

Weathering the storm

African public development banks' response to Covid-19 and their recovery role

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Key messages

African public development banks (PDBs) have proved their worth in the crisis and there is a strong case for building much stronger partnerships with international institutions. The vast majority mounted a counter-cyclical response and they have been adaptable and flexible in their operational and financial response.

African PDBs proved themselves to be resourceful actors in crisis response despite the fiscal constraints of many African states, which limited the injection of new capital or provision of state funding.

The profitability of African PDBs was adversely affected in 2020 but recovered in 2021, and asset quality was not unduly affected, showing many banks to be financially resilient.

Central banks and regulators played an important role in supporting and enabling African PDBs to respond to the impacts of the pandemic.

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Acronyms

AADFI	Association of African Development Finance Institutions
AFC	Agricultural Finance Corporation
AfDB	African Development Bank
AU	African Union
BCEAO	Banque Centrale des Etats de l'Afrique de l'Ouest
BDEAC	Banque de Développement des Etats de l'Afrique Centrale
BDEGL	Banque de Développement des Etats des Grands Lacs
BMICE	Banque Maghrébine d'Investissement et de Commerce Extérieur
BNDE	Banque Nationale de Développement Economique
BNi	Banque Nationale d'Investissement
BOAD	Banque Ouest Africaine de Développement
BOI	Bank of Industry Limited
CBK	Central Bank of Kenya
CBN	Central Bank of Nigeria
CDC-CI	Caisse de Dépôts et de Consignations de la Côte d'Ivoire
CEDA	Citizen Entrepreneurial Development Agency
DBN	Development Bank of Nigeria
DBS	Development Bank of Seychelles
DBSA	Development Bank of Southern Africa
DBZ	Development Bank of Zambia
DFI	Development Finance Institution
EBID	ECOWAS Bank for Investment and Development
ECOWAS	Economic Community of West African States
EDF	Export Development Fund
EIB	European Investment Bank
FPI	Fonds de Promotion de l'Industrie
GCAM	Groupe Crédit Agricole du Maroc (Tamwil El Fellah)
GDP	gross domestic product
GFC	Global Financial Crisis
GLP	Gross Loan Portfolio
IDBZ	Infrastructure Development Bank of Zimbabwe
IMF	International Monetary Fund
MAIIC	Malawi Agricultural and Industrial Investment Corporation
MDB	Multilateral Development Bank
MSMEs	micro-, small- and medium-sized enterprises
NEXIM	Nigerian Export Import Bank
NIB	National Investment Bank Ltd
NPLs	non-performing loans
PDB	public development bank
PPE	personal protective equipment
PRGT	Poverty Reduction and Growth Trust
PSGRS	Prudential Standards, Guidelines, and Rating System
RDB	Regional Development Bank
ROA	return on assets
RST	Resiliency and Sustainability Trust
SADC	Southern African Development Community
SDGs	Sustainable Development Goals

SDR	Special Drawing Rights
SME	small- to medium-sized enterprise
STB	Société Tunisienne de Banque
TIB	TIB Development Bank
USD	United States Dollars

Executive summary

This paper represents the first deep study of African public development banks (PDBs) in their response to Covid-19. It seeks to highlight the role of African PDBs in the wake of the Covid-19 pandemic; understand the impacts of the shock on the banks themselves; and explore the implications for their role in sustaining a low-carbon and climate-resilient economic recovery in the countries where they operate.

The study demonstrates **how African PDBs have proved their worth** in the crisis and **underscores the case for a much closer partnership with international institutions**. The experiences documented here underscore the critical roles that PDBs can play, not only in building economic resilience to crises but also as active agents of industrial and economic policy. These roles become even more critical as crises become more frequent and complex, reversing years of development progress in Africa and leaving African countries some of the most exposed in the world to the most harmful effects of climate change. However, several challenges – particularly high capital costs and limited access to funding – inhibit the full realisation of this potential.

We highlight the following key findings:

African PDBs have been adaptable and flexible in their operational and financial response to the unprecedented impacts of the Covid-19 pandemic, moving to new, flexible ways of remote working, streamlining investment approval processes and adopting new technologies, resulting in greater efficiency and faster disbursement of finance. Many banks shifted their sectoral focus to respond to the crisis, with a noticeable move to support domestic healthcare systems and micro-, small- and medium-sized enterprises (MSMEs). Some PDBs have also shifted strategically to address important future needs – with a strong focus on the green transition and infrastructure in several PDBs, which will have lasting economic benefits for their countries.

The vast majority of the African PDBs studied mounted a counter-cyclical response. Most of this has been in the form of short-term debt relief to existing clients and/or expanded lending. The necessity to respond also drove innovation in lending in several PDBs. The degree of response and innovation, however, varied. The study finds that PDBs adopted a restricted, responsive or proactive strategic response depending on institutional circumstances and

financial health. For a handful of banks of weak financial standing, the crisis accelerated internal reform efforts.

Portfolios remained resilient – the profitability of African PDBs was adversely affected in 2020 but recovered in 2021. Profitability levels are low overall and will limit the ability of African PDBs to materially scale their future lending. The study analysis suggests that, for many PDBs, decreases in net interest margin and/or increased cost bases affected profitability more in 2020 than loan impairment due to servicing difficulties associated with the Covid-19 shock. While African PDBs' financial management has sometimes been viewed with scepticism, we find evidence of good financial health, and many banks are seeking to reform and restructure their internal processes, strengthening their governance and risk management.

Central banks and regulators have played an important role in supporting and enabling African PDBs to respond in a counter-cyclical manner. Central banks and regulators undertook several actions which supported the PDB response and eased the financial pressures on PDBs created by Covid-19, including relaxation of non-performing loan (NPL) provisioning and liquidity requirements and the provision of new concessional funding. For banks in a weak financial position, government or central bank support was critical in improving risk management practices and increasing PDBs' autonomy and resilience.

Considering the fiscal constraints facing many African states, which limited new equity injections and new external support from Multilateral Development Banks (MDBs), Regional Development Banks (RDBs), Development Finance Institutions (DFIs) and climate funds, African PDBs proved themselves to be important and resourceful crisis response actors. Despite their small size and insufficient capitalisation, they managed to respond in a counter-cyclical manner, leveraging external commercial borrowing and customer deposits and using reserves (such as retained earnings) to support their crisis response. However, overall gearing levels remain very low, which limit ability to scale new investment.

Lack of access to finance and high capital costs remain key constraints. Insufficient capitalisation, low profitability and the high costs of capital limit the firepower and capacity of many PDBs in supporting recovery, as well as longer-term ambitions to transition to low-carbon, climate-resilient economies. These constraints also restrict the ability of PDBs to respond rapidly to future crises.

This study makes several recommendations to overcome these constraints:

Key recommendations

1 Increase the capitalisation and access to affordable funding of African PDBs

PDBs, governments and international development partners should actively explore how the capital base of well-run PDBs can be expanded, and how to increase PDB access to cheaper sources of external concessional funding. Considering the fiscal constraints facing many African countries, some ideas worth considering include:

- An exploration of how the \$100 billion reallocation of International Monetary Fund (IMF) Special Drawing Rights (SDR) through the IMF's Poverty Reduction and Growth Trust (PRGT) and/or the new Resiliency and Sustainability Trust (RST) or more broadly, how the excess SDRs of advanced economies can be made accessible to African PDBs in this endeavour.
- Where feasible, PDBs should seek to increase borrowing to increase their current low levels of gearing. Ratios of debt to equity of less than four are deemed fully compliant with the Association of African Development Finance Institutions (AADFI) Prudential Standards, Guidelines, and Rating System (PSGRS) and is deemed by Fitch to be a fairly conservative financial structure. Untapped sources of domestic savings could be explored, such as sovereign wealth funds and state-managed pension funds. Banks should also seek to build their debt issuance capacity where local capital markets allow.
- The issuance of sovereign guarantees to support increased borrowing of well-run PDBs. This can help ease access to international concessional finance and domestic and international private finance, since credit ratings of domestic PDBs are most often driven by the availability of sovereign support.
- The expansion of the equity base of PDBs by offering new shares to non-state actors such as private investors and/or MDBs, RDBs and other DFIs.
- Use of innovative balance sheet and risk management approaches such as insurance products, for example on callable capital to improve credit ratings or use of insurance to optimise use of capital and meet regulatory limits.

2 Increase international support to build the capacity of PDBs

Many banks are seeking to expand their portfolio in order to play a larger role in economic transformation, in supporting the green transition and ensuring their own financial resilience. There is a key

role for external partners and global funds in supporting these ambitions through increased technical assistance, training and co-financing. This includes an enhanced external role for AADFI.

3 Build strong PDB governance frameworks and adopt best practices in risk management

The Covid-19 crisis and the necessity to respond has highlighted the importance of building well-governed, financially strong and resilient PDBs with strong risk management frameworks.

African PDBs that do not yet assess their governance and financial performance against the AADFI PSGRS should aim to do so. Those African PDBs that do should target annual improvement in areas where they are found to be partially or non-compliant. Platforms such as the AADFI should be supported as a channel for knowledge exchange and information sharing.

4 Ensure a supportive regulatory and policy environment

The experience of the studied PDBs has underscored the importance of tailored regulation of PDBs, central bank support and integration with government policy. National governments and bank regulators should review national regulation to ensure that it supports the development mandate of PDBs, as well as ensuring that this mandate aligns with national strategic objectives.

1 Introduction

Over two years on from the onset of the coronavirus pandemic, economies across the world face an ongoing challenge in managing health interventions and ensuring economic recovery, while being buffeted by the impacts of new geopolitical shocks.

In Africa, the impacts of Covid-19 have been grave for health, for economies and for public finances. In the early phases of the crisis, there were urgent calls for finance to protect households, individuals and livelihoods, and to shield the private sector against lasting damage. However, unlike in Europe, where citizens have access to government stimulus payments, social protection and relief for businesses, the fiscal space for African governments is far more constrained.

In March 2020 African finance ministers called urgently for a fiscal stimulus, and requested the release of \$100 billion from the IMF, including \$50 billion for the 'building back' process and meeting debt repayments (UNECA, 2020a). There were also call for the G20, the EU and northern DFIs to support refinancing, rescheduling and the implementation of guarantee schemes and liquidity facilities for the private sector, including the creation of a 'bounce back better' facility (Griffith-Jones and te Velde, 2020). At the national and regional level, PDBs and DFIs were also identified as a key part of the public finance counter-cyclical response (Miller et al., 2020; Bilal, 2021).

This study examines the following questions:

- 1) Did African PDBs play a counter-cyclical role in confronting the Covid-19 crisis? What kind of responses do we see, and on what scale?
- 2) How were African PDBs financially impacted by the effects of Covid-19 on domestic economies? How did this affect their ability to react?
- 3) How have African PDBs been utilised or supported by shareholding governments and partners in their response, and as instruments of broader economic recovery?

In doing so we explore *what* PDBs did in 2020 and 2021 in responding to the crisis and financing an economic recovery, and *why* some were better prepared than others in their response.

1.1 Motivations of the study

This study aims to further develop a body of evidence on the role of PDBs in economic development, and as a counter-cyclical vehicle for economic resilience in times of crisis. Specifically, it aims to contribute to the knowledge and evidence base on the role of PDBs in Africa, which remains understudied compared to other regions.

Many African PDBs were established in the late colonial/early independence period to provide access to credit, often targeting specific sectors and industries, such as agriculture and housing. During the era of structural adjustment in the 1980s many of these banks were dismantled or privatised as financial markets and capital accounts were liberalised (Culpeper, 2012). Despite their ubiquity across the continent, and their significant diversity, their small size and capacity have limited their potential to play the kind of catalytic role seen in Asia and Latin America, where PDBs were key instruments in fostering industrialisation and infrastructure investment (Lazzarini et al., 2015; Griffith-Jones and Ocampo, 2018; Attridge, Chen and Mbate, 2021). Perceptions of political interference have also been a major issue (Karingi, 2007; Scott, 2007; Attridge, Chen and Mbate, 2021).

An inherent dilemma for many PDBs is reconciling two sometimes contradictory objectives in their operations: achieving a social or policy objective that is developmental rather than commercially driven, while remaining financially sustainable. In the event of a crisis, this dilemma becomes more acute – PDBs have a mandate to support the wider economy and ensure sustainable recovery, while at the same time their financial soundness and resilience will come under pressure as economic shocks impact their client base and portfolios.

While the health impacts of the pandemic in Africa were relatively contained, lockdowns, a halt on travel, and backlogs in global supply chains in 2020 had grave economic impacts for the private sector. In 2020, four out of five businesses in Africa were ‘significantly impacted’ by the drop in demand, shutdowns in the economy, and a lack of working capital (UNECA, 2020b). The tourism and hospitality sectors were particularly hard hit: the former accounts for more than 10% of GDP in 20 African states, and in small island states constitutes over 20% of total employment (AU, 2020). For small firms, the risk is that impacts may be structural: for example, firms may sell off their productive assets to cope with the effects of the pandemic, reducing their ability to recover and impacting the long-term productivity of the economy (Miller et al., 2020).

For banks and financial institutions exposed to affected sectors, the growth in ‘bad debts’ (i.e. non-performing loans) impacts asset quality and their ability to provide additional support (Tyson, 2020; EIB, 2021). One study by AADFI in April 2020 highlighted several salient challenges for PDBs, including: the risk of reallocated finance away

from the bank to other sectors such as health and social protection; risks for asset quality from the slowdown in sectors such as hospitality and small- to medium-sized enterprises (SMEs); and additional pressures on banks to grant moratoriums and revise terms of credit. At the same time, banks need additional funding to build their own capital buffers, capacity-building in areas such as digital and fintech, and better risk assessment and risk management (AADFI, 2020).

The evidence from this study supports the idea that **African PDBs, when well-governed and financially sound, play a key role as vehicles of national strategy, in supporting crisis response and economic recovery**. We found a strong tendency to counter-cyclical responses from a significant proportion of banks. However, banks that were dealing with poor financial performance were less well-positioned to play this buffering role in the economy, and in some cases, the crisis tipped them over the edge financially.

African PDBs show not only adaptability and flexibility in their response to crisis in the short term, but also in their long-term role, reforming their capacity for risk management, adopting new technologies, and positioning themselves to support new sectors, including in emerging climate sectors for a potential green recovery (Griffith-Jones et al., 2020; Muñoz Cabré et al., 2020).

The growing interest in PDBs in recent years, encapsulated in the creation of the Finance in Common movement, raises fresh questions for their role in the wake of the Covid-19 crisis, and in the 'build back better' process (Riano, 2020; Bilal, 2021). Alongside this, the movement for reallocation of SDRs to Africa has gained momentum, following summits in Paris in 2021 and the EU–Africa Summit in early 2022. In April 2021, G20 countries pledged to reallocate \$100 billion of SDRs to vulnerable countries in Africa and Latin America. While progress on this has been piecemeal, new developments, including the IMF's RST, show the potential for SDRs to support a sustainable transition, and as a new resource for African states.

