

# CRS Report for Congress

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## African Development Bank and Fund

Raymond W. Copson  
Specialist in International Relations  
Foreign Affairs, Defense, and Trade Division

### Summary

The African Development Bank Group, including the Bank itself (AfDB) and its “soft-loan” affiliate, the African Development Fund (AfDF), is a development finance institution based in Abidjan, Côte d’Ivoire. The Bank has 53 African members, as well as 24 non-regional members, including the United States. In the mid-1990s, the Bank faced management problems and difficulties arising from non-performing loans, but reforms launched in 1995 by a new Bank president, Omar Kabbaj, brought new pledges of support from the non-regionals. U.S. contributions to the Fund resumed in FY1998 and to the Bank in FY2000. This report will be updated as events warrant.

### Background

The African Development Bank Group, including the Bank itself (AfDB) and its “soft-loan” affiliate, the African Development Fund (AfDF), is a multilateral development finance institution based in Abidjan, Côte d’Ivoire.<sup>1</sup> Both the Bank and the Fund are supported by the United States, and when funds are provided they must be authorized and appropriated by Congress.

The Bank makes “non-concessional” loans — that is, loans on terms that approximate those of commercial lenders — to creditworthy borrowers, including governments, official agencies, and to an increasing degree, the private sector. The Fund makes loans on highly concessional terms to the poorest African countries, which do not have access to commercial credit. These loans, regarded as a form of economic assistance, bear no interest, although there is a .75% annual service charge on outstanding balances. They may be repaid over 50 years, including a 10-year grace period.

The Bank has 53 African members, including both the North African and the sub-Saharan countries, as well as 24 non-regional members, including all of the major donors

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<sup>1</sup> The Development Fund for Africa (DFA) and the African Development Foundation (ADF) are U.S. bilateral assistance programs for Africa. CRS Issue Brief IB95052, *Africa: U.S. Foreign Assistance Issues*.

of development aid to Africa. The Fund has 27 contributing members, including 25 non-regionals and South Africa, in addition to the Bank itself. In 1999, the Bank and Fund approved 93 loans and investments totaling \$1.7 billion in both North Africa and sub-Saharan Africa. The Bank Group lent approximately the same amount in 1998, but the total number of loans in that year was 133. Of total Bank Group lending in 1999, concessional lending by the Fund amounted to \$630 million through 70 loans, down from \$810 million and 115 loans in 1998. The Bank Group had 967 employees at the end of 1999, including 481 professionals.<sup>2</sup>

**Origins.** The African Development Bank was founded as an exclusively African institution in 1964. Most African countries had just become independent amid great optimism about the continent's economic prospects. The Bank's charter reflected the belief that these prospects could best be furthered by self-reliance and cooperation among African states, rather than by reliance on outsiders.<sup>3</sup> Nigeria, the leading contributor to the Bank, and some other members were very concerned to maintain the Bank's "African character," but it soon became clear that the exclusively African membership of the Bank was limiting the amount of capital that could be raised. Consequently, in 1973, the United States and other donor countries from outside Africa were invited to join the African Development Fund, which had been created in 1972.

The sharp oil price rises of the mid 1970's worsened Africa's capital shortage while making it impossible for most African countries to consider increasing their contributions to the Bank. In 1976, oil-rich Nigeria did establish the Nigeria Trust Fund at the Bank to make development loans, particularly to low-income countries, but the Bank sought additional capital to help members cope with mounting economic difficulties. Finally, in 1982, non-regional countries were invited to join the Bank itself, although Bank policy limited them to a one-third share.

**Resources.** The Bank has two types of resources: paid-in capital and callable capital. Paid-in capital consists of funds actually transferred to the Bank by member countries, while callable capital, representing by far the largest part of the Bank's total capitalization, is a promise by member countries to provide funds to the Bank, in the event lenders to the Bank should demand to be repaid. These two resources make the Bank a high-quality borrower, enabling it to borrow money on world capital markets on favorable terms in order to lend to African borrowers.

