandates, objectives, roles and functions of SRDBs vis-à-vis those of national and regional DFIs in their respective areas of operation. Where there was a clear understanding of this issue and a clear delineation of roles (i.e. BOAD), the outcome was discernibly more productive.

- An axiomatic presumption that there had to be a special need for institutions at the sub-regional level in order to provide development finance inputs, without that presumption being tested before the SRDBs were set up. In other words, it was presumed that development finance was needed, in whatever quantity, without the actual demand function for such finance being properly analysed and established on a sectorally and geographically desegregated basis.

- Relatively poor management and direction along with staffing and board direction based on political concerns about 'equitable sub-regional representation' in the management and staffing of SRDBs with less priority on competence and capability criteria. This led (in CTDB and BDEAC) to institutional dissipation in the face of unanticipated pressures. Where management was more confident and staff more capable (as in the EADB and BOAD), these institutions withstood crippling pressures and survived even if they did not fully meet their original expectations.

- In African regional integration arrangements outside of UMOA, there was insufficient political commitment to ensuring the success of the SRDBs established. In one instance, the regional arrangement (EAC) supporting the EADB was actually dissolved, depriving that SRDB of the raison d'être which justified its being established in the first place.

- Insufficient credibility of sub-regional capital backing for the African SRDBs was a problem in undermining the SRDBs. Credibility was eroded further when member governments failed to make capital commitments and/or honour guarantees on time, leading to these institutions unravelling financially. The problem worsened when almost all sub-Saharan African governments saw their creditworthiness diminish between 1985-94 to the point where callable capital guarantees lost all credibility for resource mobilisation purposes.

- The relentless deterioration of the macroeconomic and policy environments in which the African SRDBs had to operate; especially in between 1985-94, leading to severe portfolio, provisioning and financial performance problems.

- A very high exposure to adverse project selection risk that materialised during the life cycle of projects being financed. Most projects and enterprises supported by African SRDBs were designed and implemented in environments vulnerable to policy distortions and corrective policy changes. The financial viability of too many projects depended on high rates of effective protection, over-valued exchange rates, misaligned relative to their real equilibrium levels, and administratively controlled interest rates, which reflected negative real costs of capital.

- Most such projects were undertaken by parastatals, which operated on political rather than commercial lines within protected monopoly structures, with no competition either from imports or from domestic private producers. When the environments for such projects were radically altered under structural adjustment programmes, it was not surprising that most of them failed, resulting in massive aggregated portfolio failures and losses for African SRDBs.

- Thus, SRDBs in Africa were unable to withstand the successive stabilisation and adjustment shocks (accompanied by spiral devaluations, escalating inflation and effective de-industrialisation) inflicted on member countries between 1985-94. SRDBs were particularly vulnerable to the effects of such shocks on the financial viability of their clients, and therefore, of their loan and investment portfolios. Whereas national DFIs were exposed to the risks of economic deterioration and adjustment in one economy, SRDBs were exposed to the compounded effects of such risks in several countries.

- African SRDBs proved fatally vulnerable to exchange risks, country risks and interest-rate risks which they had no means of managing or covering. Passing on exchange and interest rate risks to their borrowers proved impractical when their borrowers went into arrears and default, leaving the SRDBs concerned on their own when it came to meeting their own debt service obligations to external creditors.

- The unravelling (EAC) or progressive weakening (PTA/COMESA) of some of the regional integration arrangements, which the SRDBs were created to support, resulted in weakening the SRDBs themselves.

- SRDBs suffered from the difficulty of establishing clear leadership and direction in institutions owned by several governments, each with different objectives, views and interests. The management of most SRDBs was insufficiently equipped to reconcile and deal with the political repercussions of such differences although some (EADB, BOAD) were more able to cope than others (CTDB, BDEAC)

- The relatively high costs of institution-building and capacity development in African SRDBs proved to be debilitating for SRDBs. These overheads could not be spread over a sufficiently large business volume and contained within administrative cost coverage spreads of 50 basis points or less. Often, in African SRDBs such overhead costs were high enough to require administrative cost coverage spreads of 250-400 basis points, suggesting that the financial intermediation services provided by SRDBs were both uneconomic and inefficient.

- One clear lesson that emerges concerns the importance of involving *non-regional* shareholders constructively in African SRDBs, especially from the resource mobilisation viewpoint in pressured situations. Unfortunately, non-regional shareholders are now reluctant to participate in new SRDBs in Africa given the experience of those that they have supported over the last three decades.

- Development finance is not simply a matter of mobilising resources from foreign donors and MDBs. It requires mobilising domestic savings and devising financial securities that offer sufficiently attractive inflation-protected returns to local investors, institutional as well as individual.

- Even well-managed SRDBs are not good vehicles for implementing industrial location policies, which are inconsonant with underlying economic fundamentals, location comparative advantages and infrastructure imperatives. Thus the objectives of dispersing industrial investment across poorer parts of African sub-regions is a task which even the more capable SRDB's have failed at.

- Assets and liabilities need to be carefully matched with SRDBs undertaking pro-active risk management activities to ensure that their exposure to currency risk, term transformation risk, interest-rate risk and volatility risk is contained within manageable bounds.

- In current circumstances, where SRDBs exist they should focus on helping member governments to privatise rapidly and to encourage the development of sub-regional cross-holdings in privatised enterprises rather than expanding their development financing roles.

- To be successful in the long-run African SRDBs need to be involved in wider efforts aimed at financial system development and in regional co-ordination of banking and financial markets. Eventually they must be privatised and become investment or universal banks operating on a sub-regional or pan-African scale.

4.83 With these broad lessons learnt from the African SRDBs, this chapter turns (in the next section) to examining the case of the Caribbean Development Bank and the succeeding section focuses on the European Investment Bank.