1.2 Structure of this paper

This paper is organised into five parts. Part 1 introduces our key research questions and the motivations for this study. Part 2 outlines our methodological approach and the survey methods and data that inform the subsequent analysis, as well as limitations of the research. Part 3 reviews the academic and policy literature on the economic development role of PDBs, and their role in crisis response. Part 4 interrogates the results of our qualitative and quantitative survey and our interviews with key PDB informants.

Part 4 focuses on five areas: the operational adaptability and flexibility of PDBs during the crisis; responses to the crisis by the banks; the impacts of Covid-19 on PDBs; financial allocations and

external support from governments and other partners; and finally, the challenges and constraints facing these banks. The analysis is supported by ‘deep-dive’ case studies of four PDBs, and two comparative case studies of multiple banks. Part 5 concludes with a summary of key takeaways from our analysis, and policy recommendations for governments and international partners of PDBs.

2 Methodology and research approach

The study research relies on a mixed-methods approach, drawing on three types of data and evidence: a qualitative survey of PDBs, highlighting broad trends; a quantitative analysis of financial metrics collected directly from primary and secondary data; and semi-structured interviews with representatives of PDBs.

2.1 Survey and financial metrics analysis

In partnership with the AADFI, we conducted two cross-sectional studies with respondents from African national and sub-regional PDBs. The first was a structured survey questionnaire, which received 25 full responses, regarding the impact of Covid-19 on each bank's financial resilience and response to the pandemic, as well as their role in the broader economic response to the crisis.

Of the 25 surveyed banks, five were regional, multilateral PDBs with multiple African sovereign shareholders, while the remainder were national PDBs, with shareholding largely within a single country. The majority of sampled banks had a broad, multi-sector developmental mandate, with a minority of approximately seven that had a specific, sectoral mandate, including agriculture, MSMEs and export-import. Five were deposit-taking banks. A full list of participating banks can be found in Appendix 1.

The second study was a financial metrics questionnaire and analysis, asking respondents to provide key information from the bank's balance sheet from both pre-crisis and post-crisis years. Where possible, data was collected between 2017 and 2021 and substantiated by public data from audited Annual Reports. In total, we gathered data for 17 PDBs spanning the period 2017–2021. This allowed us to look at variations between institutions as well as over time before, during and following the pandemic.

The 17 responses to the questionnaire were compiled to build an anonymised data set aggregating key financial indicators. To ensure comparable modes of data analysis between PDBs, expert assessments of key financial criteria were used to generate raw measures; this was done instead of an index or categorical measures, which may obscure variation in financial performance, with all data (unless otherwise stated) analysed in USD. Where data was collected in local currency, an average annual exchange rate

was calculated in order to convert data representing yearly flows, and an end of year exchange rate used to calculate stocks for balance sheet figures.¹

A geographic breakdown of sample banks by sub-region is shown in Table 1.

2.2 Case studies

Based on the list of respondents to the survey and financial analysis, follow-up interviews were arranged with selected institutions to probe further PDB responses to Covid-19 as well as the impact of the crisis on banks. This provided a more detailed understanding of individual experiences, the chronology of responses, as well as idiosyncratic contexts and constraints of individual banks. Between July and September 2022, a total of 11 banks were interviewed, using a semi-structured questionnaire.² Our constrained sample size and language coverage meant we focused on Anglophone and Francophone institutions; Lusophone country PDBs are not represented in our interviews or in the study.

Table 1 Breakdown of PDB study participants: survey, financial metrics and case study interviews

Africa sub-region	Survey	Financial metrics	Case study
North	3	2	1
West	9	5	5
Central	2	0	0
East	5	5	3
South	6	5	2
TOTAL	25	17	11

2.3 Scope and limitations of the research

Over 100 institutions are classified as PDBs across Africa (Attridge et al., 2020). While this research does not provide a comprehensive overview of this large universe, it does showcase a wide range of experiences by studying banks across geographies and income levels.

The data collection process began through a process of contacting the AADFI membership, which, though not fully representative, does include a wide array of African PDBs. However, only a subset of these institutions participated in the research surveys and interviews. The voluntary and self-selective nature of our data collection

¹ It is important to note that even though the use of USD units allows for a comparable analysis between banks, some discrepancies may result from this currency conversion.

² Eight interviews were conducted in English and two in French. However, our survey respondents were broadly split between Francophone and Anglophone banks, with 11 and 14 banks, respectively.

methods entails a degree of selection bias in our analysis as transparency standards, levels of capacity and bureaucratic incentives to respond will vary significantly across African PDBs. As such, we may experience an overrepresentation in our sample and in our analysis of stronger, well-connected or more well-managed banks, who have greater capacity or incentives to participate.

Lack of data was a challenge, especially in regard to the quantitative financial metrics analysis. Only 13 banks completed the survey requesting detailed financial data. To broaden the sample size of the research data set we extracted information from annual reports, but only a limited number of PDBs had public online documentation, and even fewer had updated financial statements to 2021. This sample size thus struck a balance between the availability of data and the capacity of the researchers to extract it.

3 Public development banks in times of crisis

3.1 The role of PDBs

PDBs serve several, often overlapping, roles.³ First, and fundamentally, they provide capital that increases financial access for firms and households otherwise unable to access capital markets (Eslava and Freixas, 2021). In low-income countries, where the cost of capital is prohibitively high, PDBs can provide better terms and longer tenures. This can be crucial for supporting long-term infrastructure investment (Hu et al., 2022).

Second, PDBs, and particularly national PDBs, resolve market failures and inefficiencies (Ocampo and Ortega, 2022). Many PDBs lend to smaller firms and SMEs as a focus, and their knowledge and embeddedness in local economies gives them a comparative advantage over larger or commercial lenders in targeting projects and assessing risk (Luna-Martinez, 2017). They can also inform and shape productive public policy (Fernández-Arias et al., 2020).

Third, PDBs can serve as instruments of industrial policy, given their unique position ‘at the frontier between state and market’ (Xu et al., 2021). Beyond fixing market failures, banks can shape and create new markets: investing in frontier sectors that private finance may be reluctant to enter, promoting innovation and mobilising further investment (Mazzucato and Penna, 2015). Their close integration with public policy structures and national strategies gives them a structural role in fostering economic growth and transformation (Gerschenkron, 1979; Culpeper, 2012; Musacchio Farias and Lazzarini, 2014), from SME sectors to green technologies (Griffith-Jones et al., 2020).

Finally, PDBs can be an instrument for counter-cyclical policy in supporting economic resilience. This role of catalysing supply is highly relevant during periods of crisis, as PDBs can buffer against the pro-cyclical tendencies of private sector finance, smoothing out credit cycles when private capital goes into retreat (Smallridge and de Ollouqui, 2011; Brei and Schclarek, 2017; Griffith-Jones and Ocampo, 2018). It is this role of resilience and recovery that forms the focus of this paper.

³ See, for example, Griffith-Jones and Ocampo (2018), which identifies at least *five* roles that development banks play in the development process.

3.2 PDBs as a vehicle of crisis response

In times of crisis, uncertainty from an economic shock can cause a credit crunch, leading to wider deflationary spirals unless there is exogenous support (Culpeper, 2012). In mediating the social and economic impacts of these crises, there is arguably an intervention role for government and public actors in shortening the duration of such crises, and fostering economic recovery (Calderón et al., 2016; Fetai, 2017).

PDBs can be a key vehicle in such counter-cyclical responses (Wagner, 2020). While lending from private and foreign banks tends to pull back, PDBs' lending tends to be smoother, ensuring a stabilising or smoothing effect on credit access (Micco and Panizza, 2006; Bertay et al., 2015) and helping to buffer impacts of exogenous, international shocks (Allen et al., 2013).

Owing to their public mandate, PDBs are less driven by profit maximisation, and may also benefit from more stable financial resources, given their proximity to the state (Behr et al., 2017; Léon, 2020). This gives them a higher risk tolerance in periods of crisis, and greater capacity than private banks to act counter-cyclically.

Primarily, this involves increasing liquidity to the economy, usually through the rapid expansion of lending. In Latin America, governments used development banks and public sector banks as instruments of counter-cyclical policy to mitigate the impact of the global financial crisis (GFC) (Ocampo, 2009). Brei and Schclarek (2017) note the average growth rate of lending by national PDBs in the region increases from around 3% to 10% during times of crisis, compared to a reduction in average lending of 3% from foreign and domestic private banks.

During the GFC, the loan books of PDBs globally expanded significantly: a 2012 World Bank study found that, between 2008 and 2009, the combined loan portfolio of the PDBs surveyed grew from \$1.16 trillion to \$1.58 trillion, a 36% increase in lending that far outstripped the 10% increase in private bank credit (De Luna-Martínez and Vicente, 2012). This also supported customers from private commercial banks who faced difficulties in refinancing loans or acquiring new credit (ibid.: 8).

PDBs may also support clients by increasing the concessionality of products (i.e. lowering the cost of lending) or creating new targeted financial products or innovations. In Latin America, PDBs during the GFC created targeted preferential credit lines to a range of sectors, including agriculture, housing, industry, infrastructure, trade and SMEs. They also channelled resources to infrastructure funds and financial intermediaries, and used them to guarantee company share issues (Smallridge and de Olloqui, 2011). Brazil's BNDES, for example, implemented new investment programmes to finance acquisition of domestically produced machinery and equipment,

reducing interest rates to further incentivise borrowers (Brei and Schclarek, 2017).

In Europe, European Investment Bank (EIB) lending supported SME sectors hit by the GFC through intermediated lending – which increased lending to SMEs by 128% – as well as innovations such as equity and mezzanine financing and risk funding, and non-financial support through technical assistance (Griffith-Jones et al., 2011). However, many European PDBs were also criticised for not being counter-cyclical *enough* as the value of new commitments was lower following the crisis than previously (te Velde, 2011).

PDBs have also been involved in supporting other crises, for example during the Ebola epidemic in 2014, where regional and multilateral PDBs – most visibly the African Development Bank – played an intervening role in capacity-building in the healthcare sector, alongside smaller financial contributions from sub-regional PDBs to the emergency response (AfDB, 2015).⁴

3.3 Financial structure and capacity

The mobilisation of an expansionary counter-cyclical response may be predicated on broader structural conditions. It is dependent on a bank's own financial and technical capacity, but this in turn is dependent on the enabling institutions, such as government shareholders or regulators, that can provide external directives or political and financial support.

A key feature of PDBs' funding structures that favours their ability to act counter-cyclically is that they are generally less dependent on deposits, instead relying more on stable, longer-term funding structures, as well as being better positioned to call on government support and recapitalisation during a crisis (Brei and Schclarek, 2015). This credibility may give them a higher risk tolerance during periods of instability.

Sufficient capitalisation of PDBs is a crucial factor in enabling counter-cyclical responses. Griffiths-Jones et al. (2011) note that the EIB's lending during the GFC was feasible because of its capitalisation in the years prior to the crisis, which meant no capital constraints to increasing lending rapidly.

3.4 Institutional context and enabling environment

The wider enabling environment, in terms of a government's broader macroeconomic response, as well as the responsiveness and quality of governing and regulatory institutions, also conditions the scope of PDBs' counter-cyclical responses. During the Covid-19 pandemic, EU state aid laws were relaxed to allow governments to extend support to MSMEs and hard-hit sectors in tourism and hospitality.

⁴ Examples include small donations from PTA Bank (now TDB) to the Africa against Ebola Solidarity Trust (AAEST), and from Afrieximbank to AfDB facilities to counter Ebola. EBID also supported national-level Covid responses in Liberia.

PDBs were instrumentalised as part of this emergency response, with loan guarantee schemes as a key mechanism (Mertens et al., 2020).⁵

The intervening role of the state in South Africa during the Covid-19 pandemic was also significant, with a large fiscal stimulus package, a raft of monetary measures, and support for small businesses – some of which was channelled through the Industrial Development Corporation (IDC) (Khambule, 2021). However, low-income and fragile states will have far less fiscal space and reserves to implement such counter-cyclical measures (Kasekende et al., 2010).

Some scholars also advocate caution on the use of PDBs as instruments of counter-cyclical policy. Smallridge and Olloqui (2011) argue that the counter-cyclical role of PDBs should be temporary and limited, noting the risk of crowding out effects on the private sector in the long term. Others criticise the poor record and efficiency of state banks in credit allocation (Bertay et al., 2015).

In weaker institutional contexts, monetary and fiscal policy tend to be more pro-cyclical (Calderón et al., 2016), reducing the likelihood of PDBs being mobilised or adequately supported to mount a crisis response. Evidence suggests that stronger counter-cyclical responses may be conditional on the presence of good surrounding institutions (Bertay et al., 2015; Léon, 2020). The positive impacts on bank performance and GDP growth that come from lending increases by government banks is also strongly predicated on low levels of corruption (Chen et al., 2016). In sum, the responses of PDBs will be heavily conditioned by the institutional context and enabling environment in which they operate.

⁵ Loan guarantee schemes from the EIB aimed to mobilise up to €40 billion of liquidity support to mid-cap (mid-capitalisation) firms and SMEs, covering up to 100% of risk.

4 Responses to and impacts on African PDBs from the Covid-19 shock

African PDBs faced significant, unprecedented impacts from the Covid-19 shock, in parallel to their counterparts in other parts of the world, with ramifications for their operations, the sectors they served and their financial performance.

Drawing from existing research and evidence, we focus on three main categories of crisis response: operational, financial and institutional. While much of the literature focuses on *financial* responses, largely in terms of volumes of counter-cyclical lending, it is also important to examine the operational responses of African PDBs in their day-to-day work, given the unprecedented nature of the Covid-19 pandemic and lockdowns, as well as institutional conditions, in order to understand how they were supported and enabled in their financial response. These aspects have been neglected in the academic literature.

Based on these categories, we identify three broad types of strategic responses from PDBs, which we label *restricted*, *responsive* and *proactive*. This assessment is based on the type and scale of activities, responses and institutional changes observed from the survey, financial metrics analysis and case interviews (Table 2).

Restricted strategies focused on prioritising the financial health and survival of the PDB itself, with minimal counter-cyclical activities. *Responsive* strategies indicate a notable counter-cyclical response from the PDB to support its clients and sectors, while *proactive* strategies indicate a significant expansion to new clients, sectors or issue areas. These are *not categories of individual PDBs*, but the strategies and actions taken. A single bank may take actions that fall across multiple types of strategies.