If the Bank's lenders should lose confidence in it for some reason, the United States, along with other donors pledging callable capital, could conceivably be called upon to assist the Bank from their pledges. Such an event would be unprecedented, however. The United States has never had to expend callable capital despite pledges to a number of international financial institutions.<sup>4</sup> Callable capital pledges are provided only to the Bank

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<sup>2</sup> The information in this paragraph is from African Development Bank Group annual report for 1999, the most recent report available, at [<http://www.afdb.org/home.html>].

<sup>3</sup> E. Philip English and Harris M. Mule, *The African Development Bank* (Boulder, Colorado: Lynne Rienner, 1995), 19-20.

<sup>4</sup> However, the House report (H.Rept. 106-254) on the original FY2000 Foreign Operations bill (continued...)

and not to the Fund. The Fund's resources consist entirely of contributions from the member states, which are normally replenished on a three-year cycle.

**Voting.** At the Bank, every member state is represented on the Board of Governors, the highest decision-making body. Members are shareholders in the Bank, and their voting power is largely determined by the size of their contribution. Hence, the non-regionals have about one-third of the votes, while the regionals have about two-thirds. At the Fund, the non-regional members have contributed nearly all of the lendable resources but control 50% of the voting power, distributed according to the size of their contribution. The remaining 50% is controlled by the Bank.

## Crisis in the Mid-1990s

In the mid-1990s, the African Development Bank faced what has been called a “mid-life crisis,” after non-regional members lost confidence in its lending policies and management practices. Many African countries had been experiencing severe economic and budgetary problems for years, resulting in part from inappropriate economic policies and in part from external factors, including high oil prices and low prices for their commodity exports. They were becoming increasingly uncreditworthy; yet the Bank had continued to extend them non-concessional loans. By 1994, arrears had reached \$700 million, twice their level in 1992.<sup>5</sup> The Fund was also short of resources and made virtually no loans in 1994. Yet the non-regionals were unwilling to replenish the capital of either institution until there were reforms. In April 1995, the U.S. General Accounting Office issued a report that called the Bank “solvent but vulnerable” and criticized a governance system that allowed borrowers to control decision-making.<sup>6</sup> The report noted that the Bank enjoyed a top credit rating in world credit markets because of the paid-in and callable capital provided by the non-regionals, yet the non-regionals were unable to prevent loans they regarded as unsound because they were outvoted.

Standard & Poor's lowered the Bank's credit rating slightly in August 1995, citing concerns over governance and management. The downgrading came after a long struggle at the Bank over the choice of a new president, but on August 26, 1995, after nine rounds of voting, Bank members had finally elected Omar Kabbaj, a Moroccan financial official who advocated management and fiscal reforms at the Bank.

**Kabbaj Reforms.** President Kabbaj has won wide praise from financial analysts and non-regional governments for his success in implementing promised reforms. In its 1999 budget request, the U.S. Treasury, which had led the non-regionals in demanding

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<sup>4</sup> (...continued)

(H.R. 2606) noted “many concerns” about U.S. participation in replenishing the Bank's resources. While expressing support for reforms at the Bank, the Committee on Appropriations did not fund the paid-in capital request because it was accompanied by an \$80 million callable capital request. In final action, Congress partially funded both the FY2000 paid-in and callable capital requests (see below).

<sup>5</sup> English and Mule, p.29.

<sup>6</sup> *Multilateral Development Banks: Financial Condition of the African Development Bank* (GAO/NSIAD-95-143BR).

reforms, lauded the “aggressive new President” for restricting poor country access to non-concessional lending, reducing the Bank staff by 14%, replacing 70% of managers, reducing arrears, reforming the Bank’s procurement system, and other measures. In May 2000, Kabbaj was unanimously re-elected for a second five-year term as Bank Group president.