The Caribbean Development Bank (CDB)[4]

4.84 The CDB is a sub-regional development bank, which its members believe has played a useful, durable development-financing role in the Commonwealth countries of the Caribbean. It has played a particularly useful regional role among members of the Caribbean Community and Common Market (CARICOM). CDB has focused most of its attention on seven small island economies (shown in italics below) that are members of the Organisation of the Eastern Caribbean States (OECS) and are the least developed of the Caribbean countries. The

[4] In analysing the CDB the authors have relied heavily on the CDB's Annual Reports as well as on a recent book *The Caribbean Development Bank* authored by Chandra Hardy for the North-South Institute in Ottawa, Canada (1995, publishers Lynne Rienner, Boulder, Colorado, USA).

members of CARICOM include: *Anguilla*, *Antigua & Barbuda*, the Bahamas, Barbados, Belize, the British Virgin Islands (BVI), the Cayman Islands, *Dominica*, *Grenada*, Guyana, Jamaica, *Montserrat*, *St. Kitts-Nevis*, St. Lucia, *St. Vincent & the Grenadines*, Trinidad & Tobago and the Turks & Caicos Islands. The total population of its borrowing member countries was under 6 million in 1996 with an average per capita income of about US$ 3,000, and that of the OECS countries being just over US$ 1,000. Like sub-Saharan Africa, the Caribbean sub-region has grown at an average rate of less than 1.5% per annum between 1970-96. In 1996 it had a sub-regional GDP of about US$ 12 billion.

4.85 Annually and cumulatively, the CDB's financing operations accounted for 7% of total investment in the Caribbean between 1970-95 and 11% of total *public* investment. The multiplier effects of its operations have probably been greater than these numbers imply. In the OECS countries the CDB financed nearly 40% of public investment and over 30% of total investment, thus, playing a crucial role in their development. The Prime Minister of Guyana observed that the CDB was 'an important piece of the machinery in the pursuit of integration in the Caribbean'. That view has been borne out in practice.

4.86 CDB was established in 1970, with its headquarters in Barbados. Originally it had 18 members, two of which - Britain and Canada - were non-regional. Its initial capital subscriptions amounted to US$ 50 million. Half of this amount was paid-in and the other half was callable. By 1995 CDB's membership had expanded to 25 countries with Germany, France and Italy joining as non-regional members and Venezuela, Colombia and Mexico as regional members.

4.87 In 1995, paid-in capital exceeded US$ 150 million. With a progressive reduction in the paid-in proportion through successive capital increases, its callable capital amounted to over US$525 million giving it a total subscribed capital base of US$675 million. The CDB has received strong support from all its members in meeting their capital subscriptions on time. All its capital increases have been fully subscribed and no capital subscriptions were in arrears. In fact, many members paid their capital subscriptions in advance of their being called! Though diminishing over time CDB's present paid-in to total capital ratio is in excess of 20%, nearly thrice the level of the World Bank and EIB. With accumulated reserves exceeding US$105 million, CDB's ordinary usable capital resources were in excess of US$780 million at the end of 1995. Concessional Special Fund resources, financed mainly by non-regional members as well as non-member OECD and Latin American countries, aggregated more than another US$720 million.

4.88 Thus within 25 years the CDB had mobilised total usable resources of nearly US$1.5 billion (30 times what it started out with) to assist its member countries with. The African SRDBs were created at the same time in a similar or even better position. Yet the CDB has outperformed them all in fulfilling its mandate and mobilising a greater volume of resources than any African SRDB, even though it had a much smaller population (but a larger number of smaller borrowers) to serve. The wisdom of its founders in engaging non-regional members (and non-members) constructively to secure sustained financial support for the CDB was demonstrated in practice without sub-regional shareholders ever risking loss of control over policy and decision-making. By the end of 1995, non-regional members had provided about 35% of CDB's total usable resources while *non-member* countries (the US, Netherlands, Nigeria and Sweden) had provided a further 15%. Of the remaining 50%, the regional members provided 12%, other sub-regional members 10%, while 15% came from MDBs (World Bank and IADB) and international capital markets, with the balance of 13% being derived from the CDB's accumulated net income.

4.89 Britain and Canada provided 40% of CDB's initial capital, i.e. each provided US$10 million with US$ 5 million paid-in. They absorbed the full initial allocation for non-regional members that was permitted in the capital structure. In the early 1980s, Britain and Canada reduced their shareholdings from 20% to 10.44% each when France, Germany and Italy joined as non-regional members with shares of 6.26% each. The U.S., whose coastline borders the Caribbean, was constrained from joining the CDB because of a long-standing policy of not joining *sub*-regional development banks. But it adopted a stance of constructive engagement with the CDB throughout the 1970-95 period and made substantial contributions to the CDB's Special Fund resources. Altogether the US has provided almost 12% of its cumulative resources between 1970-95.

4.90 Adjustments were also made in the regional membership when new members joined with the aggregate sub-regional share remaining at about 60.4% of the total. Jamaica and Trinidad & Tobago are the largest sub-regional shareholders, each with a 16.63% share. The Bahamas, Guyana and Barbados are the next largest sub-regional shareholders with shares of 4.91%, 3.58% and 3.12%, respectively, while Colombia, Mexico and Venezuela each have a 3.13% share. Sub-regional members enjoy the benefits of weighted voting rights in their favour with each sub-regional member having 150 votes in addition to one vote for each share (value US$ 5,000) held.

4.91 Majority ownership and control of the CDB clearly rests in the hands of its sub-regional borrowing members. But all policy and project loan approval decisions are arrived at by consensus in the Board. The CDB has been fortunate in ensuring that interaction between sub-regional and non-regional members has remained harmonious. The connection is of a quality that has encouraged non-regional members (and even non-members like the US) to support the CDB with hard and soft financial resources to levels well beyond those enjoyed by any similar African institution in a proportionate sense (see above). That outcome has been largely due to the quality and adroitness of its management in dealing with non-regional members and in ensuring amity and community of purpose between regional and non-regional members.