Table 2 Strategies of PDBs in confronting Covid-19 impacts

<div>Banking strategy</div> <div>Focus area</div>	Restricted <i>Protecting bank</i>	Responsive <i>Protecting clients</i>	Proactive <i>Supporting economy</i>
OPERATIONAL (Adaptation of staff and management; changing staffing/personnel structure; sectoral focus)	Staffing reduced Significant cost-saving measures	Minor change or redeployment of staff Adoption of new technologies Streamlining approval processes	Redeployment or expansion of staffing in new areas Training and capacity building for staff Diversification into new sectors Supporting emergency responses
FINANCIAL (Lending volumes; debt relief; financial instruments; non-financial initiatives)	Pullback of lending and finance Restricting or reducing services from existing client base Limited or short-term debt relief measures Increasing costs on financial products	Maintaining or slightly increasing levels of lending Debt suspension for clients Flexible debt relief measures for clients Decreasing costs on financial products	Expanding lending services significantly beyond existing client base Creating new financial products and innovations Covid-19 targeted interventions Participation in other government initiatives
INSTITUTIONAL (Collaboration and cooperation; institutional reform; capitalisation and funding structures)	Minimal change, isolated responses Narrowing of bank priorities	Seeks to bolster funding support from shareholders and partners Reform of operational procedures and processes to ensure financial sustainability	Expanding bank priorities, diversification into new economic sectors Expanding collaboration with other banks and institutions Diversifying funding structures and financing models

Note: Authors' synthesis from literature and collected data.

While heavily impacted, our sample of African PDBs shows a high level of adaptability and resilience to the economic shocks created by the global crisis. They faced heterogeneous financial impacts and took diverse approaches in their response. With a minority of PDBs, we see *restricted* strategies, particularly in financial responses, with decreased risk appetite and a contraction in its products and services offered. For PDBs that used restrictive strategies, weak financial

health, often as a result of pre-existing financial governance issues, alongside impacts from Covid-19, limited their ability to play a counter-cyclical role and forced them to focus on protecting their financial health.

The vast majority of PDBs surveyed adopted counter-cyclical responses, with (often overlapping) *responsive* and *proactive* strategies. Primarily, this included debt relief to existing clients, expansion of the loan book and, in some cases, expanding services into new areas and involvement in wider national strategies, such as health capacity or investment in new sectors. Despite this, there has been little public short-term or emergency financial support for most banks, and capital constraints – in access and cost – remain a key challenge.

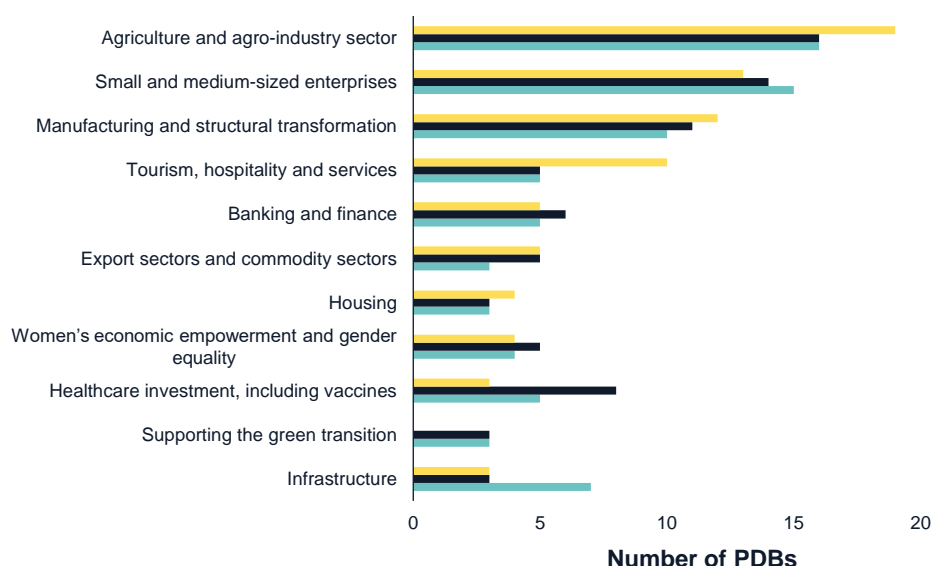
4.1 Operational strategies and responses

While publicly owned banks are often perceived as rigid and inefficient, PDBs in our sample showed adaptability and flexibility in confronting the impacts arising from the Covid-19 pandemic. Many proactively shifted their strategic priorities, adopting new technologies and remote work, and taking measures to expand operations and improve productivity.

4.1.1 Shifting strategic priorities

Figure 1 Shift in PDBs' sectoral priorities 2019–2020

■ 2019 ■ 2020 ■ 2021



Note: Represents the number of PDBs that cited each sector as a priority year-on-year.

Source: ODI-AADFI survey of African PDBs

Our sample of PDBs has a strong sectoral focus in agriculture and agro-industry, SMEs and manufacturing and structural transformation. Over the three years from 2019, however, we see a moderate shift from the impact of Covid-19 on how the sample banks evaluated their strategic priorities. Unsurprisingly, a small number of banks shifted heavily towards healthcare sectors in 2020; SMEs have slightly grown as priorities for a number of banks, while tourism fell as a priority for a significant number of banks in our sample.

The latter is somewhat surprising, given the impact of Covid lockdowns in the travel sector, though our interviews highlighted ways that PDBs targeted travel and hospitality sectors. In the case of the Development Bank of Seychelles (DBS), there was a shift to support businesses adjacent to the tourism and hospitality sector that were impacted by the downturn in travel, rather than the travel sector itself. In the case of the ECOWAS Bank for Investment and Development (EBID), the hotel sector was a clear focus in 2020 in its response to Covid-19, and the bank was proactive in reaching out to hotel enterprises with financial support and debt relief.

We see a slight shift in 2020 and 2021 as infrastructure and supporting the green transition become more prominent among our survey respondents as strategic priorities, indicating – at least for a small number of PDBs – a more proactive focus in these sectors in the post-Covid recovery. For the Development Bank of South Africa

(DBSA), for example, climate initiatives and renewable energy generation were a particular focus, though interviewees noted this was still ‘a work in progress’ (see Box 1). The green transition in the Seychelles is also a key focus of the DBS, which is actively diversifying into new sectors, with a strong emphasis on sustainable transport and renewable energy, via support from an EIB line of credit.

Box 1 The Development Bank of Southern Africa: supporting the healthcare sector, infrastructure development and the green transition

The Development Bank of Southern Africa (DBSA), one of Africa’s leading DFIs, aims to foster inclusive development across Africa by increasing access to development finance targeted towards sustainable infrastructure development. Created in 1983 and wholly owned by the government of South Africa, the DBSA raises debt funding from multiple sources, including local and international financial institutions and fund managers. Like MDBs, the DBSA’s on-balance sheet capital is supported by callable capital amounting to 20 billion rand and is conservatively geared, via a regulatory gearing cap of 2.5 times capital. In recent years, the Bank has sought to diversify its funding, balancing debt market issuance across various tenors, with bilateral loan facilities from banks, MDBs and DFIs.

Covid-19 response package

Following the onset of the pandemic, DBSA channelled its efforts specifically towards the health sector while also targeting green infrastructure projects. In response to the pandemic, the bank financed an array of short- and long-term interventions. Funding to the former envelope was a combined 150 million rand, divided across five initiatives.

- 1) Southern Africa Development Community (SADC) personal protective equipment (PPE) funding – (30.5 million rand). DBSA provided the member states of SADC (including Mozambique, Zimbabwe, Lesotho and Eswatini) with PPE.
- 2) National disaster management centre funding – (15 million rand). The bank provided finance to meet the increased staffing and software procurement needs of the National Coronavirus Command Centre, which has coordinated the national response to the pandemic in South Africa.
- 3) Ventilator production – (6.9 million rand). Through the Council for Scientific and Industrial Research, the DBSA provided financing for the Non-Invasive Ventilators Project, which mitigated the pressure to import equipment.

- 4) Mobile testing units – (26.1 million rand). DBSA is working with 25 district municipalities to provide mobile prefabricated testing units.

Alongside these efforts, DBSA spearheaded long-term interventions, most significantly the Infrastructure Fund, originally announced in 2019 with the goal of accelerating infrastructure delivery in South Africa while channelling investments towards socio-economic infrastructure projects (e.g. student and social housing, broadband and water reuse). This blended finance fund, which received seed capital of 100 billion rand over a 10-year period from the government, seeks to engage with the private sector, MDBs, DFIs and institutional investors to catalyse a total of 1 trillion rand for infrastructure development.

Renewed focus on a clean and just transition

Although Covid-19 slowed the implementation of several infrastructure projects, the pandemic also revived DBSA's approach to the green transition. The bank has committed to net zero by 2050, a commitment supplemented the bank's projects as a Green Climate Fund Accredited Institution and signatory to the Paris Agreement. In 2020, the Department of Energy announced a desire to shift to locally embedded renewable energy generation. DBSA helped manage and finance these activities via its Renewable Energy Independent Power Producer Program. Currently, the Bank seeks to support small municipalities to take steps to make electricity operations more sustainable.

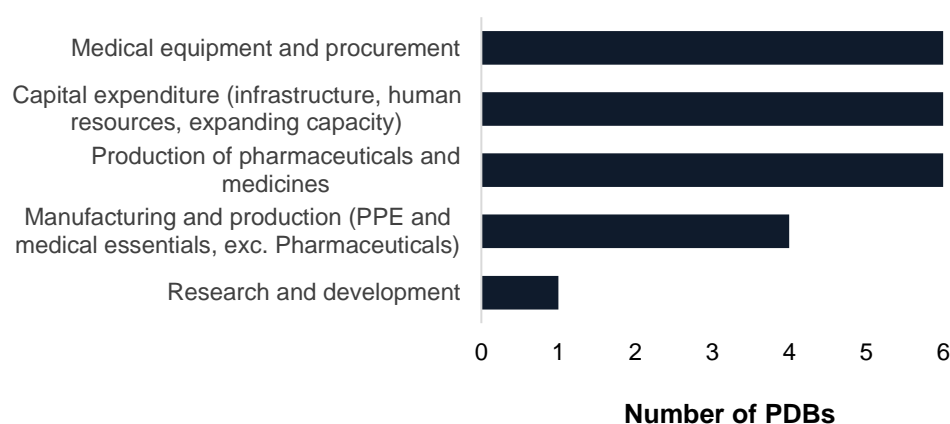
DBSA issued its first Green Bond worth €200 million in 2021 through a private placement with AFD. The proceeds of the bond will be used to fund climate mitigation and adaptation projects envisioned in South Africa's national development plan, which is aligned to the SDGs and supports the transition to a low-carbon and climate-resilient economy. The DBSA's second green bond (3 billion rand) in 2021 was a local currency denominated fixed-rate green bond. This was issued through a private placement fully subscribed to by PIMCO, a global investment management firm. This was the first transaction under the United Nations Economic Commission for Africa SDG7 programme to fund green energy in Africa.

4.1.2 Health interventions and pandemic response

Around a third of banks surveyed indicated that they had stepped into a public health role in some way (Figure 2). This largely took the form of medical equipment procurement, capital expenditures in healthcare sectors and in the production of pharmaceuticals, though some PDBs also noted support in manufacturing (for PPE and other medical equipment). The National Investment Bank (NIB) of Ghana,

for example, was directed by the government to extend its lending into pharmaceutical sectors, and to support local companies to manufacture PPE and Covid-19 medication. Interviewees noted that the NIB was able to expand funding access through the relaxation of provisioning requirements for pharmaceutical sectors, as well as a 10-billion-cedi fund made available by the government, though this was not fully utilised.

Most striking is the case of DBSA, which provided proactive support in the form of medical equipment and PPE domestically and regionally across the SADC, but also in funding national Covid-19 responses, including provisions for funding software for the National Disaster Management Centre, to augment the country's management of the pandemic and strengthen future resilience (see Box 1).

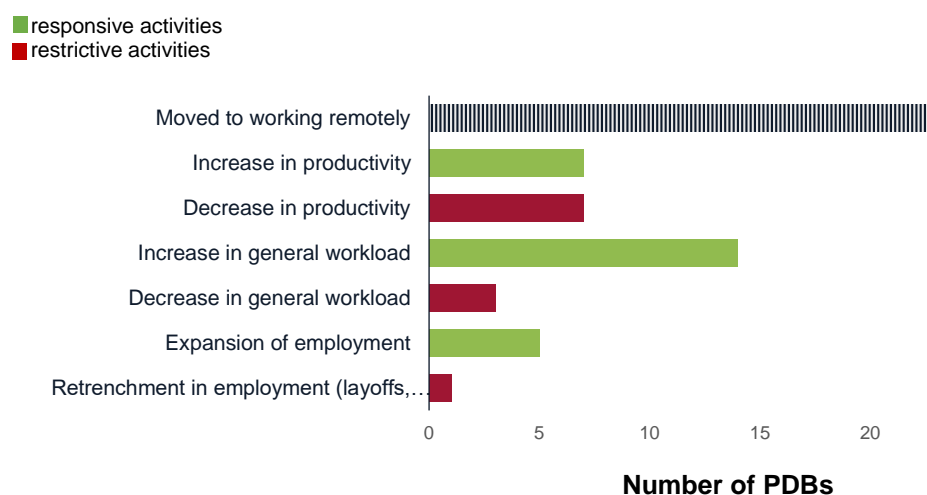
Figure 2 Subsectors of healthcare with PDB involvement

Source: ODI-AADFI survey of African PDBs

4.1.3 Adaptations to work and operational flexibility

A large majority of surveyed respondents (over 80%) stated that they moved to remote work due to the pandemic (Figure 3). On operational impacts, we find mixed responses from PDBs in terms of productivity, workloads and employment changes, showing divergence in how surveyed banks were able to adapt to circumstances.

Increases in workload were more commonly reported, and just under a fifth of surveyed PDBs stated their banks had increased staffing (only one bank stated they had seen retrenchment (layoffs) in employment). These operational responses indicate that, for many banks, the impact of Covid meant *greater* demand for their services.

Figure 3 Operational impacts on PDBs

Note: the move to remote working is deemed to be neither responsive nor restrictive.

Source: ODI-AADFI survey of African PDBs

Aside from moving to remote work, nearly two-thirds (15 out of 25) of surveyed PDBs took *responsive* or *proactive* measures in their operational strategies, including using new digital technologies, and just over half reported capacity-building or staff training. A few exceptions, such as the Development Bank of Seychelles (DBS), faced constraints on their technology and equipment which meant full remote working was impossible, though interviewees noted system upgrades were planned to allow this in the future.

With the move to a digital working model, some banks streamlined their investment approval and information sharing processes to speed up due diligence, approval and disbursement. For example, DBSA moved all its financing systems online, reducing transaction costs in the amount of paperwork and the time involved in approval processes and third-party procurements. As one interviewee noted, '*we used to have reams of paper and we have to deliver to the office, now this has all moved online*'. DBSA also increased the frequency of investment committee meetings, from once to twice a month, to speed up the approval process. This has been a lasting positive impact and outcome of the pandemic.

4.2 Financial responses and impacts

Although banks differ in their strategies and responses, our survey, financial analysis and interviews indicate that the vast majority of PDBs adopted strategies that were counter-cyclical rather than pro-cyclical, with the goal of increasing access to finance and supporting businesses.

At the onset of Covid-19, we find most banks were *responsive* in the provision of short-term debt relief, which targeted existing clients and sectors. Some banks have also played a more expansive role over the pandemic, with clear increases in the gross loan book for many banks, as well as other *proactive* measures such as shifting financing to other sectors of the economy, technical assistance and other innovative forms of engagement with client sectors.

