AN UPDATE ON THE ACTIVITIES OF THE ADF POLICY INNOVATION LAB

ADF-14 Second Replenishment Meeting
July 1, 2016

THE ADF POLICY INNOVATION LAB

Aloysius Ordu
Lead Advisor
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THE HIGH LEVEL PANEL ON THE FUTURE OF THE ADF

Nancy Birdsall
President of the Center for Global Development

Ngaire Woods
Dean of the Blavatnik School of Government at Oxford University and Professor of Global Economic Governance and former Advisor to the IMF Board

Luisa Diogo
Former Prime Minister/Finance Minister of Mozambique and current Chair of Barclays Mozambique

Mary Robinson
Former President of Ireland, former UN Secretary-General's Special Envoy for the Great Lakes region of Africa, and currently President and Chair of the Board of Trustees, the Mary Robinson Foundation – Climate Justice (MRFCJ)

Ngozi Okonzo-Iweala
Former Minister of Finance of Nigeria, former Managing Director of the World Bank and currently co-chair of GAVI and senior advisor of Lazards

ADVISORY TEAM

Aloysius Uche Ordu

Former VP, AfDB & former Director, WBG

Lead Advisor

Lauréline Pla

Former Economist in charge of francophone countries for the African Economic Outlook, AfDB

Coordinator

Margaret Ann Dijkerman

Former CEO for Emerging Markets Group & former Director, Deloitte

Gaiv Tata

Director, Growth Solutions for Development LLC & former Director, WBG

Brian Pinto

Former Chief Economist, Emerging Markets, GLG Partners LP & former Senior Adviser, WBG

Concessional and Innovative Development Finance Experts

OBJECTIVES OF THE ADF POLICY INNOVATION LAB

- Examine the future of the ADF & its strategic positioning
- Amplify the African voice in the debate about development finance
- Propose innovations to expand the pool of resources

THE ADF POLICY INNOVATION LAB HIGH-LEVEL PANEL REPORT

- The Report of the High Level Panel will be titled: "*ADF-Transforming Trust to Influence*"
- It will be discussed at the 2017 AfDB Annual Meetings; dissemination thereafter.

PRELIMINARY FINDINGS ON DEBT SUSTAINABILITY IMPLICATIONS OF HARDENED MDB LENDING TERMS TO ADF COUNTRIES

Brian Pinto
Advisor
ADF Policy Innovation Lab

OBJECTIVE OF THE STUDY

To respond to ADF Deputies' concerns about hardened lending terms causing debt sustainability problems for ADF countries

Three realities:

1. African countries are increasingly borrowing from the market (domestic and external) at interest rates higher than charged by non-concessional wings of MDBs
2. Concerns mounting about a possible new debt crisis in Africa
3. Hardened terms likely to become a permanent feature of development finance

MAIN POINTS

1. Hardened terms are not likely to be a tipping factor in debt sustainability problems for ADF countries
2. Essential that hardened terms be accompanied by larger volume of funds to displace expensive market borrowing
3. Should also be accompanied by a hardened policy dialogue with ADF countries

METHODOLOGY [1]

- ADF Policy Innovation Lab 1st working paper examines the implications of hardened terms for *public debt sustainability*
- Based on 8 countries: Benin, Cote d'Ivoire, Ethiopia, Ghana, Kenya, Mali, Rwanda, Zambia
- Addresses two basic questions:
  1. Are public debt dynamics sustainable?
  2. What is the marginal cost of borrowing (local currency and forex)?

METHODOLOGY [2]

- Why public debt? Three reasons:
  1. Better coverage since both public and publicly guaranteed (PPG) external debt, the bulk of external debt, *and* domestic debt are included
  2. Immediate impact of hardened terms will be on public finances and public debt
  3. Addressing unsustainability requires policies to remedy *public* debt dynamics (via fiscal policy, domestic resource mobilization, etc., *and* growth policy)
- And of course current account deficits and foreign exchange reserve adequacy continue to be important.

FINDINGS ON PUBLIC DEBT SUSTAINABILITY

1. Four countries with unsustainable debt dynamics: Benin, Ghana, Mali and Zambia
   - Slight deterioration in Kenya but comfortable debt dynamics in Cote d'Ivoire, Ethiopia and Rwanda

2. Except for Mali, hardened terms:
   - Not likely to be pivotal in causing unsustainable debt burden. **NB:** Hardened terms from donors and MDBs will still be highly concessional relative to commercial terms
   - Could even improve debt sustainability if funding volume rises to displace expensive market borrowings: 40-year MDB loan with 10Y grace charging a hardened interest of 2-3% superior to a 10Y Eurobond costing 10%.

POLICY IMPLICATIONS OF THIS STUDY

1. Hardened terms also a much-needed wake up call for better economic governance.
2. Such hardening could reconcile donor difficulty in supplying pure grants (given their own problems) with ADF countries' demanding increasing amounts of development finance

CHALLENGES FOR AfDB

AfDB must manage transition to hardened terms while:

1. Working with IDA and other partners to ensure adequate development finance, including from nonconcessional sources

2. Hardening policy dialogue to ensure faster growth and sustainable debt dynamics

3. Serving as a "Knowledge Bank", not just a bank of money: it can dispense *hard* advice given its African franchise value and be proactive in the economic policy dialogue on debt and growth.

REMARKS FROM MRS. LUISA DIOGO, MEMBER OF THE HIGH LEVEL PANEL ON THE FUTURE OF THE ADF

Former Prime Minister and Finance Minister of Mozambique and current Chair at Barclays Mozambique

MERCI BEAUCOUP ! THANK YOU !

Thank you for this opportunity to share our findings. We are happy to take questions.