4.92 Of the SRDBs established at the time, the CDB's mandate was similar to that of BOAD. Its charter required CDB to:

- assist regional members with co-ordinating their development programmes;
- help make their economies complementary;
- promote the orderly expansion of intra-regional trade;
- mobilise development resources within and outside the Caribbean;
- finance projects/programmes that contributed to regional economic development and to the national development of its members;
- provide technical assistance for feasibility studies and project preparation;
- promote public and private investment;
- promote regional and local financial institutions;
- create a regional market for credit and savings; and
- encourage the development of a regional capital market.

4.93 Starting out with a staff complement of fewer than 20 in 1970, the CDB had 190 staff in 1995 of which 90 were professionals. It has had three highly capable Presidents in its 25-year history. All were technocrats and statesmen of international calibre and repute. They endowed CDB with their personal integrity and with continuity of leadership; exercising enormous personal influence with political leaderships and governments in the sub-region and beyond. Those relationships enabled them to muster constructive political support whenever necessary but, at the same time, to withstand and insulate the CDB from counterproductive political intrusion on the rare occasions when that was attempted. In turn, leaders of this calibre ensured that competence and capability were the key priorities in hiring the CDB's top management teams and its professional staff. These attributes were rarely, if ever, subordinated to the imperatives of equitable regional representation, which the CDB nevertheless managed to achieve; mainly because its staff were appointed through its own independent and rigorous staff selection processes rather than at the instance of member governments or politically well-connected individuals.

4.94 Staff development, career mobility and continual training to update skills at all levels have been accorded high priority in the CDB. The Bank recognised that small DFIs have the advantage of cohesiveness and 'togetherness' but the disadvantage of limiting the scope for professional specialisation and upward mobility. Small institutions must necessarily have flat organisational structures with few layers of management. To ensure that its staff remained skilled but flexible the CDB encouraged internal rotation across departments. It also arranged medium-term assignments for staff at the IADB, World Bank and in borrowing countries. Such assignments strengthened the knowledge base of staff, enhanced their technical skills, and added maturity and breadth to their judgement. CDB's staff development efforts have resulted in a remarkably high retention rate of competent staff. That, in turn, has enhanced continuity in relationships with clients and enhanced the credibility of the CDB with borrowing members and shareholders.

4.95 Starting with loan approvals of less than US$ 15 million in 1970, CDB's cumulative financing amounted to over US$390 million by 1982 and US$1.2 billion by 1995. Annual lending tripled between those two periods: i.e. from US$30 million between 1970-82 to US$90 million between 1983-95. Of total approvals, 90% were for direct concessional and non-concessional loans. The remaining 10% represented technical assistance grants financed from special funds. By 1995 cumulative disbursements exceeded US$950 million. Virtually all lending has been for project financing. The total cost of the projects it financed up to 1995 exceeded US$2.5 billion with the CDB accounting for nearly 50%. More than 52% of CDB's total lending, 75% of its concessional lending, and over 80% of its grant financing was directed to the least developed members of CARICOM.

4.96 About 45% of CDB's lending has gone into infrastructure, mainly transport. Projects to build feeder roads, and extend and rehabilitate main roads, ports and airports have shown good rates of return particularly with the dependence of the Caribbean on tourism. Similar success has been achieved with the financing of electric power and water supply projects. Most importantly, the CDB made a vital contribution to ensuring that public utilities in the Caribbean operated on commercial principles from the outset; insisting as a condition of its loans that they realise annual operating surpluses. Agriculture absorbed a further 13% of CDB's lending and focused on providing credit for small farm improvements and for agricultural production. About 15% of CDB's lending has been dispersed over a range of miscellaneous purposes. The balance (27%) of CDB's lending has gone into providing lines of credit to smaller national DFIs for on-lending to SMEs. In the Caribbean these have been mainly service enterprises connected to the tourism industry, and rural agro-industrial enterprises. Such enterprises were supported both by way of credit programmes as well as by financing industrial estates that provided SMEs with finished factory units.

4.97 In developing a wholesale funding relationship with its network of smaller national DFIs, the CDB has operated in the same way as BOAD with much the same success. CDB has also provided financing, through national DFIs for low-cost housing and student loans, thus, gaining considerable credibility and popularity within the region and becoming a household name. By 1992 there were 27 national DFIs being supervised by the CDB with 14 of them still actively drawing down CDB lines of credit. More recently, CDB has also started channelling credit to SMEs through local commercial banks throughout its region.

4.98 CDB exerted considerable effort to be pro-active in lending to the Caribbean's weakest economies. Overcoming the constraints imposed by too few and inadequately trained government staff in these countries, the CDB did its own work to identify and prepare suitable projects for financing. It acquainted borrowers with procedural requirements for effectuating loan disbursements and meeting loan effectiveness conditions. CDB financed mainly *national* projects, which were too large for local DFIs to finance.

4.99 CDB had less success with financing *sub-regional* projects. In the 1970s it made loans to a sub-regional shipping line and a sub-regional airline. Both proved unsuccessful because of poor management, low traffic and the under-capitalisation of both companies. It also made loans for two sub-regional projects for the production and processing of soybeans, corn and black-eyed peas. Again, both failed due to insufficient economies of scale, inadequate guarantees from governments, poorly trained staff and under-capitalisation of the enterprises involved. Studies were also carried out for regional fisheries and livestock projects and CDB lent to national projects for expansion to meet regional market needs. Again these projects proved unviable, suffering from poor management, poor project design, rapid cost escalation problems, low productivity, inadequate marketing arrangements and the lack of indigenous local technical expertise.

4.100 Based on this experience, no sub-regional projects have been approved since 1980. Instead, CDB has focused its attention on 'soft' regional activities and programmes that have had more success. It has financed a number of studies for agricultural diversification and input supply in the OECS. It has also financed studies to achieve reductions in power transmission losses across the sub-region; regional water management and training programmes. Working with the IADB, the CDB has co-financed a project to strengthen the University of the West Indies (which serves the entire sub-region) and support adult distance learning programmes.