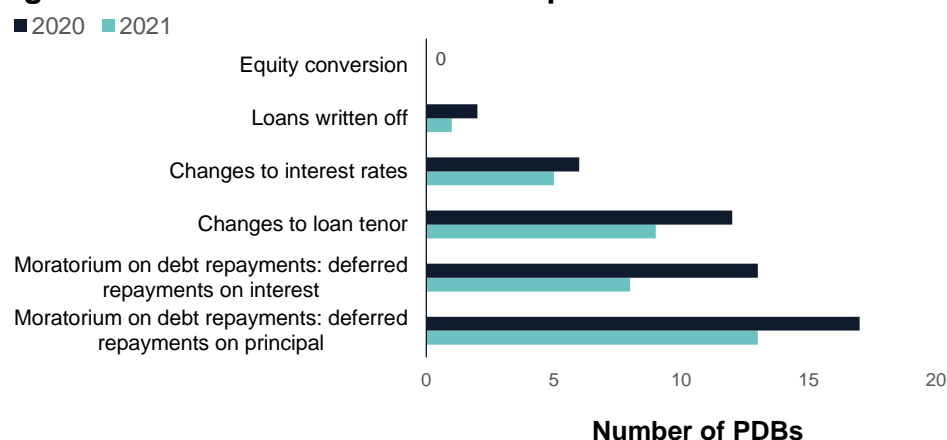
This was strongly conditional on the financial health of the bank, and banks that were financially constrained were more *restrictive* in their activities. While the overall quality of bank portfolios was resilient, the low profitability of many PDBs meant little room to scale their operations and increase lending in times of need. However, we also see many banks implementing internal reforms to improve their financial structure and risk assessment, strengthening their internal resilience.

4.2.1 Provision of debt relief and liquidity

Debt relief was the primary counter-cyclical response offered by PDBs surveyed, with 81% of respondents in 2020 stating their bank

had provided some form of debt relief on financial products to their clients.

Figure 4 Debt relief and financial responses of PDBs 2020–2021



Source: ODI-AADFI survey of African PDBs

This largely took the form of moratoriums on debt repayment on principal, followed by moratoriums on interest and debt rescheduling through changes to loan tenor. The provision of debt relief declined in 2021 (Figure 4), and cases of restructuring involving changes to interest rates are rare. No banks recorded any deeper restructuring via equity conversion.

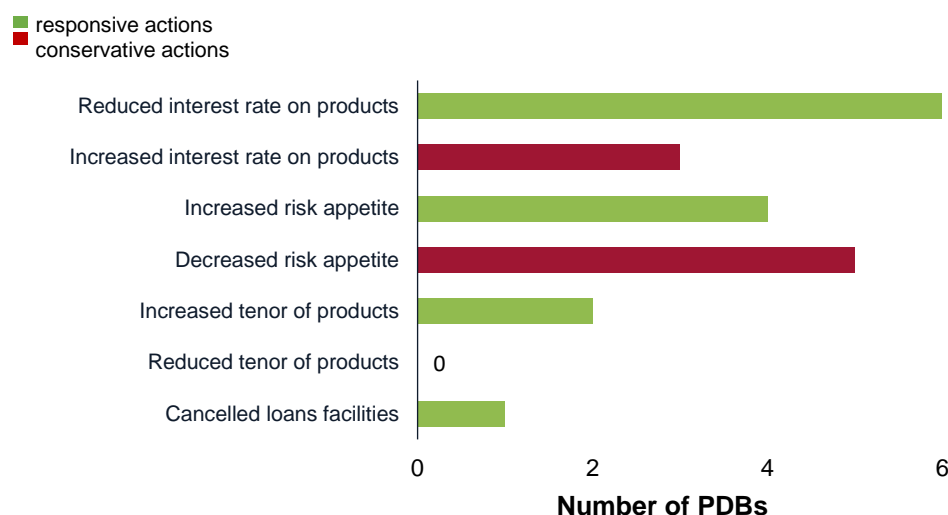
For wholesale PDBs such as the Development Bank of Nigeria (DBN), debt relief was channelled through financial intermediaries. Since the shock of Covid-19 led to a credit crunch in its client banks, DBN issued targeted moratoriums, intended to be passed onto MSMEs and to encourage the resumption of lending in this sector (discussed further in Box 3).

These moratoriums were between six months to a year and were intended as short- to medium-term responses. Some interviewees suggested that liquidity and/or debt distress were less pervasive in the second year of the pandemic as economies reopened, though others had had to extend their moratoriums beyond the original six months, or eventually restructure, as the impacts of Covid-19 wore on.

Our interviews also highlighted that central banks and regulators played a role in enabling PDBs to provide debt relief, often through the relaxation of provisioning rules for non-performing loans (NPLs), which was the case for Malawi, Ghana and Nigeria (see Section 4.3). Although moratoriums affected net interest margins, they did not appear to impact the financial soundness of our sample banks: we find that the asset quality of the gross loan portfolios of many PDBs proved to be quite resilient, with no noticeable increase in NPL ratios (see Section 4.3).

Under half of our sample PDBs stated that they also made changes to their terms and conditions to existing products and services. However, when breaking down these changes, there is a bifurcation between banks that appeared to have a higher risk appetite and took a *responsive* approach (green in Figure 5), and banks that were more risk-averse, with a contractionary or *restrictive* approach (red in Figure 5).

Figure 5 Changes to PDB product terms and conditions



Source: ODI-AADFI survey of African PDBs

Survey responses indicate that slightly more banks in our sample became more *conservative* in their risk appetite. Despite this, far more *reduced* interest rates on existing products as a response than *increased* interest rates, indicating a common move towards counter-cyclical actions towards existing clients.

Interviews shed some light on these responses. For the Agricultural Finance Corporation (AFC) Kenya, the financial stability of the bank and the need to counter moral hazard issues prompted an increase in interest rates, although the bank still ensured products were competitively priced compared to market rates (see Box 2). While this can be seen as a conservative or *restrictive* action, the bank also took other *proactive* strategies, notably expanding its lines of business to include wholesale lending, which has led to an overall significant increase in the loan book.

Box 2 Agricultural Finance Corporation

AFC was formed in 1963 as a subsidiary of the former Land and Agricultural Bank. Six years later it was incorporated as a DFI with branches across Kenya. Since then, AFC, wholly owned by the Kenyan government, has sought to support the development of agriculture and agricultural industries by making loans and providing managerial and technical assistance to its clients. Its sector-focused mandate and comprehensive portfolio across the entire agricultural value chain, end-to-end, cemented AFC as the leading government credit institution focused on expanding credit for the sole purpose of developing the agriculture sector.

Impacts of Covid-19

Almost a year before Kenya witnessed its first reported case of Covid-19, the country experienced a drought which impacted the ability of AFC clients to service debts to the bank. This negatively impacted AFC's loan book, drastically increasing its share of NPLs. By 2020, AFC had improved its financial position by writing off poorly performing loans and received a capital injection from the government to enable it to do so.

This government support alongside a new focus on quality lending and an increase in collections enabled AFC to restore its financial health and increase its gross loan portfolio. The impact of the drought prompted the bank to formalise a funding diversification strategy to ensure financial sustainability and reduce reliance on a few funding sources. The bank had recently secured funding from the African Development Bank (AfDB), which was due to be disbursed in 2021 but at the time of writing had not yet been disbursed. Prior to 2020, AFC also benefited from World Bank loans that were later converted into equity.

Response to Covid-19 and the creation of a wholesale window

AFC applied some form of debt relief to approximately 10% of its gross loan during the pandemic. Like many other PDBs, AFC provided moratoriums to its clients. It also established the duration of the relief based on where in the agricultural value chains its borrowers were operating. For example, borrowers with businesses in processing and storage were granted a moratorium of six months, while those involved in livestock production received an average of three months. In addition, AFC rescheduled loans to provide longer repayment periods and refinanced agricultural plants across the country to ensure they could continue their business.

Prior to the pandemic, the low interest rate charged by AFC limited the bank's ability to expand its loan book. Following the drought, the transfers from the National Treasury and government assistance in

repayment of loans written off to AFC had generated concerns over issues of moral hazard tied to its direct lending operations.

As the bank faced increasing numbers of borrowers unable to repay and an increase in NPLs, it shifted its strategy. This led to three major reforms. First, AFC began to refocus its lending away from MSMEs towards larger to medium-sized farmers and SMEs to lower its NPLs, on the assumption that larger, more established borrowers would more reliably fulfil their debt obligations. Second, it sought to re-price its lending to bring it more into line with market rates, while maintaining a discount to further financial access. Most importantly, AFC added a new wholesale lending window.

After taking necessary steps to stabilise its financial position, AFC began developing a wholesale lending model to de-risk and catalyse private sector agricultural financing. This reform led to a 10% increase in AFC's gross loan portfolio book by the end of the 2021 financial year as 18% of its portfolio consisted of wholesale lending. To explore the full potential of this model, AFC aims to deploy wholesale products, including credit guarantees, asset-backed products that aggregate agricultural loans and reinsurance products, to a tailored private sector clientele. The bank will continue to seek to enhance government collaboration to support its wholesale window.

4.2.2 Expansion of services and lending

Evidence suggests most banks played a counter-cyclical and *proactive* role in the economy through expanding lending beyond existing clients: 85% of the PDBs surveyed noted that they had expanded their services either 'significantly' or 'somewhat' beyond existing clients. This is supported by the financial metric analysis, which finds that most of our sample PDBs (where data was available) increased their lending in response to Covid-19, with 11 of 16 PDBs expanding their gross loan portfolios (GLPs).

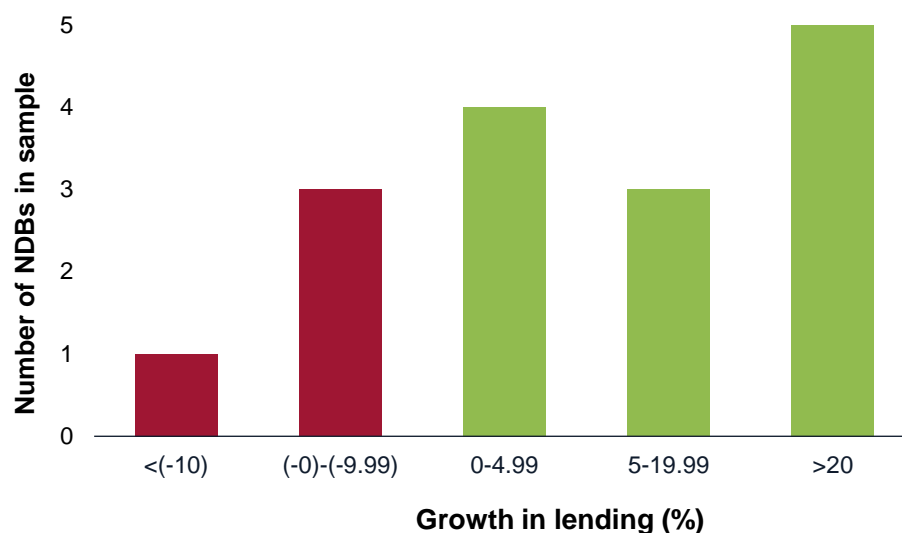
In some cases this expansion is significant: five PDBs expanded their GLPs by over 20% in 2020 compared to 2019 (Figure 6).⁶ For example, DBN significantly accelerated the expansion of its GLP by the end of 2020 through the proactive development of new loan products. New initiatives included the Interest Drawback Programme (Box 3), as well as the development of a new long-term finance product which could meet the Tier 2 Capital requirements for commercial banks to support their lending to MSMEs.⁷ This expansion was also in part due to DBN being a relatively new bank,

⁶ For example, the Banque Nationale de Développement Economique of Burundi (BNDE), the Banque Nationale d'Investissement of Côte d'Ivoire (BNI), the Development Bank of Nigeria (DBN) and the Export Development Fund of Malawi (EDF).

⁷ This refers to the supplementary layer of a bank's capital structure, required under the Basel Accords. It is usually composed of items such as revaluation reserves, general provisions, hybrid instruments and subordinated bank debts, and is generally considered less secure than Tier 1 capital.

still in growth mode, and freshly capitalised, which allowed it to expand rapidly.

Figure 6 Sample PDB gross loan portfolio growth, 2019–2020



Note: CDC-CI has been excluded for lack of comprehensive data. The sample includes MAIIC, which only started lending in 2020, so its growth equates to 100%.

Source: Authors' calculations based on ODI dataset

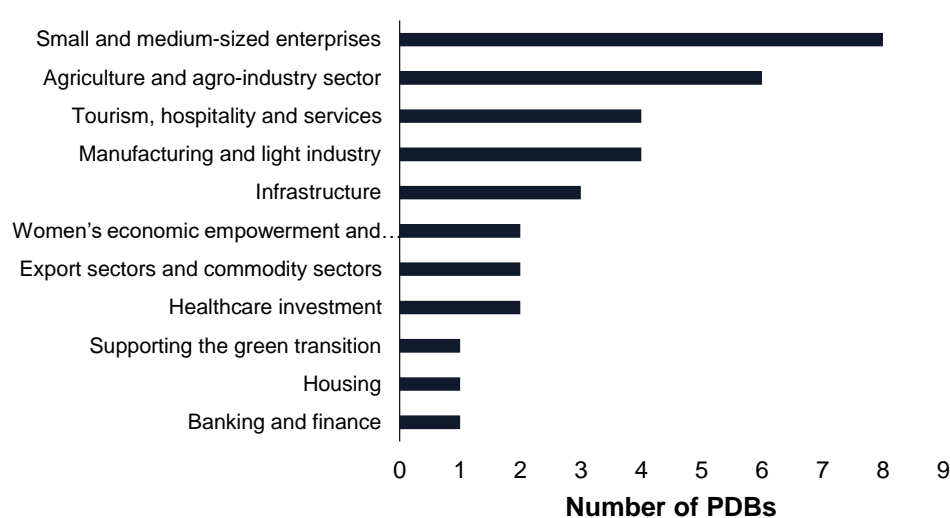
Our detailed financial metric analysis also explored the relationship between GLP growth and internal financial variables including changes in total assets; solvency (e.g. interest coverage ratio); profitability (e.g. net interest margin and return on assets); and gearing (e.g. debt to equity ratio). We found no strong correlations. This would suggest that, for many PDBs in good financial health, the external economic context – the Covid-19 shock – was the primary factor driving the growth of the GLP. Several interviewees highlighted the impact that these external realities had on demand for new loans.

Of the minority of banks surveyed that restricted lending to existing clients or reduced lending, this was often due to extreme financial constraints – for example, in the case of NIB, this was a result of poor financial health entering the crisis due to high NPL issues associated with legacy construction loans. For DBS, its GLP contracted significantly in 2020 due to a freeze in lending. This was necessitated by liquidity issues, and a huge loss of reserves, owing to its high exposure to the tourism sector, where clients were struggling with debt service. This *restrictive* approach was thus seen as a necessity, rather than a choice.

