Leveraging ADF Resources for Private Sector Development
1. Context and Objectives
2. The First Loss Portfolio Guarantee
3. Partial Risk Guarantees
An evolving context requires new approaches

- Private investment is necessary to:
  - Boost growth and pull ADF countries out of poverty.
  - Narrow the development financing gap.

- ADF countries are committed to private sector led growth.

- Reduced liquidity and heightened risk aversion inhibit their ability to attract foreign and domestic investment.

- Two instruments to innovate and consolidate:
  - The First Loss Portfolio Guarantee
  - Partial Risk Guarantees
The instruments would leverage AfDB Group capabilities and boost results

- Demonstrated capacity to process and supervise an increasing volume of non-sovereign operations in LICs.
- One-stop-shop for private sector development.
- Growing non-sovereign pipeline across ADF countries.
- Every 1 UA of non-sovereign lending attracts an additional 5 UA from external sources.

Non-sovereign operations, targets, achievements

<table>
<thead>
<tr>
<th>PSO Target</th>
<th>LICs</th>
<th>Regional Operations</th>
<th>MICs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Target</td>
<td>40%</td>
<td>20%</td>
<td>40%</td>
</tr>
<tr>
<td>Average 2007 to 2009</td>
<td>37%</td>
<td>26%</td>
<td>37%</td>
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The FLPG significantly raises the share of PSO in LICs over the ADF 12 cycle

- The GCI provides headroom for non-sovereign portfolio growth in LICs and MICs.
- The FLPG would boost the non-sovereign portfolio risk-bearing capacity for LICs.
- Ring-fenced benefit to eligible transactions to offset high country risk in LICs.
- Overall risk for an entire portfolio is lower than the sum of risks on individual transactions in that portfolio.
The FLPG takes the first 10% of losses on a designated portfolio

- ADB remains risk bearer of residual risk.
- The pilot approach assumes a gradual build up of the portfolio.
- Seeded by a UA 100 million ADF “top-slice” and voluntary bilateral contributions.
- Procedures and modalities would be governed by Framework Agreement to be negotiated between the ADB and ADF Boards.
Eligibility criteria would also need to consider the implications of ...

- Country and sector portfolio diversification.
- Portfolio homogeneity:
  - A few very large operations could deplete the facility rapidly
- Size of the guarantee facility

### Average country risk

<table>
<thead>
<tr>
<th>Country</th>
<th>Rating</th>
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<tbody>
<tr>
<td>Fragile state</td>
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</tr>
<tr>
<td>LIC</td>
<td>4.3</td>
</tr>
<tr>
<td>MIC</td>
<td>2.2</td>
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</table>

### Commercial risk

<table>
<thead>
<tr>
<th>Sector</th>
<th>Rating</th>
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<tbody>
<tr>
<td>MFI and SME</td>
<td>2.8</td>
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<tr>
<td>Agriculture &amp; agribusiness</td>
<td>2.5</td>
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<tr>
<td>Infrastructure</td>
<td>1.9</td>
</tr>
<tr>
<td>Industry &amp; services</td>
<td>1.4</td>
</tr>
<tr>
<td>Financial intermediation</td>
<td>1.3</td>
</tr>
</tbody>
</table>
Content

1. Context and Objectives

2. The First Loss Portfolio Guarantee

3. Partial Risk Guarantees
Partial risk guarantees (PRGs) are an enabling instrument for PPPs

- In LICs, PPPs remain risky business for investors: projects bear higher premiums to pre-empt the risk of government non-performance.

- PRGs are not a substitute for non-sovereign loans but increase the feasibility of PPPs:
  - Cover non-performance of the public sector partner.
  - Encourages Government to undertake enabling reforms.
  - Defaulting on one loan triggers default on other loans.
  - Only uses 25% from the requesting country’s PBA.
  - Guarantees have a 1:4 leverage.
PRG structures are customized to specific project risks, partners and modalities.

- Commercial Bank
- Guarantee
- Counter-guarantee
- Fees
- LoCs
- Government
- GOE / Public Utility / Off-taker
- Concessionaire / Project Company (SPV)
The AfDB will leverage the 20 year-strong experience of sister institutions in PRGs

- During ADF XII, PRG demand is about UA 475 million.
- Financing modalities are built into the PBA and are therefore contingent on government demand:
  - Serving both public and private sector clients enables the AfDB to mobilize demand effectively.
- PRGs require project finance skills and methods:
  - Investment officers, credit risk managers and legal officers have solid experience.
  - Technical assistance and piloting to grow in-house expertise.
In summary...

- Private sector development is essential for sustainable economic growth that leads to meaningful poverty reduction.
- Two new financing instruments have been proposed that will leverage more private sector operations in LICs by significantly amplifying the benefits of the GCI.
- Both instruments would be introduced on a pilot basis before mainstreaming and scaling up.