4.101 The scope for policy-based lending by the CDB has been limited. The IADB and the World Bank have undertaken such lending more. But CDB has participated in channelling fast-disbursing structural adjustment funds from these institutions to smaller Caribbean economies. In 1976, CDB helped to establish the Fund for Emergency Programmes and Common Services in response to the widespread balance-of-payments problems of its borrowers. In 1978 it proposed the creation of the Caribbean Development Facility and the Basic Human Needs Fund to mitigate the social effects of SAPs. In 1991 it co-financed with the World Bank the economic recovery package for Guyana aimed at clearing its multilateral arrears and restructuring its economy.

4.102 CDB's main strength, and the basis for its durability and credibility, has been the success of its financial management when member economies experienced economic turbulence. Their adjustment problems were just as traumatic as those faced by African economies between 1978-94. During this difficult period the CDB, with the support of its members, managed prolonged arrears and defaults more adroitly and with greater resolve than its African counterparts. It cancelled loans when projects were delayed because borrowing countries were unable to meet their share of project costs. CDB avoided a build-up of protracted arrears by not making new loans, or disbursing to members in arrears. It applied rigorously and quickly its non-accrual and provisioning policies on loans on which debt servicing was delayed. At the peak of its portfolio problems in 1988, non-performing loans represented 15% of the total loan portfolio. This was reduced to less than 3% by 1992 and even lower by 1995.

4.103 Deterioration in portfolio quality affected CDB's lending and financial performance adversely although it still managed to avoid making a loss. Lending (and consequently disbursements) dropped to less than 25% of earlier annual levels in 1987 and 1988. Non-accrual policies and the need to make provisions on an unprecedented scale, resulted in net income falling from an annual average of US$3.5 million between 1981-83 to under US$1 million in 1986. But the timeliness of measures taken by management, in the face of resistance from borrowing members in difficulty, resulted in profitability reviving to about US$6 million annually for 1987-89 and US$18 million between 1990-92 when Guyana's arrears were cleared, non-accrued income was collected, and provisions were written back. In 1992 the CDB did its first borrowing (US$ 30 million) in international capital markets and was rated as a triple-A borrower by Moody's.

4.104 A number of country and project evaluation studies make a compelling case that the CDB had a positive impact on the OECS economies in particular and the Caribbean in general. Its role in the larger, middle-income economies of the sub-region was subordinate to that of the IADB and World Bank. The OECS countries see the CDB as the main, and most supportive, partner in their quest for economic development. Because of its close ties to, and its influence with member governments, CDB has had a qualitative impact on their economic policies, and particularly on the management of public finances, which has perhaps exceeded the impact of its financial transfers. Most OECS economies in the 1990s have been generating budget surpluses rather than deficits largely as a result of the discipline and influence exercised by the CDB. The CDB's role in human resource development and institution building in its sub-region has also been impressive.

4.105 The CDB, like BOAD, clearly defined and delineated its role vis-à-vis national DFIs, the regional MDB, operating in its broader region (i.e. IADB), and the World Bank. The quality of its relationships with these DFIs at different tiers contributed to enhancing its own resource mobilisation role and to regional development. It embedded CDB's unique role within the DFI framework by ensuring that instead of competing with them, it provided value-added services to national and supra-national DFIs which they found indispensable.

4.106 CDB's experience suggests that, in the right set of circumstances, there can be advantages to pluralising development finance flows to developing countries. It has demonstrated the advantage that an efficient SRDB can have over larger MDBs with lower costs of project identification, preparation, appraisal and supervision. CDB is closer to the operating ground level in the Caribbean and knows its borrowers better. Vis-à-vis the national DFIs (especially in the smaller OECS economies) it is a more efficient vehicle for pooling and wholesaling resources as well as pooling bilateral grant aid into efficiently sized packages for regional training and environmental programmes.

4.107 ***Lessons for SADC from CDB's experience:*** Like BOAD, the CDB has been a successful SRDB. All its members feel that CDB has played a useful and supportive development role. Its least-developed members feel that they could not have done without the CDB. The CDB succeeded not simply because it was a well-managed, capable and responsive institution. It was helped by: (i) the unique circumstances defining the make-up of the Caribbean sub-region; (ii) entry into the institutional DFI structure of the sub-region at precisely the right time when development finance represented the only source of funds for the region; (iii) the backing given to it by Britain and Canada and later by other non-regional members and non-members, in particular the other large EU states and the US; and (iv) foresight on the part of its management of the kind of role it should play vis-à-vis national DFIs, bilateral aid agencies and the MDBs so that it added value in complementing the work of all of them. CDB also succeeded in creating a large network of national DFIs, which depended on it for funds, and for their own institutional development. *Indeed both BOAD and CDB established themselves at the hub of a network of national DFIs, a major role that contributed to their success*. Most of all, the CDB's success was based on its political influence and technocratic credibility with its member governments and with its principal providers of funds.

4.108 In considering CDB's experience, it should be borne in mind that the Caribbean economies were just as badly affected as Africa by the twin effects of: (i) the debt crisis and (ii) excessive vulnerability to externally induced terms-of-trade shocks because of their dependence on primary commodity exports. They suffered many of the same problems as African countries in having small domestic markets, no industrial or manufactured exporting base, and weak human resource and indigenous entrepreneurial endowments. Yet they were able to deal with these problems better because of the higher quality of overall economic management and the ability to represent their case jointly and more powerfully to their external interlocutors. Unlike the African SRDBs, the CDB was not brought to the brink of bankruptcy by the defaults of borrowing members. Its sub-regional members were more supportive and protective of the financial credibility of their institution than African governments were in their respective sub-regions. They were also more adroit and able in their handling of relationships with non-regional members than African governments have been in handling similar relationships in African SRDBs.