4.2.3 Financial innovations and other products

Alongside debt relief, over a third of banks surveyed took *proactive* approaches in creating new financial products (i.e. lending or equity instruments) targeting the impacts of Covid-19. Our survey showed these interventions were concentrated in a small number of sectors, primarily SMEs, agriculture, manufacturing and tourism and hospitality (Figure 7).

Figure 7 Targeted sectors of new financial products



Source: ODI-AADFI survey of African PDBs

An interesting example of such innovation was the DBN's use of interest rebates to incentivise new lending. The interest rebate product only applied to *new* loans and was targeted to key sectors, including green, manufacturing and exports, and focused on women and youth. The rebate also applied to non-traditional institutions including fintech and microfinance (see Box 3).

Another example from interviews was the Covid-19 Credits programme from the Société Tunisienne de Banque (STB). This was designed by the central bank following a market analysis survey by the Tunisian Professional Association of Banks and Financial Institutions measuring the impact of the pandemic on borrowers. Two types of Covid-19 credits were developed by the central bank and then issued by STB.

Credit Type 1 supported STB to finance customers with new loans totalling \$137 million (438 million dinar), two-thirds of which were guaranteed through the Tunisian guarantee company SOTUGAR. This was backed by the central bank via a state guarantee for new credits worth \$469 million (1,500 million dinar). Credit Type 2 entailed the mobilisation of \$56 million in advances on current accounts, helping over 1,500 companies to meet cash flow needs tied to

operating expenses. The Bank also deferred credit maturities for an amount totalling \$128 million (412 million dinar), following direction from the central bank to defer loan repayments for the tourism sector up to September 2021.

4.2.4 Non-financial services and capacity-building

A final and less recognised area of help provided by PDBs was in non-financial, technical support to clients. Just over half of surveyed banks noted they had provided non-financial support to clients.

This took multiple forms, including technical assistance and support to MSME clients in areas such as project preparation and financial advisory roles, and other forms of business mentoring. Others launched targeted capacity-building initiatives, such as digital platforms for non-oil exporters (e.g. the Nigeria Export Import Bank – NEXIM) and a farmers' and agribusiness school (the Malawi Agricultural and Industrial Investment Corporation – MAIIC).

DBN introduced a Service Ambassadors programme, comprising a network of contacts embedded as employees across its client base of banks and financial institutions. They served, as one interviewee put it, as 'eyes' for DBN to help target lending to businesses that support women, youth and SMEs (Box 3).

Box 3 Development Bank of Nigeria

The Development Bank of Nigeria (DBN) was created in 2017 by the Federal Government, with the African Development Bank and the European Investment Bank. Its mandate focuses on alleviating the financing constraints facing Nigerian MSMEs. The DBN is a wholesale DFI funded from both local and international capital markets and on-lends through Participating Financial Institutions (PFIs) to MSMEs, which include commercial, mortgage and microfinance banks licensed with the Central Bank of Nigeria. This wholesale structure means that PFIs bear the credit risk of end-borrowers directly, while DBN provides wholesale term funding and risk-sharing facilities.

Impacts of Covid-19

Following the outbreak of the pandemic, DBN largely paused its lending operations, issuing a limited amount of new loans. This temporary halt, combined with the bank's provision of moratoriums to its clients, led to a significant negative impact on profits in 2020, with a slight recovery in 2021. However, the bank's profitability has remained resilient as DBN was able to slowly increase its loan portfolio via its *Interest Drawback Programme* (IDP, discussed below), which led to large loan growth in the final months of 2020. By the end of the year, the bank was supporting over 200,000 MSMEs

by disbursing funding worth \$1.15 billion, while recording a return on equity of approximately 10%. The bank has recorded no non-performing loans over this period given that its wholesale structure ensures that PFIs record loan performance.

Responses to Covid-19 and rebates to priority sectors

In line with the government's pandemic recovery and environmental sustainability plan, DBN shifted its strategy to focus increasingly on local content to help improve the country's current account balance in light of the effects of the Ukraine war. Priority sectors include green transition industries, manufacturing, health and agriculture. There has been increased focus on the provision of financing to women and youth.

Like many DFIs, DBN provided a debt moratorium in 2020 to its clients on both interest and principal, extending to a maximum of six months and around 60% of the bank's PFI clients. Moratoriums averaged around three months, allowing microfinance institutions to extend debt relief to their MSME end-borrowers.

Second, to operationalise its strategic shift, the bank introduced incentives to encourage PFIs to issue new loans to new priority sectors. Under the IDP, the DBN provides rebates on PFIs' loans to MSMEs engaged in sustainability sectors such as renewable energy and waste management. DBN offered all PFIs extending new loans to the bank's priority sectors a rebate via a 15% interest drawback.

The new programme was designed to maximise financial accessibility for MSMEs by creating opportunities for new lending while ensuring that loans would be channelled to sectors that DBN and the government identified as having high impact. It also allowed DBN to test a new incentive structure that expanded the bank's impact and could be used as a template to target new priority sectors in the future.

To maximise the impact of its rebate programme, DBN also launched a new *Service Ambassador Programme*, whereby employees of PFIs were tasked with increasing loan disbursement to MSMEs while identifying new solutions and objectives to increase the financial access of their PFI for key groups (e.g. women and youth) and priority sectors. In return, financial incentives were provided to Ambassadors directly for their work (rewards were attached to specific key performance indicators outlined by DBN at the start of the programme).

Following these efforts, DBN became the first DFI in Nigeria to receive an Accreditation Certificate of Acceptance in line with Sustainability Standards and Certification Initiatives (SSCI) by the World Development Finance Forum in Germany.

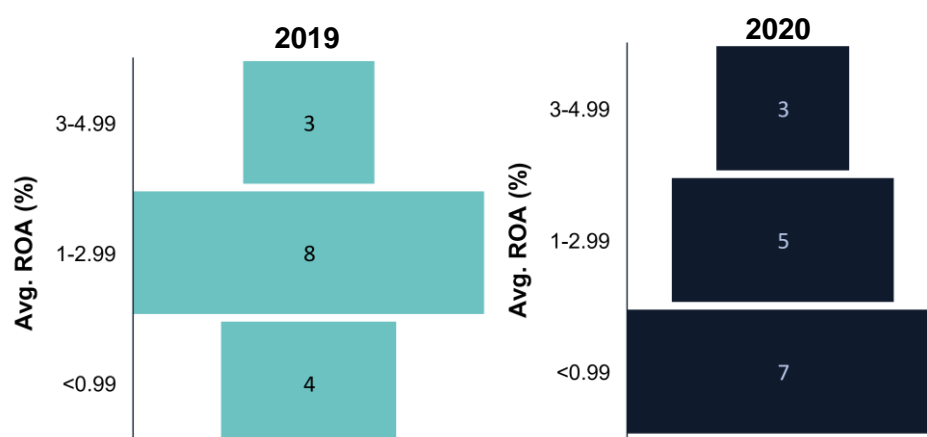
4.3 Financial impacts of the Covid-19 shock on African PDB profitability and asset quality

The impact of the Covid-19 shock on the financial performance and health of PDBs varied and was influenced internally by the financial position of the bank entering Covid-19, and externally by the sectoral focus of the bank, the specificities of the wider economy and other external factors such as directives from the central bank/regulator and/or central government.

Our financial metric analysis shows that the profitability of many of the studied banks was adversely affected, primarily due to squeezes on the net interest margin, rather than significant impairments on loans, indicating that changes to profitability and returns were due more to the counter-cyclical provisions of banks via debt relief, and their higher borrowing costs, than to any significant deterioration in asset quality, which has remained notably resilient.

The sample of PDBs analysed showed low levels of profitability, as measured by returns on assets (ROA), and Covid-19 adversely impacted profitability in 2020 (Figure 8). Ten out of 15 sample PDBs saw their ROA decrease in 2020, with a few taking a big hit to their profitability. Four PDBs were able to increase their ROA, but in general this increase was small, at less than 1%. Very few banks were able to increase profitability by more than 1%.

Figure 8 Sample African PDB return on assets



Note: MAIIC and CDC-CI have been excluded due to lack of data.

Source: Authors' calculations based on ODI dataset

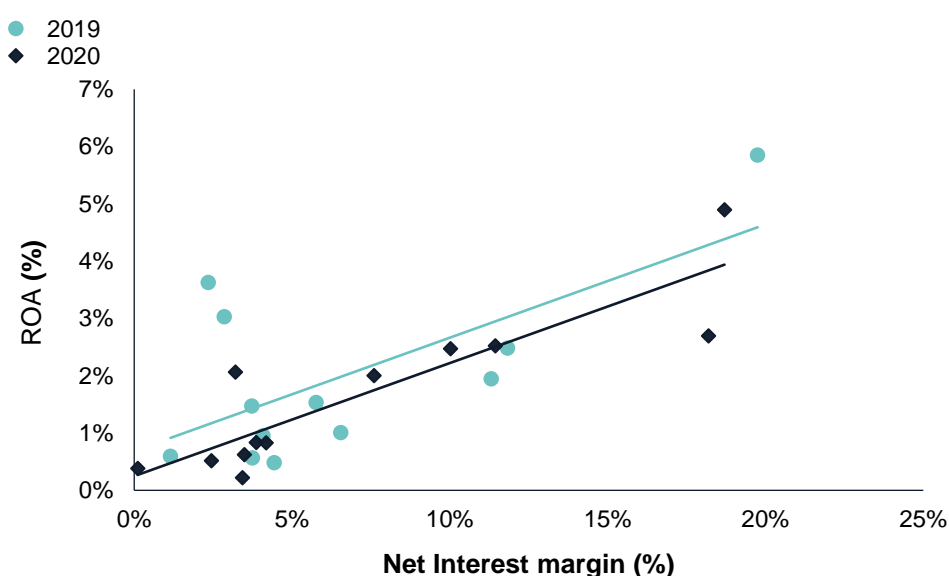
While profitability is not and should not be the priority of PDBs given their development mandate, the ROA metric illustrates that PDBs have little room to scale their operations from retained profits. Furthermore, consistent loss-making undermines the financial health of a PDB and affects its ability to increase its GLP and attract new capital. The study noted three PDBs carrying large accumulated

losses on their balance sheets. These financial constraints are significant barriers to *responsive* or *proactive* actions.

Three general areas affect the profitability of a PDB whose main business is lending: net interest margin, impairment of assets and the general cost base. For many sample PDBs, an analysis of financial metrics suggests that decreases in net interest margin and/or increases in the cost base affected overall profitability more than asset impairment. Interviews revealed that net interest margins were squeezed due to debt relief on interest payments and/or increased costs of borrowing due to tight market conditions and/or exchange rate depreciation, which affected the cost of hard currency funding. On the cost front, several PDBs highlighted that they had seen their cost base increase due to increased IT costs associated with remote working and PPE.

As expected, there is a positive correlation between net interest margin and ROA (Figure 9), which is much stronger in 2020. Although the underlying relationship did not change in 2020, we do see a squeeze on net interest margins which has impacted ROA in 2020 compared to 2019.

Figure 9 The net interest margin squeeze in 2020



Note: Two outliers have been omitted. MAIIC, CEDA, and CDC-CI have been excluded because of lack of data.

Source: Authors' calculations based on ODI dataset

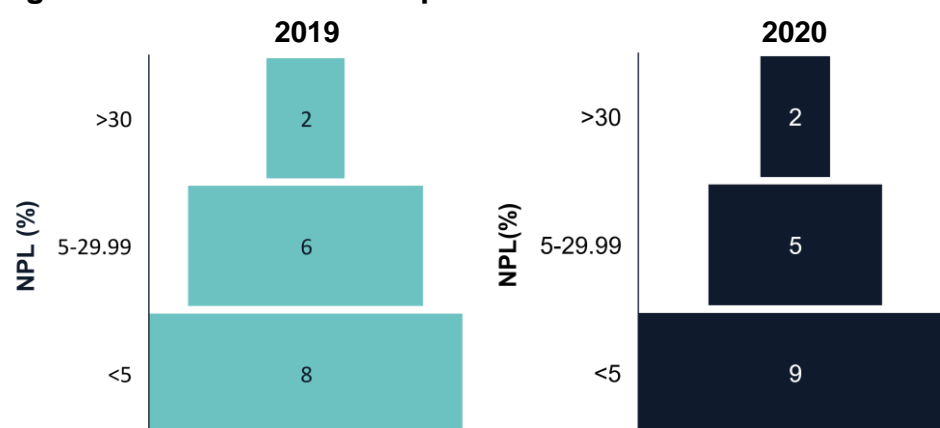
Contrary to expectations, the quality of the loan books of our sample PDBs proved resilient in 2020. Asset quality (as measured by NPL ratios) improved in 2020 (Figure 10). Nine PDBs saw a decrease in their NPL ratios – some, including AFC, significantly so (Box 2).

PDBs whose asset quality improved in 2020 also saw an improvement in their return on assets. We also note that several

central banks relaxed NPL provisioning requirements (discussed in Box 5). Five PDBs saw an increase in their NPL ratios, significantly so in the case of MAIIC and TIB. However, in some instances this deterioration in asset quality was driven not by a deterioration in credit risk of borrowers per se (e.g. non-payment), but the application of more stringent assumptions in risk modelling about the impact of Covid-19 on sectors and economies, and consequent additional risk overlays.

Recognising the long-term and negative structural impacts of high NPL ratios for banks' operations and access to finance, interviews with several PDBs highlighted structural reforms which seek to improve their asset quality and strengthen internal processes around risk management (Box 4).

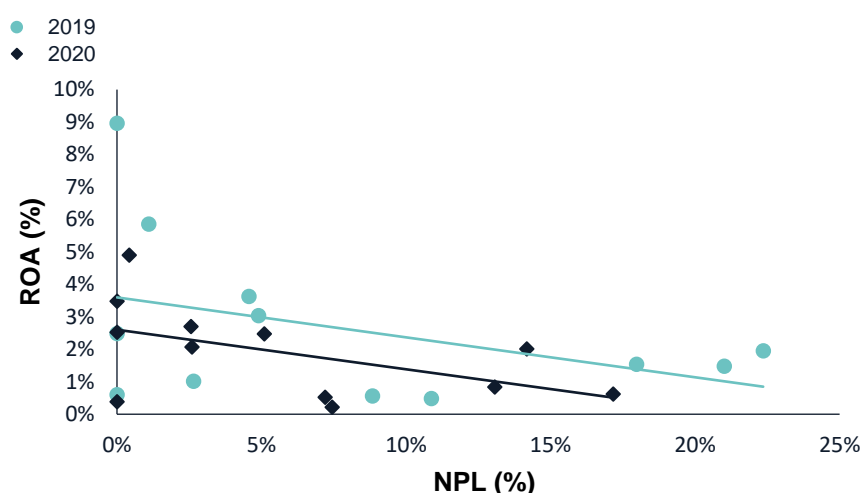
Figure 10 NPL ratios of sample PDBs



Note: CDC-CI has been excluded because of lack of data.