The Joint Africa Institute (JAI), a training center Kabbaj has set up in Abidjan with the International Monetary Fund (IMF) and the World Bank, has also drawn praise, as has the Bank’s vision statement, drafted under his guidance. The statement commits the Bank to being the leading development finance institution with respect to poverty reduction and sustainable development in Africa through investments in agriculture and rural development, human resource development, private sector development, and governance. Leadership in costly infrastructure areas, such as power, industry, telecommunications, and transportation, is to be left to other lenders, principally the World Bank. In its 1999 annual report, the Bank Group noted that in view of the HIV/AIDS pandemic, its health sector policy guidelines had been revised to allow lending that will strengthen African health care institutions and promote sustainable health care delivery.

**New Replenishments Approved.** The change in attitude toward the Bank Group among the non-regionals first became evident at the annual meeting of the board of governors in May 1996, when the non-regionals pledged \$2.6 billion over three years as the seventh replenishment of the AfDF (AfDF-VII). Several countries, though not including the United States, later made additional pledges to AfDF VII.

Non-regional endorsement of the reforms at the Bank itself came at the May 1998 meeting, when the board agreed to the fifth general capital increase (GCI-V), representing a 35% boost in the Bank’s resources. The last 5-year general capital increase had been approved in 1986, and negotiations in the early 1990s on a new increase had stalled due to the concerns of the non-regionals over the Bank’s problems. The latest increase, which is to be spread over eight years beginning in 1999, would increase the non-regional share in the Bank’s capital from one-third to 40%, thus giving non-regionals 40% of the votes on the governing board. Moreover, at the insistence of the non-regionals, decisions on Bank operations are to be taken by a 66% majority, while “crucial” decisions will require the approval of 70% of shareholders.<sup>7</sup> Thus, there will have to be at least some non-regional support for major Bank actions. These modifications to the Bank’s “African character” were initially opposed by some regional members, but Kabbaj announced in May 1999 that GCI-V and the accompanying rules changes had won the necessary support.

In January 1999, the non-regionals agreed to the eighth replenishment of the African Development Fund (AfDF-VIII), a \$3.4 billion contribution to be made over three years. The Bank has pledged that new loans from the Fund will have a strong poverty focus, targeting income generating activities for the poor as well as primary health and education. The Bank also promises that the Fund will promote good governance in borrowing countries, including anti-corruption efforts, and that there will be a strong linkage between resource allocation and country performance.

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<sup>7</sup> *Africa Research Bulletin, Economic Series*, May-June, 1998, p.13455-13456.

## The United States and the AfDB Group

From 1993 through 1999, the United States made almost no contributions to the African Development Bank. Nonetheless, over the course of the Bank's history, the United States has provided about 5.3% of the Bank's capital. It is the largest non-regional shareholder and the third leading contributor after Nigeria (9.1%) and Egypt (5.5%). The U.S. pledge to GCI-V over eight years, if fulfilled, would make the United States the second leading contributor by giving it a 6.7% share in the Bank.

For FY2000, the Clinton Administration had sought a \$5.1 million appropriation for the Bank to pay the first instalment of its \$40.8 million paid-in capital pledge. The final Foreign Operations Appropriations (H.R. 3194/P.L. 106-113, incorporating H.R. 3422) provided \$4.1 million. The Administration had also sought an authorization of \$80 million in callable capital,<sup>8</sup> since it had pledged \$640 million over eight years under GCI-V. Instead, H.R. 3422 authorized \$64 million in callable capital. Thus, for FY2001, the Clinton Administration sought and obtained an appropriation of \$6.1 million in paid-in capital and an authorization for \$97.5 million in callable capital for the Bank in order to put the U.S. pledge to GCI-V back on schedule (H.Rept. 106-997/P.L. 106-429). The Bush Administration is requesting \$5.1 million in paid-in capital and \$80 million in callable capital for the Bank in FY2002,<sup>9</sup> which would maintain the GCI-V schedule.