4.109 Many of the other lessons that can be learned from the CDB's experience have already been outlined above. They are much the same as those to be learned from BOAD. They do not need to be repeated again. What both experiences show is that SRDBs are rarely needed for financing *sub-regional* projects as such. In fact such projects have usually proven to be failures. SRDBs usually succeed because they capture economies of scale and operating efficiencies in financing *national* projects in their member countries more effectively than very small and limited national DFIs are able to do.

4.110 The question that the CDB experience raises, at least hypothetically, is whether a single sub-regional SRDB - established at a time when donors were willing to support such DFIs and capital market alternatives did not exist - to meet the development finance needs of *smaller* SADC countries, such as BLNS and Malawi, might have worked. Had it been able to replicate the experience of BOAD and CDB, such an SRDB might have been a lower cost, more efficient (from the resource mobilisation, management and operating points of view) alternative to these countries establishing several national DFIs. Such DFIs in these economies could have been smaller, lower-cost institutions focusing only on SME and rural enterprise lending, and operating as a network of linked institutions, with an SRDB at their hub, in much the same way as the CDB and BOAD created their own linked networks.

4.111 The larger SADC economies (Zimbabwe, Zambia and Tanzania) would probably have needed their own national DFIs. In Angola and Mozambique it is unlikely that any DFI would have survived the ravages of conflict and war. But such speculation serves no practical purpose. Circumstances in the mid-1990s have changed dramatically. The proclivities of donors to support SRDBs have diminished to the point where the question of establishing a SRDB for SADC at this point in time raises entirely different issues. At the same time, SADC countries have a large number of different national DFIs with different institutional and financial capabilities and with large non-performing portfolios that need cleaning up. Moreover, the structure of SADC is different (with one dominant hegemonic economy at its centre) to either the Caribbean or UMOA. That feature raises doubts about whether a single SRDB would be able to meet the needs of such heterogeneous members in terms of their size, as well as their levels of industrialisation and development. The experience of CTDB suggests otherwise. In such circumstances yet another DFI at the sub-regional level would probably create more problems than it might solve. But the concept of forming a *network* of DFIs within the sub-region, with some sort of supportive hub (even if not a financial one) to help solve common-problems and knit the DFIs of the region together, is one which suggests itself as worthy of pursuit.

The European Investment Bank (EIB)

4.112 Strictly speaking, the EIB is not an appropriate comparator for SADC in considering the possibility of establishing a SRDB for a number of reasons. To begin with, although originally established as a SRDB, the EIB is actually a very large MDB with a continually expanding regional (as the EU itself expands) and global remit. Although principally a SRDB for Western Europe, the EIB can now lend to about 130 countries around the world. Its assets in 1998 were twelve times the size of AfDB's and about the same as those of the World Bank; which is really the EIB's only relevant comparator in terms of size although not in terms of clientele, mandate or functions. In about five years the assets of the EIB will probably exceed those of the World Bank and the EIB will shift even more towards becoming a global MDB rather than remaining a SRDB.

4.113 The EIB therefore operates in a very different environment and milieu from SADC, comprising mainly *developed* country members and borrowers. At present its lending to developing country borrowers is relatively insignificant though quite large in absolute dollar terms. That might change in the future as more economies from Central and Eastern Europe become members of the EU. Over the years, the EIB has become an important instrument for implementing financial relationships between the EU and sub-regions in other parts of the world. It has access to a volume of public and market resources on terms very different from any that are likely to apply to SADC for the foreseeable future. And it raises almost all of its resources within its own sub-region.

4.114 EIB's main business is intermediating financial flows alongside structural (development) funds from the richer to the poorest parts of the EU. The richest EU country has a per capita income nine times higher than the richest SADC country. The poorest EU country has an income three times higher than the richest SADC country and 100 times higher than the poorest. The EIB also provides service agency functions for the EU in disbursing funds under successive Lomè agreements to the Africa, Caribbean and Pacific (ACP) countries and also lends to non-ACP countries under special bilateral programmes between the EU and other developing countries in e.g. Eastern Europe, Asia and Latin America. For all these reasons, comparisons or lessons from the EIB's experience run the risk of being misleading rather than instructive. Nevertheless, it has been included in this analysis since the ToR specifically asked for that to be done.

4.115 Created in 1958 under a special statute (in the Treaty of Rome and confirmed in the 1993 Maastricht Treaty on European Union), the EIB is a financially independent organisation with policy and decision-making structures independent of the European Commission and Parliament. Between 1958-72, EIB had provided cumulative financing of only €2.83 billion (US$ 3 billion) to its member states i.e. averaging less than US$250 million per year. Its financing role expanded rapidly after the EEC's enlargement in 1973 and again in 1993. Annual lending rose from €1.5 billion in 1973 to €23.2 billion in 1996.

4.116 By the end of 1996, the EIB had extended cumulative financing of €214 billion to EU and non-EU countries. Its capital has been enlarged six times and is now €57.6 billion (US$ 65 billion). Of this amount only € 4.32 billion (or 7.5%) has been paid-in. Permitted to incur outstanding liabilities of up to 2.5 times its subscribed capital base, the EIB can expand its outstanding loans and guarantees to €144 billion without the need for a further capital increase. Its asset base at the end of 1996 was about €120 billion.

4.117 EIB's support of intra-regional development through its loans, is dovetailed with grant aid channelled through the European Commission's various Regional Development, Structural and Cohesion Funds. These were set up to support the redevelopment and adjustment of those parts of the EU that are: (i) affected by industrial decline; (ii) rural areas in need of development; and (iii) located in the Arctic region. These funds are also aimed at combating the problem of long-term unemployment that Europe faces, encouraging the occupational integration of young people into the permanent labour force, and adapting productive structures in Europe's agriculture and forestry sectors.