Source: Authors' calculations based on ODI dataset

As one would expect, we see a negative relationship between the return on assets and NPL ratios. However, in 2020, lower levels of NPLs are associated with lower levels of returns on assets, implying that other factors were affecting profitability in 2020 (Figure 11), such as the net interest margin discussed above.

Figure 11 Relationship between ROA and NPLs 2019 vs. 2020

Note: Two outliers have been omitted. MAIIC, CEDA and CDC-CI have been excluded because of lack of data

Source: Authors' calculations based on ODI dataset

Box 4 How Covid-19 propelled internal PDB reform

Prior to Covid-19, several PDBs were already facing worrying NPL levels, encouraging them to craft reforms to improve their financial health well before the crisis began. The timing of the crisis added urgency to mobilise and accelerate these reform efforts. Several notable examples are described below.

Société Tunisienne de Banque

In 2016 Moody's estimated that STB's NPLs represented 118% of equity, largely due to heavy exposure to the tourism sector. That same year STB, alongside government partners, started drafting a new risk policy and strategy with the help of the Central Bank. In support of these initiatives, the government invested 110 million DT into STB as part of a wider PDB restructuring programme.

The programme, which began prior to Covid-19, meant that throughout the pandemic STB placed a strong focus on improving asset quality, reducing its exposure to tourism and expanding its portfolio towards clients in the manufacturing, agricultural, SME and export commodity sectors. In addition to an improved selection process for new loans and a renewed credit risk assessment system, STB introduced mechanisms to deal with impaired loans (e.g. consolidation of amicable, judicial and transactional collection efforts and a write-off for certain impaired loans). By March 2021 STB had achieved the majority of the objectives outlined in its original restructuring plan, leading to a 64% increase in the bank's lending between 2016 and 2021. In 2019–2020, the bank maintained a positive 14% increase in the size of its loan book.

ECOWAS Bank for Investment and Development

In 2020 and 2021, the EBID went through a series of reforms to reduce the level of legacy NPLs. This coincided with the recruitment of new senior managers, many of whom had a commercial banking background. This new cohort drove through risk management reform initiatives, including the introduction of best practices in risk management such as the first and second line of defence model,⁸ and the implementation of a new independent risk assessment structure. The bank's credit rating has since improved from a B- to B stable outlook, indicating that improvements to risk management and liquidity have improved credibility and access to external funding. Better financial management has also enabled an increase in activity, with a rapid increase in lending in 2021.

National Investment Bank, Ghana

Facing an issue with asset quality, the NIB has reformed its governance structure, with increased representation of sectoral experts on the Board and a new management team. This has helped to balance government control with the need for experienced bankers to manage the bank well. NIB has also developed a range of new initiatives to improve governance and management and is working with the consultancy firm Oliver Wyman to promote the transition from a commercial bank to an industrial development bank.

Beyond internal reforms, NIB has also made changes to its external funding model. A longstanding lack of capital and funding from MDBs, RDBs and other DFIs meant that NIB was overly reliant on government finance. To ease this, legislation was relaxed to allow the bank to take deposits to help fund operations. However, the cost of capital has been very high, with a 20% interest rate payable on fixed-term deposits in 2019. Due to base rate increases announced by the Bank of Ghana, the cost of capital has further increased compared to 2019 levels. With the aim of reducing its weighted average cost of capital to between 12% and 14%, the bank is now focused on securing access to cheaper funding (including from MDBs, RDBs and DFIs).

Tanzania Investment Bank

Entering the crisis, TIB faced three financial challenges: capital constraints and a reliance on short-term borrowing resulting in a maturity mismatch on its balance sheet; a very high NPL ratio (in part due to adoption of Basel 3); and significant accumulated losses on the balance sheet. This was compounded by a challenging political and policy environment, which impacted private markets and the ability of TIB to collect some loan repayments. Other issues have

⁸ See <https://www.ii.org.uk/policy-and-research/position-papers/the-three-lines-of-defence/>

been exacerbated by Covid-19. For example, NPLs increased during the pandemic due to loan restructuring and debt relief, which rendered the reform programme TIB embarked on prior to 2020 even more urgent.

To address its funding base and reliance on short-term financing, TIB has been in discussion with the government for a new capital injection and has been included in the national budget, but this financing promise has not yet been forthcoming. TIB is thus actively seeking support from DFIs and international partners. However, its high NPL ratio and the government's inability to provide a guarantee to the bank has limited TIB's access to affordable capital sources. TIB has been assessing both the possibility of converting deposits by institutional investors into equity, and issuing a bond. The bank is also discussing a new scheme with the government which would require revenue-generating state-owned enterprises to bank with TIB, providing additional deposit funding and liquidity. This would help build confidence in the bank and demonstrate government support.

4.4 Institutional responses and enabling environment

4.4.1 Government engagement and support

PDBs considered themselves integral parts of their governments' response to Covid-19, and the majority of our survey respondents saw themselves as 'well-integrated' into a wider government strategy, with just under half of surveyed PDBs saying they 'strongly agree' with the statement.

Examples of this came through in interviews, particularly with newer banks such as MAIIC and DBN, which were created by their governments in the last 5–10 years with a clearer and sector-targeted mandate (respectively, tourism and SMEs) that were strategic priorities for the government. Responsive PDB initiatives such as moratoriums on debt relief were in many cases mandated by the government as part of national relief plans.

Some PDBs noted their advisory role to the government. TIB, for example, helped to shape priorities in the Tunisian government's 2022 and 2023 budget, and supported the government in negotiating and structuring infrastructure projects. EBID and STB conducted studies of the impacts of Covid-19 on the economy and for client sectors, which informed their response to Covid-19: for the former, the targeting of the tourism and hospitality sector; for the latter, the creation of the Covid Credits STB product. In a few cases, such as TIB, the bank did not manage government-allocated funds or have access to the central bank's rescue budget, as this required meeting both the government's NPL criteria and reform demands regarding internal restructuring.

Despite strong strategic links perceived by many PDBs, very few banks actually received new finance from government bodies or shareholders. Our survey recorded only two banks that had received additional financial support in response to Covid-19 in 2020, while three received additional funds in 2021. The financial analysis shows that few banks received additional capital injections, and borrowing from private sources was far more common than from the international and national public sector (see Section 4.3).

Some notable support from governments included the case of DBS, which obtained a credit line to support capital repayments to external creditors. This was in two tranches of 50 million and 60 million rupees over two years and would be repaid to the government over a 3–5-year period. MAIIC accessed funds received by the Malawian government from the World Bank Financial Inclusion and Entrepreneurship Scaling project (Box 6). However, most banks did not receive new government funds and appear to have relied on internal financial reallocation and external private borrowing in some cases.

4.4.2 The enabling role of central banks in supporting PDB counter-cyclical responses

Central banks across Africa played a critical role, as regulators and lenders, for some of the banks we interviewed, specifically ensuring that their banking sectors remained liquid and well capitalised (Cantú et al., 2021). This section details how African central banks also implemented monetary reforms in tandem with fiscal authorities to mitigate negative impacts on the banking sector.

The different policy options pursued by each African central bank tended to reflect country-specific factors (Aguilar and Cantú, 2020), and varied widely in the nature and depth of impact. In turn, the extent to which central bank interventions had a direct effect on how African PDBs were able to respond also varied.

Of the central banks analysed, almost all issued some form of debt relief framework and moratorium to the banking sector, which in turn allowed PDBs within their jurisdictions to extend this same support to their own clients. This means that the extent of relief and length of moratorium provided by PDBs to their borrowers was often mandated by, and highly contingent upon, external central bank debt relief frameworks, as well as the financial resilience of banks going into the pandemic.

Realising the stress points afflicting the banking sector, including high NPLs and structural problems that limited the shock-absorbing capacity of PDBs, several central banks engaged more actively with their banking sector and issued policies aimed at tackling the internal financial limitations of PDBs. These included liquidity injections and measures aimed at boosting profitability and limiting NPL increases. For example, central banks began relaxing accounting regulations

and provisioning requirements, as in Malawi, Ghana and the Seychelles (see Box 5).

Central Banks also provided finance to support PDBs' counter-cyclical responses. The Seychelles central bank was a source of concessional finance for the DBS, which was able to borrow at 0% and on-lend at a margin, which the bank used for targeted working capital support to the SME sector. In Tunisia, while the central bank did not change the provisioning around NPLs, it instead played an active regulatory and advisory role in 2020 to implement a reform programme with STB to resolve and improve the bank's NPL ratio and ensure it could reduce the stock of loans classified as NPLs over five years.

While these policies had a huge impact on the financial resilience of many banks, they fell short of addressing the structural economic realities stemming from the pandemic which were also limiting PDB capacity. In response, banks such as the Central Bank of Nigeria (CBN) played a more proactive role in incentivising PDBs to diversify their portfolios away from fragile industries like tourism and towards sectors such as green infrastructure.

Box 5 Central banks' Covid-19 response

Reserve Bank of Malawi

During the pandemic the Reserve Bank of Malawi introduced measures to ease liquidity constraints in the country's banking system. Most significantly for MAIIC, the Reserve Bank provided financial support to enable the bank to offer loan restructuring and a three-month moratorium on debt service to SMEs, while also providing provisioning relief that would be passed on to SME clients (IMF, 2020). This relief meant that the Reserve Bank itself made provisions for losses on loans which MAIIC had provided debt relief towards. This provisioning relief was initiated on top of an already generous timeline used to define PDBs' non-performing loans in Malawi, which sets out a distinction between the NPL timeline of commercial banks and that of PDBs. The latter are provided a more generous span of 181 days with lack of payment before a loan is categorised as non-performing, double the timeline offered to commercial entities (IMF, 2020).

This NPL definition and provisioning relief were paired with a Reserve Bank directive which allowed MAIIC to avoid counting on-moratorium loans as non-performing, in turn helping MAIIC's financial stability throughout the pandemic. The positive impacts of the directives were especially felt considering that, prior to Covid-19, MAIIC dealt with several clients in the tourism industry who suffered significant difficulties servicing their debt in 2020.

This package of proactive Central Bank policies helped MAIIC maintain a stable asset quality, allowing it to expand its loan book to support Malawi's recovery process.

Central Bank of Nigeria

In May and September 2020, the CBN cut the monetary policy rate by 100 basis points on both occasions. This 200-basis point reduction was paired with a sizeable liquidity expansion to non-commercial financial institutions, which significantly lowered the market yield for government securities, reducing the cost of capital in the market. Specifically relevant to DBN was the CBN's disbursement of over N3.5 trillion in 'intervention' loans to support DBN's Covid-19 response. Additional country-level measures which benefited DBN included (KPMG, 2020):

- A one-year extension of a moratorium on principal repayments for CBN intervention facilities.
- Granting regulatory forbearance to banks to restructure terms of facilities in affected sectors.
- The reduction of the interest rate on central bank loans to DBN for key sectors from 9% to 5%.
- On 15 March 2022, the CBN extended the 5% per annum interest rate on its development finance intervention funds for one more year through end-February 2023.

The CBN's reduction on rates for its intervention facilities created the space for DBN to extend its *interest drawback programme* (see Box 3). The emphasis that the CBN has placed on alleviating funding constraints to sectors considered instrumental to pandemic recovery has shaped DBN's operations, both by providing the bank with much-needed relief and by restructuring its sectoral priorities (discussed in Box 3).

Central Bank of West African States

In Côte d'Ivoire, the regional Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO)⁹ took clear steps to promote the liquidity demand stemming from the banking sector. A month after the first confirmed case of Covid-19, BCEAO announced a new allotment strategy with a fixed rate of 2.5%, which provided banks the ability to operate at 25 basis points below pre-crisis levels. For the Banque Nationale d'Investissement (BNI), this increased its net interest margin as it increased the rate on its products as the size of the clients it was attracting also increased.

⁹ The BCEAO is the common issuing institution of the member states of the West African Monetary Union, comprising eight states: Benin, Burkina Faso, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal and Togo

BCEAO incentivised banks and microfinance institutions (including studied PDBs in the region) to provide a three-month extension on payments to solvent customers with Covid-19-related repayment difficulties, by reassuring banking institutions that these extensions would not need to be classified as non-performing. BCEAO also promoted the use of electronic payments, which had a clear impact on the speed of BNI's digitalisation efforts.

Central Bank of Kenya

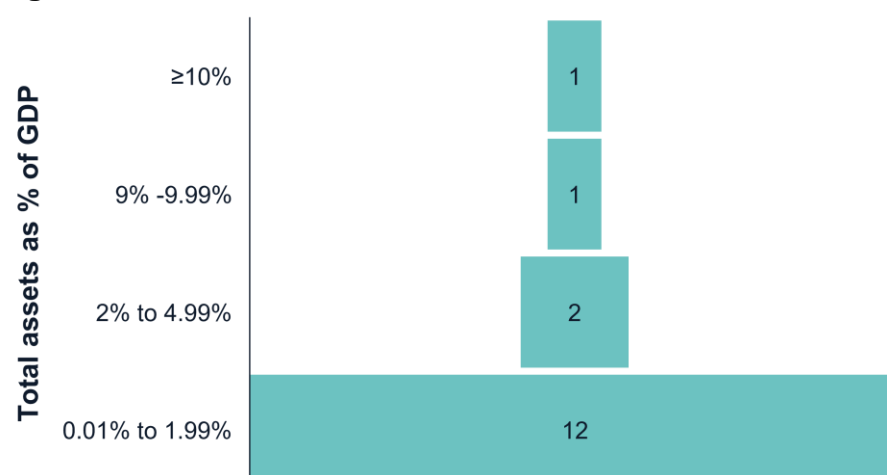
The Central Bank of Kenya (CBK) responded to the pandemic by relaxing measures on loan restructuring. For loans that were performing two fortnights prior to the first confirmed Covid-19 case in Kenya, the CBK granted flexibility in both loan classification and provisioning.

With the push from CBK to Kenyan financing institutions to extend flexibility on loan terms to borrowers, AFC was able to reschedule loans to provide longer repayment periods and refinanced agricultural plants across the country to ensure they could continue their business. As AFC shifted to wholesale banking in 2020, its end-borrowers also benefited from the CBK's waiver and reduction of charges on mobile transactions.

Although AFC has announced that it will not seek to be a deposit-taking institution (as this would require Central Bank approval, which has not been previously granted), it will partner with the CBK to build debt issuing capability as it seeks to issue commercial and green bonds.

4.4.3 Size and funding of sample African PDBs

While a majority of PDBs in our study took *responsive* or *proactive* counter-cyclical measures, their ability to make an impact in the economy depended heavily on their financial capacity and size. Our analysis of financial metrics shows that, with the exception of Groupe Crédit Agricole du Maroc (GCAM), which had a total asset-to-GDP ratio of 10.1%, most of our sample PDBs are very small in relation to country GDP (Figure 12), echoing previous studies (Attridge, Chen and Mbate, 2021).