In the mid-1990s, the United States led other non-regionals in a decision to suspend negotiations on a new replenishment for the African Development Fund until the Bank agreed to sweeping reforms. Congress rescinded half of the FY1995 appropriation for the Fund. In subsequent years, the Administration requested new appropriations for the Fund as a means of showing approval for the Kabbaj reforms and maintaining U.S. influence, but Congress made no appropriation for FY1996 or 1997, due to concerns over the situation at the Bank and overall budgetary constraints.

### African Development Fund: Requests and Appropriations

(fiscal years, \$ millions)

	1997	1998	1999	2000	2001	2002
Request	50.0	50.0	155.0	127.0	100.0	100.0
Appropriation	0	45.0	128.0	128.0	100.0	

Contributions to the Fund resumed in FY1998, and the funding levels in recent years have made the Fund an important component of the overall U.S. economic assistance program for Africa. The United States historically has contributed 12.4% of the capital

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<sup>8</sup> Callable capital does not need to be appropriated, but it must be authorized. See CRS Issue Brief IB96008, *Multilateral Development Banks: Issues for the 107<sup>th</sup> Congress*.

<sup>9</sup> Executive Office of the President, *Budget of the United States Government, Fiscal Year 2002, Appendix*, p.1010-1011.

of the African Development Fund and is the second leading contributor after Japan (14%). The Bush Administration is seeking \$100 million for the Fund in FY2002.

## Current Issues

**Bank Lending Policies.** The stricter lending policies introduced at the Bank with the Kabbaj reforms mean that most sub-Saharan governments are ineligible to borrow from what they regard as “their bank.” The thirty-nine poorest members of the Bank Group must rely solely on the resources of the Fund. International banking experts note that if lending standards were lowered, both the Bank and the borrowers would likely face deepening economic problems. Moreover, some point out, the Bank has launched an initiative aimed at increasing lending for viable private-sector projects around the continent, including foreign exchange-generating projects in poor countries.

**HIPC.** In 1996, the World Bank and the International Monetary Fund launched the Highly Indebted Poor Country (HIPC) Initiative aimed at reducing debts owed by poor countries to bilateral and multilateral lenders. (CRS Report RL30214, *Debt Reduction: Initiatives for the Most Heavily Indebted Poor Countries*). In June 1999, the G-7 summit in Cologne, Germany, endorsed an enhanced HIPC Initiative aimed at providing even deeper debt relief, including relief from debt owed to multilateral development banks (MDBs). Some MDBs, including the AfDB, lack sufficient resources to forgive debts owed them, and will have to rely in part on contributions from the World Bank’s HIPC Trust Fund in order to fully participate in the initiative. The potential total cost of AfDB debt forgiveness is estimated at \$2.2 billion. The HIPC Trust Fund is funded by donor countries, and some question whether taxpayers in the non-regionals should be asked to bear the costs of unsustainable loans made by Bank managers in the past. Others maintain that debt forgiveness is essential to African economic recovery.

**Role of the Bank Group.** The Bank Group is one of many development agencies active in Africa, and it disburses smaller amounts in the sub-Saharan region each year than the World Bank and the major bilateral donors. Thus, some question why there is a need for the Bank Group or for U.S. contributions. In their view, the United States might better focus on its own assistance programs and perhaps those of the World Bank’s IDA, where U.S. influence as a shareholder is greater. IDA concessional lending in Africa totaled \$2.1 billion in 1999 – more than three times the amount lent by the AfDF. Others argue, however, that the Bank Group has a unique understanding of African needs, that African governments more readily accept its advice, and that it is useful for the United States to be seen in Africa as a supporter of an African institution. Some also see value in the development dialog that takes place at the Bank between the regionals and the non-regionals. By participating in the Bank and Fund, they argue, the United States is able to influence the ways in which a significant pool of resources for African development is used.