4.118 EIB lending, alongside the EU's structural funds (ESFs), have financed public and private investments totalling over €200 billion between 1989-96. About 75% of the EIB's financing (of about € 100 billion) over this period has been concentrated in the less developed parts of the EU. These are not necessarily the same as the less developed European countries; even rich European countries have poor areas within them. Even so, whereas EIB lending corresponded to over 5% of GFCF in the EU, it represented over 22% of GFCF in Portugal, 15% in Greece, 14% in Spain and Ireland and 12% in Italy's Mezzogiorno. The rapid economic development of Spain, Portugal and Ireland, with corresponding increases in their incomes and social indicators between 1980-95, are examples of the EIB-ESF's success. The Mezzogiorno (into which the EIB-EU have been pouring funds since 1970) represents its major failure. Greece has proven a more difficult country in which to achieve rapid development than earlier anticipated although considerable progress has been made. In performing the key function of intra-regional financing, the EIB is involved at every stage of preparing the programming of EU structural support in order to achieve an optimum loan/grant mix. This is to ensure that borrowing projects and countries can sustain debt service obligations and make the most efficient use of loan and grant funding.

4.119 The EIB also administers a €1 billion EU Facility with a 2% interest rate subsidy. That Facility is aimed at encouraging investment by job-creating SMEs as part of a drive to stimulate growth, employment and competitiveness. It is being implemented under the EIB's *global loan scheme* in co-operation with participating agent banks and financial institutions in EU member states. Subsidised loans may be for up to €30,000 per job created for 5 years with the interest subsidy being up to € 3,000 per job or 10% of the loan amount; equivalent to a 2% annual subsidy spread over five years.

4.120 The EIB's global loan scheme was launched in the late 1960s under which EIB provided wholesale financing to support SMEs through loans which are retailed by eligible banks and financial intermediaries (FIs). These wholesale 'global loans' are in the form of 5-12 year lines of credit which about 140 participating banks and FIs can draw down to fund SME projects which meet criteria laid down by the EU. Before the EIB makes such funds available it ensures that each eligible intermediary meets geographical, sectoral, financial and business size criteria specified in its contract with the EIB. Between 1989-96 over 40,000 SMEs drew down € 12 billion from EIB global loans - 65% of these SMEs were located in less developed areas and employed fewer than 50 people. About 55% of the SMEs assisted were manufacturing units while the remainder was engaged in business support services, energy conservation and environmental protection activities.

4.121 Financing the development of Europe's poorer regions remains EIB's basic function. But its operational priorities have evolved as the EU has evolved and as new areas of focus have emerged. At present the EIB's key priorities are to: finance trans-European transport and telecommunications networks; increase the reliability and stability of internal energy supply; promote greater energy efficiency and conservation; maximise environmental protection; generate productive employment; and improve the competitiveness of European industry. In that context, about 66% of EIB's lending operations in 1996 were for regional development in conjunction with the EU's structural funds. Of this proportion, 31% was spent on improving/completing transport and communications networks, 19% for energy, and the remaining 16% for industry, services, urban development and agriculture. Of the remainder, 28% was focused on lending for environmental protection while 6% was lent to improve industrial competitiveness.

4.122 The EIB also administers the European Investment Fund (EIF) which was set up in 1994 to provide guarantees for major infrastructure projects and underwrite capital investment undertaken by SMEs. The EIF operates on a self-sustaining basis as a separate legal entity with accounts distinct from those of the EIB. EIF's initial capital was €2 billion; funded by EIB from its annual surpluses and by the European Commission and private financial institutions.

4.123 In the 1990s, EIB operations *outside* the EU have assumed a more prominent profile. Since 1990, the EU has formalised various agreements with a number of regions and countries around the world involving flows of capital, trade and aid. In 1990, more than 97% of the EIB's lending was inside the EU. By 1996 that proportion had dropped to 90%. Of the remaining 10% about 2% went to the ACP countries and South Africa. Just over 3% went to Mediterranean Rim countries outside the EU, 4% to Central and Eastern European countries, and under 1% to countries in Asia and Latin America. EIB lending outside the EU could grow from 10% to 15% or even 20% within the next decade or two. During that time it is likely that the EU will be enlarged to include members from Central and Eastern Europe. That would of course result in those 'external financing' proportions being effectively 'internalised' through the EU's continual expansion.

4.124 The longest standing involvement of the EIB outside the EU has been with the ACP countries that were former colonies of European countries. Such involvement has been codified under successive Lomè agreements governing aid flows and preferential trade arrangements between the EU and ACP. From the first Yaounde Convention, ACP countries have received concessional loans and grants from the European Development Fund (EDF), which is administered by the European Commission. They have also obtained loans from EIB's 'own resources' which attract an interest subsidy from the EDF in order to maintain the cost of such loans at between 3-6%. Concessional loans to ACP countries between 1986-95 amounted to €3 billion of which €1.6 billion was from the EIB and €1.4 billion from the EDF. In addition, ACP countries received about € 12 billion in EDF grants during the same period.

4.125 Over 80% of the loans to ACP went to sub-Saharan Africa, 11% to the Caribbean and 6% to the Pacific islands. The main beneficiaries of such loans were the more advanced countries in each of the three ACP regions. In these countries the EIB has lent for industry, mining and construction (26%); energy (23%), transport and communications (11%); agriculture and fisheries (11%); water supply (7%); tourism development (1%) and to financial intermediaries for lending to SMEs (21%). EIB's Board authorised it to commence operations in South Africa in June 1995, allocating €300 million for lending to industry, SMEs, energy, telecommunications, small public infrastructure schemes (mainly for water supply in rural areas) and environmental protection between 1995-97. Of this, € 45 million has been allocated for SMEs in productive sectors using the global loans approach.