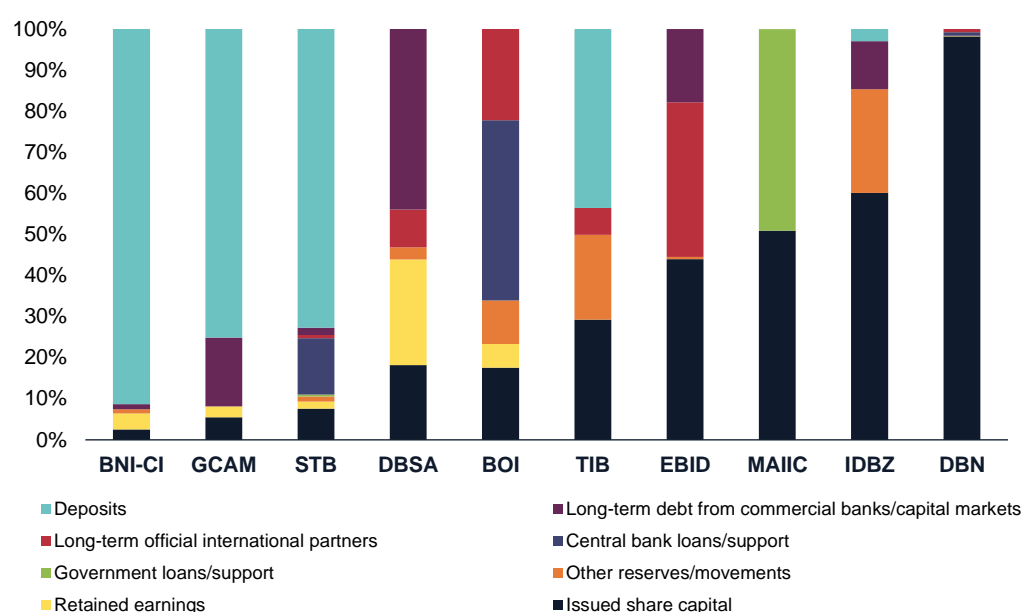
Figure 12 Size of African PDBs in 2019

Note: BDEGL has been excluded for lack of comprehensive data. All regional banks have been calculated using a weighted GDP average.

Source: Authors' calculations based on ODI dataset (for total assets of PDBs) and World Bank Development Indicators (for GDP)

In terms of the impact of the Covid-19 shock on PDB balance sheets, a mixed picture emerges. In 2020, seven out of 16 sample PDBs saw their total assets contract, while nine saw their total assets increase, some significantly so.

PDBs are essentially funded by equity (e.g. equity capital, retained earnings and other reserves, including revaluation reserves) and long-term borrowing (e.g. from the state, central banks, capital markets, commercial banks and international development partners). There is quite a degree of diversity in the funding structures of the 11 sample PDBs for which we have funding data, although most PDBs have low gearing levels (Figure 13). Seven PDBs (over half our sample) have loan facilities with international development partners, which for three PDBs represents a large percentage of their overall funding (e.g. over 20%). Very few sample PDBs are funded by state or central bank borrowing. Five PDBs are also funded by customer and/or business deposits, which are generally short-term.

Figure 13 Funding structure of sample African PDBs, 2019

Note: Reports were available for 11 of the 26 PDBs that completed the qualitative survey. Retained earnings have been omitted from calculations in all cases where they were negative in 2019 (e.g. TIB, EBID, MAIIC, IDBZ). All calculations in local currency units.
Source: Authors' calculations based on data on funding structure compiled by ODI from PDB annual financial statements.

In 2020, nine out of 11 sample PDBs saw their overall funding increase in 2020, while overall funding declined for two sample PDBs (Table 3).

Table 3 Sample African PDB funding growth or decline in 2020

Growth in overall funding	9
<i>Growth in both equity and borrowing</i>	<i>8</i>
<i>Growth in equity but decline in borrowing</i>	<i>1</i>
Decline in overall funding	2
<i>Growth in equity but larger decline in borrowing</i>	<i>2</i>

Note: The table represents 11 banks for which data was available. Data calculated in local currency.

Source: Authors' calculations based on data on funding structures compiled by ODI from PDB annual financial statements

All 11 banks saw growth in equity financing, but only in four cases was this due to new capital injections in 2020.¹⁰ The remainder was due to increases in retained earnings and/or other reserves. This is

¹⁰ BOI, BNI, EBID and IDBZ.

perhaps a reflection of the fiscal challenge facing many African states as, in most instances, with the exception of EBID,¹¹ these capital increases were the realisation of recapitalisation programmes envisaged before the onset of Covid-19. Some capital injections were quite large, as was the case of the BNI in Côte d'Ivoire, whose share capital almost doubled in February 2020.

Another interesting case is the long-term recapitalisation programme of the Infrastructure Development Bank of Zimbabwe (IDBZ), which predated Covid-19. As a strategic priority, IDBZ has engaged professional advisors to assist in enhancing the capital base. This included a six-fold capital injection (in local currency)¹² in 2020 from its shareholders; the bank is also in discussion with the government on a proposed scheme for land assets to be ceded to the bank to further strengthen its balance sheet. IDBZ also notes some challenges in accessing external funding from MDBs, RDBs and DFIs because of unresolved external debt arrears, and given the fiscal challenges facing the government, signals an intention to rely more on private funding. In the longer term the recapitalisation programme aims to increase its capitalisation to \$1 billion by 2030, including through the issuance of quasi-equity, long-term debt to institutional investors and equity placements with strategic partners.

In the case of Nigeria's Bank of Industry (BOI), the bank reclassified a 'deposit for shares' from a liability to equity in 2020. These funds were received from the Federal Government of Nigeria in 2018 as part of a wider government programme to restructure PDBs in Nigeria and were held as a liability on the balance sheet in 2018 and 2019. In 2020 BOI conducted a reassessment of these funds and concluded that they would not be refunded to the government, and so they were reclassified.

¹¹ For EBID, some member countries made capital arrears payments to support the bank during the crisis.

¹² In USD this was the equivalent of a 56% increase in its share capital.

Table 4 Sources of increased or decreased borrowing in 2020

Overall growth in borrowing	8
<i>Growth in deposits</i>	4
<i>Growth in private</i>	6
<i>Growth in international official</i>	3
<i>Growth in central bank support</i>	2
<i>Growth in government loans and support</i>	3
Overall decline in borrowing	3
<i>Decline in deposits</i>	0
<i>Decline in private</i>	1
<i>Decline in international official</i>	2
<i>Decline in central bank support</i>	1
<i>Decline in government loans and support</i>	0

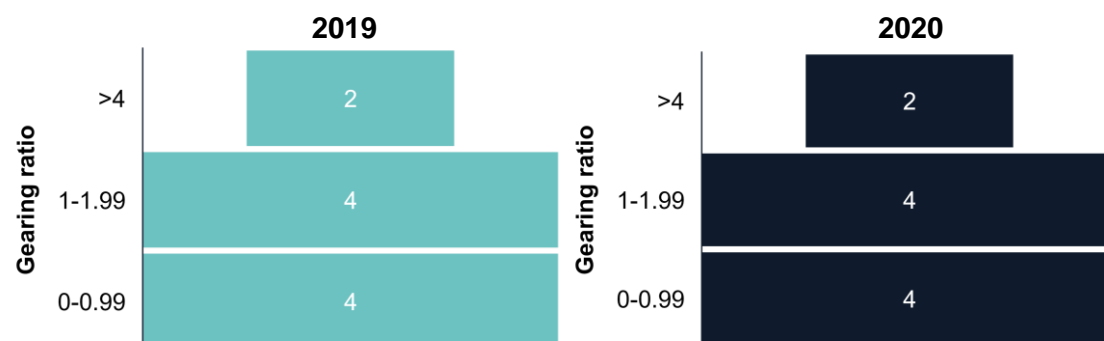
Note: The table above represents only 11 banks for where data was available. Data calculated in local currency.

Source: Authors' calculations based on data on funding structures compiled by ODI from PDB annual financial statements

In comparison to equity injection, more banks (eight out of 11 sampled PDBs) increased their borrowing, more often from private than public sources. However, overall levels of borrowing and consequent gearing (e.g. debt to equity ratio)¹³ remain very low and well below the AADFI Prudential Standards, Guidelines and Rating System (PSGRS) gearing standard of less than four (Figure 14).¹⁴ A gearing ratio of four or below is deemed to be conservative (Fitch Ratings, 2021). While this indicates sound financing structures in terms of risk, it also reflects the small capital base and limited ability of African PDBs to leverage their balance sheets. Access to affordable capital is highlighted by our sample PDBs as a major challenge.

¹³ Calculated as the ratio of long-term liabilities (liabilities with an original maturity over one year) to equity.

¹⁴ AADFI PSGRS are a set of financial standards developed by African DFIs to help them self-assess their governance, financial performance and operations against good practice. With respect to funding, a DFI is deemed to fully comply with good practice if the gearing ratio (e.g. debt to equity) is less than four. If the ratio is more than four but less than eight, the DFI partially complies with the standard. If above eight, the DFI does not comply.

Figure 14 Gearing ratios of sample African PDBs

Note: Seven PDBs have been excluded because of lack of data

Source: Authors' calculations based on ODI dataset

4.4.4 Access to external concessional finance

A minority of sample PDBs have links to international concessional financiers, including regional and multilateral development banks (Figure 13). For example, new banks such as the DBN have the EIB and AfDB as shareholders, while larger banks such as DBSA also noted their Green Climate Fund accreditation, giving them access to broader pools of finance. DBSA's first €200 million Green Bond in 2021 was also issued through a private placement with AFD to support climate projects aligned to South Africa's national development plan (Box 1).

In some cases, longstanding lines of credit from external development partners were important pools of resources, though our interviews found few examples of PDBs that had received Covid-specific emergency funding from these sources. In the case of DBS, because it had frozen lending in 2020, it was unable to access additional funding from EIB, despite holding an existing line of credit.

STB Tunisia was able to effectively leverage its government's bilateral relations to secure external funding. As part of the 2017 Investment Partnership between Germany and Tunisia, the Tunisian government received a grant of \$20 million to implement the Investment for Employment Facility, a relief loan which supported private sector employment during the pandemic. STB was one of seven partner institutions to receive funds through the facility.¹⁵ In turn, STB received \$300,000 to extend financing to MSMEs during Covid-19.

STB also received funds from other European sources. The Italian Development Cooperation Agency extended \$73 million, to finance imports of equipment, goods and services of Italian origin, and

¹⁵ The KfW pandemic relief loan is served through seven partner financial institutions (PFIs) spread over four banks: Amen Bank, Arab Tunisian Bank (ATB), Banque Nationale Agricole (BNA) and Société Tunisienne de Banque (STB).

financing of loans which have not been repaid for over 12 months. STB also has external funding agreements under similar conditions with the Spanish and French governments,¹⁶ of \$30 million and \$25 million respectively. MAIIC was able to leverage funds at favourable rates that the Malawian government had received from the World Bank, which it then passed on as concessional lending to its customers.

This again highlights the important mediating role of governments in supporting PDBs to access external finance, particularly from international development partners. TIB has struggled to access external finance, as all international partners require a government guarantee, which has been difficult for the government to provide. The implications for national debt also constrain the government and central bank from issuing guarantees. This affects the cost of funding and hence the interest rate charged on PDB loans, as funding from international capital markets is more costly.

Box 6 Malawi Agricultural, Industrial and Investment Corporation

Established in 2018, MAIIC formally began operations in 2020, partnering with microfinance institutions to bolster financial access for SMEs, farmers and start-ups to support development in Malawi. The institution, which operates under a Public Private Partnership (PPP) model, limits government shareholding to 20%. It is currently conducting a capital-raising campaign as of the date of this publication.

Impact of Covid-19

As a newly established institution, MAIIC only started lending in 2020, and much of its capital was invested in the money market. Although MAIIC had very few loans on its books, it nevertheless entered the pandemic with relatively high exposure. The first loan MAIIC awarded was to a hotel project which suffered badly from the impacts of the pandemic. The loan was disbursed in late February 2020, two months before the first Covid-19 case was officially reported in Malawi. The project was scheduled to be finalised by June 2020, using the revenues of an existing hotel owned by the borrower to service the debt on the MAIIC loan. However, the closure of the old hotel in spring 2020 due to Covid-19 meant the borrower entered into difficulties servicing their debt towards the new loan. MAIIC's small portfolio was quickly rendered unstable, especially as other clients also operated within the tourism sector.

¹⁶ While the terms of the Italian and Spanish funding agreement largely reflect one another, the support STB is receiving from the French government places a particular focus on SMEs.

Response to Covid-19

After witnessing the problems tied to the hotel project, MAIIC decided to offer debt relief and moratoriums on loan repayments to over 40% of its client portfolio.¹⁷ It also rescheduled debt and offered extended repayment periods. This was especially necessary given the cost of capital reached over 12% in 2020. Even though this pricing remains concessional compared to the standard market rate in Malawi, increases in MAIIC's rate of lending necessitated some form of debt relief for existing and solvent borrowers. While prior to Covid-19 the average tenor was six years, this was increased to 10 years, and in some cases up to 12 years. This generous debt relief would not have been possible without enabling directives from the Reserve Bank of Malawi (see also Box 5).

External support

In 2020, the government of Malawi received a loan from the World Bank via the Financial Inclusion and Entrepreneurship Scaling project, which was then extended to financial institutions. After applying for this funding from this facility via the Reserve Bank, MAIIC obtained a \$15 million loan allowing the bank to extend financing to its customers at a relatively concessional rate of 10%, compared to the standard 21% below market rate which MAIIC typically offers. The Trade and Development Bank (TDB) also provided a \$1 million grant facility to MAIIC, directed towards SMEs in the agriculture sector.

A package of proactive policies from the Reserve Bank (Box 5) bolstered MAIIC's financial stability. In addition to the impact of monetary policies at the national scale, MAIIC used its initial government capitalisation in money market operations to invest in Treasury Bills, securing its revenues and financial stability. By 2022, a combination of effective banking policies and good management had put MAIIC in a good position to increase its rate of lending as the country recovered from the pandemic.