4.126 The Mediterranean Rim countries of North Africa and the Middle East (including Mahgreb and Mashraq countries) have benefited from EIB lending of over € 3.5 billion between 1989-96. Egypt, Algeria, Morocco, Turkey and Tunisia were the major recipients of such loans. Recently, EIB increased its lending to the Lebanon. More than a third (37%) of its loans to the Mediterranean Rim countries were for infrastructure. In particular, water supply and sanitation in urban coastal areas featured heavily (16%); along with energy (11%), transport and communications (10%). A further 22% of the EIB's loans to this sub-region were for industry, mining, construction, 9% for agriculture while 32% of total loans were provided to banks and financial intermediaries for on-lending to SMEs and for environmental loans. The two main priorities under the EU's Redirected Mediterranean Policy are to protect the Mediterranean's delicate ecological and environmental balance and to promote growth of the private sector, in particular to promote joint ventures between local and European firms. EIB estimates that 175 joint ventures have been financed in seven countries over the last five years giving rise to the creation of over 11,000 new jobs. As its contribution to the Middle East peace process, the EIB began lending for projects in the West Bank and Gaza strip in 1995.

4.127 Between 1994-96, the EIB lent over €3.1 billion to eleven Central and Eastern European countries (CEECs) in line with priorities established under the EU's PHARE and TACIS programmes. These represented, respectively, the EU's separate initiatives for the CEECs (PHARE) and for the Newly Independent States (NIS) which were part of the former USSR and Mongolia (TACIS). Both programmes were created to achieve two key objectives: (i) consolidate the reform process in the economies in transition; and (ii) promote closer integration of the CEECs and NIS with the EU - and perhaps even embrace them under the folds of the EU - over time. PHARE's cross-border programme seeks to promote regional integration (within CEE) and safeguard democratic reform through co-financing investment in infrastructure (principally transport, communications and energy) and the reversal of environmental degradation. Over 50% of the EIB's and EU's commitments to the CEECs are concentrated in restructuring their banking and finance sectors. In the NIS nearly 65% has been committed to energy projects, in particular for assuring nuclear safety. Under PHARE, €300 million has been allocated for the development of SMEs in the private sector.

4.128 Finally, the EIB has lent €652 million (from a budget of €750 million) between 1993-96 to eleven non-ACP countries in Asia and Latin America (ALA) that concluded separate co-operation agreements with the EU. The projects financed by the EIB in these countries have an element of 'mutual interest' in which one of the following criteria are met. The projects must: (i) be joint-ventures between ALA and European firms; (ii) have a high content of technology from Europe; (iii) foster closer relationships between ALA and Europe - in practice this means a high import content from Europe particularly for transport (aircraft) or telecommunications equipment; (iv) incorporate significant environmental benefits (e.g. renewable energy); and (v) foster regional integration. EIB loans to ALA are only for project finance purposes (either public or private sector) in infrastructure, industry, agro-industry, mining, energy; and tourism, with special emphasis on projects, which involve significant environmental protection measures.

4.129 The EIB's substantially expanded role within the EU and its growing remit outside of it, has resulted in rapid growth of the institution's staff between 1989-96. It now has a staff complement of over 820. EIB's expanded role has made significant demands on its management, organisation structure and Board. From a staffing point of view the EIB appears to be a surprisingly efficient MDB. Assets per staff member amount to $170,000; about seven times higher than the World Bank. The EIB resorts more to wholesaling (by relying on other financial institutions to retail its funds) than the World Bank; a strategy that has major implications for staffing. The quality of EIB's management and staff is of a reasonably high international calibre. Although not as visible or as controversial as the management of the World Bank, and inclined to operate more quietly, the standing of EIB's management in international financial circles is high.

4.130 Strictly speaking EIB is a 'not-for-profit' entity. But it has a policy of generating sufficient annual 'operating surpluses' to keep accumulated reserves growing in line with balance sheet growth. At the end of 1996, EIB's total assets amounted to €118 billion of which its loans and advances for projects amounted to about €60 billion while its 'global' loans to other financial institutions amounted to a further €40 million. Over 95% of these outstanding loans were owed to the EIB by developed country sovereign European borrowers and private entities with the highest international credit standing. Its own outstanding obligations on bond issues raised in capital markets exceeded €85 billion (backed by the callable capital of fifteen of the most creditworthy countries in the world) while its accumulated reserves exceeded €10 billion against a paid-in capital base of €4.3 billion. The EIB also manages Special Funds of about € 5 billion for a variety of purposes. Its operating profit between 1992-96 averaged about € 1.25 billion annually. The EIB's financial management is conservative, robust and sophisticated with the Bank being almost entirely insulated from the effects of any seriously conceivable financial risks.

4.131 ***Lessons to be learnt by SADC from the EIB:*** From the foregoing description and analysis of the EIB what lessons can SADC learn in considering the possibility of having its own SRDB? Virtually none that are of practical use. The EU and SADC represent very different situations. There is not much that is relevant to the SADC case, which can be usefully transferred from the EIB's or EU's experience. Clearly the following ingredients have been instrumental in assuring EIB's success:

- Strong political and administrative backing from all member countries;
- A powerful *dirigiste* ethos driving the process of progressive integration;
- A high level of institutional competence with world class management and staff;
- Close interaction with a strong resource-rich European Commission;
- A budget based on automacity in receiving members' annual contributions;
- A Commission willing to use the EIB as executing agency for a variety of purposes;
- An unshakeable political resolve in *continental* Europe to achieve progressively greater integration leading eventually to monetary and perhaps even political union, in which process the EIB has been assigned a key role;
- The availability of large amounts of EU structural and regional development funds for the EIB to associate and secure its own independent lending with; and
- The financial credibility imparted by a growing number of highly creditworthy OECD shareholders.

4.132 Few of those ingredients exist in SADC as yet. Nor are the financing challenges likely to be faced by an SRDB in SADC remotely the same as those that EIB must manage. For all these reasons the EU can only be a model which SADC keeps in mind as a distant vision. It is so far from the reality that confronts SADC today, that the EIB does not provide a useful role model to learn much from in establishing a SADC-SRDB; certainly not as much as SADC can learn from the CDB and BOAD.

Conclusions

4.133 This chapter has examined the experiences of six SRDBs in other sub-regions - four in Africa, one in the Caribbean and one in Western Europe. It has done so in an effort to draw lessons that might be useful in considering the possibility of a SRDB in SADC. The specific lessons learnt from each have already been enunciated earlier and pulled together especially in evaluating the experiences of the African SRDB's whose operating history may provide the most valid pointers for SADC. They do not need to be repeated again.

4.134 ***Unimportance of Regional Projects*:** The experiences of the six SRDBs evaluated above have been mixed. Their failures have as much, if not more, to teach SADC's policy-makers than their successes. Perhaps the most valuable lesson is that SRDBs play a useful role *not* when they are financing *regional* projects, but when they are financing *national* projects in countries which are too small to justify having their own full-service DFIs. That lesson derives from the experience of BOAD in West Africa and the CDB in the Caribbean, especially when contrasted against the less salutary experiences of other African SRDBs. In fact financing regional projects has been an insignificant feature in the operations of successful SRDBs. Such projects have rarely succeeded, especially when undertaken by public sector agencies in co-operating countries.

4.135 ***Role Definition vis-à-vis National and Supranational DFIs:*** Successful SRDBs defined their roles clearly vis-à-vis other DFIs operating at higher (regional and global) and lower (national) hierarchical levels. Another ingredient for success lay in building up a network of national DFIs with the SRDB at their hub. Successful SRDBs played a wholesaling role, as well as a role in financing *large* projects (the term being relative rather than absolute), leaving national DFIs in small economies to concentrate on SMEs and rural enterprises. Moreover, successful SRDBs concentrated mainly on financing productive economic infrastructure projects with high rates of return and on supporting the development of financial systems in their sub-regions.

4.136 ***Securing Non-Regional Support:*** The contrasting experiences of the SRDBs operating in *developing* regions highlights the importance of securing the right kind of support from non-regional developed country members. Developing productive relationships between sub-regional and non-regional shareholders in SRDBs has been crucial to success. There is no SRDB in the developing world that has succeeded without the support of committed non-regional shareholders, especially when it comes to establishing the financial sustainability and borrowing credibility of these DFIs.

4.137 ***Timing:*** Yet another lesson to be learnt is that the viable SRDBs owed their success to the timing of their establishment and their subsequent operating and financial performance. SRDBs established in the late 1960s and 1970s were able to develop stronger foundations over a period of time when development finance was the principal, if not the only, source of funding available to developing regions. Those established later in the 1980s have not done as well partly because faith has been lost in the efficacy of development finance *per se*, and new alternatives have emerged for financing projects (especially infrastructure) which simply did not exist before the onset of the 1990s. It is doubtful that any SRDB or RDB created today would be able to attract the support of traditional official financiers in the same way. Those that have been established (EBRD) or are being mooted (MEDB) in the present decade have been set up for political rather than economic reasons and are having a difficult time justifying their existence; as indeed are the traditional MDBs.

4.138 These broad lessons (as well as specific ones elaborated upon earlier in this chapter) notwithstanding, the inescapable conclusion for SADC is that the experience of SRDBs - especially in Africa - should give it pause in considering the wisdom of establishing an SRDB of its own at this point in time. SADC has characteristics that raise serious issues in creating a SRDB or converting an existing institution to become one. The most problematic of these is the overwhelming size and dominance of South Africa in the sub-region. The way in which its weight would need to be accounted for and accommodated in any SRDB has implications for other members that need to be carefully considered. The second problem is the uneven distribution of creditworthiness across SADC. That feature places an excessive burden on a handful of relatively wealthy countries. It would result in using their creditworthiness to backstop the borrowings of a SRDB that would necessarily focus its lending on the uncreditworthy countries. It would need to rely on concessional rather than non-concessional resources for doing so to any useful degree.

4.139 Another feature of SADC is the enormous variation in the size and capacity of its different member economies. South Africa stands on its own in accounting for 75% of the sub-region’s GDP and having the most diversified industrial and services base. It has its own over-elaborate system of several national DFIs covering infrastructure, industry, SMEs, housing, land and agriculture. It does not need to rely on a SRDB that in all likelihood would be smaller and less capable than its own national DFIs.

4.140 The medium-sized economies of SADC, i.e. *Zimbabwe, Zambia, Tanzania, Angola* and *Mozambique,* are large enough to justify having their own national DFIs. The first three countries already do. The latter two have windows in their mono-banks that attempt to provide long-term loans. In all these countries, except Zimbabwe, DFIs face serious operating and financial problems. They face difficulties with project selection, limited portfolio choice, and inadequacy of funding (concessional and non-concessional).

4.141 Botswana and Mauritius both have their own DFIs. In these two small but relatively rich economies there is a diminishing need for development finance as such. There is a greater need for moving toward relying on more capable private financial institutions operating without any hidden subsidies on fully commercial lines. These two successful economies should now consider converting their DFIs into fully-fledged investment banks with private participation in their shareholding. That would be a useful first step to eventual full privatisation. In addition these two countries should consider utilising special refinancing or rediscount windows (similar to the global loans scheme applied by the EIB) to encourage commercial banks and other financial institutions to lend to SMEs/rural enterprises rather than relying on special-purpose public DFIs to do so.

4.142 That leaves the small SADC economies of *Lesotho, Malawi, Namibia*, and *Swaziland.* These countries might well benefit from a larger SRDB supporting their small national DFIs in a wholesale-retail relationship. But these countries could just as easily benefit from relying on existing and capable South African institutions (such as the DBSA or IDC) or even on Zimbabwean (ZIDC) or Botswana's DFIs to play that role. Indeed, where Lesotho and Swaziland are concerned that is precisely what is happening (as is also the case with Mozambique) in practice in projects such as Lesotho Highlands, the Komati River Basin, the Maputo corridor and Mozal.

4.143 Thus the experience of SRDBs in other sub-regions does little to either make, or strengthen, the case for establishing a SRDB in SADC. The weight of available evidence from experience in other sub-regions leans in the other direction when all the relevant considerations are taken into account.