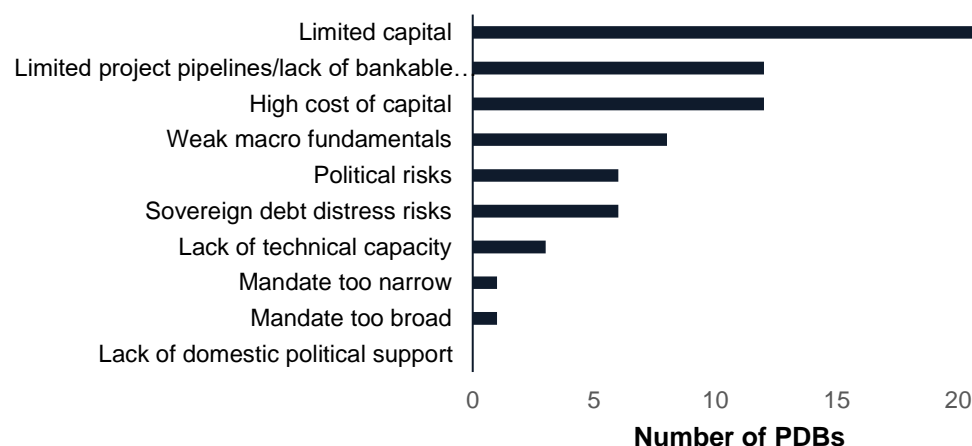
4.5 Challenges, constraints and future outlook

The primary constraint facing surveyed PDBs is *limited capital*, followed by limited project pipelines and the high cost of capital (Figure 15). Interviews with banks illustrated difficulties in accessing capital, and the limitations on what kind of capital is available. Accessing international finance via DFIs or private capital markets is a challenge for banks that are constrained by their financial performance, as high NPL ratios increase the cost of finance and

¹⁷ In the case of the hotel project, MAIIC initially provided a moratorium on capital payments and then extended this to interest payments as well.

reduce attractiveness. In the case of EBID, this was a strong motivator in reducing its NPL ratio and improving its asset quality (Box 4). In the case of MAIIC, respondents noted they had been able to secure favourable rates on loans from the World Bank, but ‘given choice and chance, what we would prefer is equity finance’.

Figure 15 Main challenges facing sample African PDBs

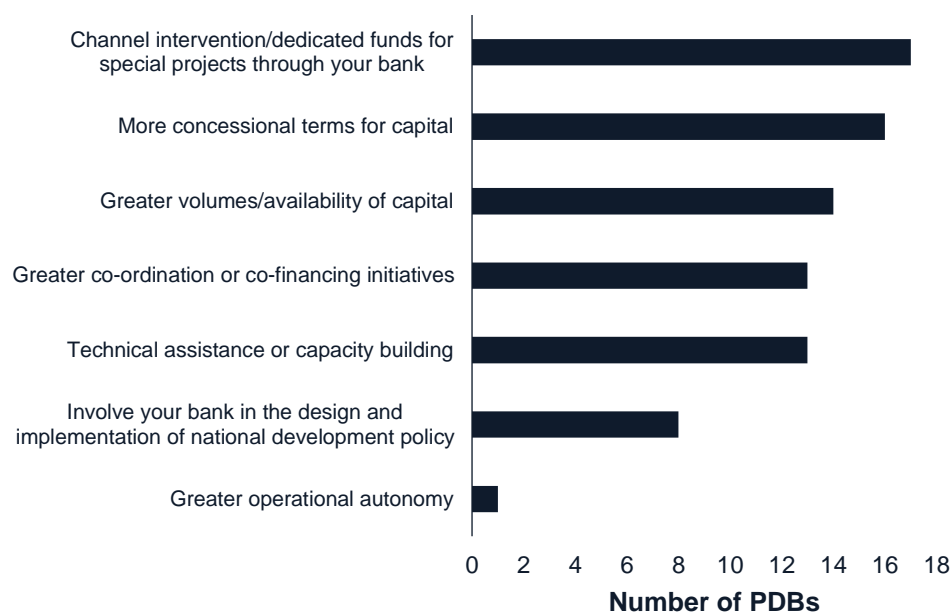


Source: ODI-AADFI survey of African PDBs

Project pipelines were a key challenge emphasised by interviews with TIB Tanzania: capital constraints were not the only factor for their operations, as even with capital resources and assets to disburse, ‘projects are not good’. The quality of the pipeline presents risks for banks if they choose to invest, but if they do not they face pressure to generate revenue and meet their mandate.

Understandably, when asked what support PDBs would like to see from shareholders and external partners, a desire for *greater availability* and more *concessional terms* of finance were high on the list (see Figure 16). Alongside this, there is a clear ambition among many banks to play an instrumental role within the wider economy, as a vehicle for dedicated funds and interventions, as well as greater coordination and opportunities for capacity-building.

Figure 16 What support would you need for your bank from government, shareholders or external partners?



Source: ODI-AADFI survey of African PDBs

While still navigating the recovery from Covid-19, African PDBs are also confronting new challenges: in the short term, the geopolitical shock of the Russia–Ukraine war; in the long term, the climate transition and its implications for African economies.

Interviews with banks highlighted the impact in the agriculture sector. Some banks, such as AFC, which supports Kenyan farmers and producers, noted that they had seen demand from clients for new financing as they had to halt exports to Russia, and required finance to support a segue into EU markets. Interviews with MAIIC noted the ‘huge’ impact on Malawi’s primarily agro-based economy, which is heavily reliant on imported fertiliser inputs. Respondents from MAIIC noted that, despite the impact of the crisis, ‘it can also be an opportunity in agricultural production’. One example is the provision of finance to a local company producing agricultural inputs, including organic fertiliser, as a first step in fostering greater domestic production in this sector.

Another area of opportunity – the green transition – was explicitly raised in interviews. While many of the banks stated that they had environmental, social and governance policies and were interested in advancing their activities in the green sector, few had an explicit climate strategy. A small number of PDBs interviewed, including DBSA and DBS, noted that climate and green finance was to be a key priority area going forward, particularly in financing renewable energy investment via international finance, and new technologies such as electric vehicles. However, banks also acknowledged the

challenges of the transition: respondents from EBID noted that a climate strategy was 'on the way', but also acknowledged the cost challenge, and that 'most governments are not there yet'.

5 Key findings and policy recommendations

This working paper has explored the role of African PDBs in the wake of the Covid-19 pandemic, and the impacts of the crisis on these institutions. The research did three things: first, it examined the proactive roles of African PDBs, the counter-cyclical measures taken, and the innovative responses of banks to an unprecedented crisis; second, it interrogated the financial impact of the pandemic and economic crisis on PDBs; and third, it explored how PDBs were utilised by shareholding governments in wider national strategies and pandemic responses, and how they have been supported in their public role.

5.1 Key findings

We highlight the following findings:

5.1.1 African PDBs have been adaptable and flexible in their operational and financial response to the unprecedented impacts of the Covid-19 pandemic

Although public institutions are often thought of as quite rigid and slow, African PDBs proved themselves to be the opposite. PDBs moved to new, flexible ways of remote working and adopted new technologies, resulting in greater efficiency. Many also simplified their approval, commitment and disbursement processes to quickly get finance to their clients.

PDBs were also highly adaptive in their strategic focus, with many shifting their sectors of operation to respond to the crisis, including interventions to support their country's health sector response and support MSMEs, the backbone of many African economies. Many banks have also gone further, expanding their client base to increase capital access in the economy. Some PDBs have also moved to address important future needs – with a strong focus on the green transition and infrastructure in several cases, which will have lasting economic benefits for their countries.

5.1.2 The vast majority of the African PDBs studied mounted a counter-cyclical response

Most of this has been in the form of short-term debt relief to existing clients and/or an expansion in lending. The necessity to respond also

drove innovation in lending in several PDBs. The degree of response and innovation, however, varied, with PDBs adopting a restricted, responsive or proactive response depending on institutional circumstance.

PDBs that were on a sound financial footing entering the crisis had more room to be responsive or proactive. PDBs whose financial health was weaker (in part due to previous governance issues) had more limited space to respond. For these PDBs, Covid-19 served to push them into further financial difficulty, leading to a much more *restricted* strategic response. However, some cases illustrate how the urgency of Covid-19 and the necessity to respond has accelerated or intensified much-needed reform efforts within some PDBs.

5.1.3 African PDBs proved themselves to be important crisis response actors considering the fiscal constraints of many African states

Although many African PDBs are small and not well capitalised, they managed to mount a counter-cyclical response at the micro level. This response was even more significant considering the fiscal constraints of many African governments, which limited the amount of government support that could be extended to businesses – in contrast to the support that many advanced economies were able to provide.

In a context of limited additional government and international public funding for African PDBs, these banks were nevertheless effective at leveraging external commercial borrowing and customer deposits, and/or used their reserves (such as retained earnings) to support their crisis response. However, overall gearing levels were relatively unchanged and remain very low. Lack of access to finance and high capital costs remain key constraints for a large proportion of the studied PDBs. These capital constraints limit their firepower and capacity to support recovery, as well as their longer-term ambitions to transition to low-carbon, climate-resilient economies.

5.1.4 Profitability of African PDBs was adversely affected in 2020 but recovered in 2021

Profitability levels are low overall and will constrain the ability of African PDBs to materially scale their future lending. Our analysis suggests that, for many PDBs, decreases in net interest margin and/or increased cost bases affected profitability more in 2020 than loan impairment due to servicing difficulties associated with the Covid-19 shock.

5.1.5 Central banks and regulators played an important role in supporting and enabling African PDBs to respond in a counter-cyclical manner

Central banks and regulators took several actions which supported the PDB response and eased the financial pressures on PDBs created by Covid-19. First, NPL classification and provisioning rules were relaxed, enabling PDBs to provide relief without affecting their NPL ratios. Second, central banks were a source of concessional finance for PDBs, which enabled PDBs to reduce the interest rates on new loans. Third, reductions in cash reserve requirements improved PDB liquidity and enhanced the capacity of PDBs to increase lending levels. Finally, for banks facing challenges of financial performance from their loan portfolio, government or central bank support for PDB reforms helped improve risk management structures and increase PDBs' autonomy and resilience.

5.2 Recommendations

African PDBs have proved their worth in the crisis and the experience documented in this study underscores the critical role that they can play, not only in building economic resilience to crises but also as active agents of industrial and economic policy. However, as documented in this study several issues currently inhibit the realisation of this potential. This study makes several recommendations to unlock their potential and makes the case for a much closer partnership with international institutions. Good governance and strong financial health will be critical in these endeavours.

5.2.1 Increase the capitalisation and access to affordable capital of African PDBs

Many African PDBs are too small to have a material economic impact. Many are insufficiently capitalised, which hinders their ability to respond rapidly in periods of crisis, and low levels of profitability and gearing constrain their ability to support recovery and the green transition in a meaningful way. PDBs, governments and international development partners should actively explore how the capital base of well-run PDBs can be expanded and how to increase PDB access to cheaper sources of external concessional capital, which will reduce the weighted average cost of capital of PDBs. Considering the current fiscal constraints of many African countries, some ideas worth exploring include:

- G20 countries have pledged to reallocate \$100 billion of a new \$650 billion issuance of IMF SDRs to support response and recovery efforts in the world's poorest and most vulnerable countries. Currently, most of these SDRs are expected to flow to countries through the PRGT and/or the RST. A dialogue should be opened to consider how African governments can make use of this reallocation to boost the capitalisation of well-

run PDBs and expand their access to concessional financing. This dialogue could also extend more broadly to explore how the excess SDRs of advanced economies could also be used in this endeavour.

- Many PDBs have low levels of leverage (for example, because central treasuries and/or regulators prohibit borrowing or certain kinds of borrowing and/or require PDBs to target low levels of gearing). Where feasible, PDBs should seek to increase their gearing ratios. Ratios of debt to equity of less than four are deemed fully compliant with the AADFI PSGRS standard and is deemed by Fitch to be a fairly conservative financial structure. Untapped sources of domestic savings could be explored, such as sovereign wealth funds and state-managed pension funds. Banks should seek to build their debt issuance capacity where local capital markets allow.
- While remaining cognisant of sovereign debt sustainability issues, African governments could consider issuing state guarantees for the borrowing of well-run PDBs. This can help ease access to international concessional finance and also domestic and international private finance, since the credit ratings of domestic PDBs are most often driven by the ability and willingness of the sovereign to support their PDB, should this be necessary (Fitch Ratings, 2021).
- Expand the equity base of PDBs by offering new shares (which could be different class, e.g. non-voting) to non-state actors such as private investors and/or MDBs, RDBs and other DFIs.
- Adopt innovative balance sheet management approaches, such as the use of insurance products – for example on callable capital to enhance credit ratings, or insurance to optimise the use of capital and meet regulatory limits.

5.2.2 Increase international support to build the capacity of PDBs

Many banks are seeking to expand their portfolio to play a larger role in economic transformation and supporting the green transition, as well as ensuring their own financial resilience. There is a key role for external partners in PDBs and global funds to support these ambitions through increased technical assistance, training and co-financing. This includes an enhanced external role for AADFI.

5.2.3 Build strong PDB governance frameworks and adopt best practices in risk management

The Covid-19 crisis and the necessity to respond has highlighted the importance of building well-governed, financially strong and resilient PDBs with strong risk management frameworks. This study has

shown how risk management practices are evolving. PDBs should ensure that their risk management develops in line with best practice. This will help strengthen and ensure the financial health of the bank.

African PDBs that do not yet assess their governance and financial performance against the AADFI PSGRS should aim to do so, and those that do should do so on a regular basis and should target annual improvement in areas where they are found to be partially or non-compliant. This will strengthen the governance and financial performance of African PDBs, which will help them in their quest to build their capital base and access more affordable concessional funding.

5.2.4 Ensure a supportive regulatory and policy environment

The experience of the studied PDBs has underscored the importance of tailored regulation of PDBs and central bank support.

Governments and central banks can play a key role in supporting PDBs to be an instrument of counter-cyclical policy in times of crisis, as well as an instrument of national industrial policy in times of growth, through finance and adequate capitalisation, and through confidence-building, utilising PDBs and their expertise to inform the direction of national policies and strategies.

The study has shown the benefits of regulatory distinction between PDBs and commercial banks, for example in the areas of liquidity and provisioning requirements. National governments and bank regulators should review national regulation to ensure that it supports and bolsters the development mandate of PDBs.

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Appendix 1

Table 5 List of African PDBs participating in the study

Institutions	Acronym	Country	Region	Mandate	Financial metric survey	Additional data collected
Citizen Entrepreneurial Development Agency	CEDA	Botswana	South	MSME	Yes	Yes
Banque Nationale de Développement Economique	BNDE	Burundi	East	GENDEV	Yes	Yes
Banque de Développement des Etats de l'Afrique Centrale	BDEAC	Congo (Rep.)	Central	GENDEV	No	No
Banque de Développement des Etats des Grands Lacs	BDEGL	Congo (DRC)	East	GENDEV	Yes	Yes
Agricultural Finance Corporation	AFC	Kenya	East	AGRI	Yes	Yes
Malawi Agricultural and Industrial Investment Corporation	MAIIC	Malawi	South	GENDEV	Yes	Yes
Export Development Fund	EDF	Malawi	South	EXIM	Yes	Yes
Development Bank of Nigeria	DBN	Nigeria	West	MSME	Yes	Yes
Bank of Industry Limited	BOI	Nigeria	West	GENDEV	No	Yes
Nigerian Export Import Bank	NEXIM	Nigeria	West	EXIM	No	No
Development Bank of Seychelles	DBS	Seychelles	East	GENDEV	Yes	Yes
Development Bank of Southern Africa	DBSA	South Africa	South	GENDEV	No	Yes
TIB Development Bank	TIB	Tanzania	East	GENDEV	Yes	Yes

ECOWAS Bank for Investment and Development	EBID	Togo	West	GENDEV	No	Yes
Banque Ouest Africaine de Développement	BOAD	Togo	West	GENDEV	No	No
Banque Maghrébine d'Investissement et de Commerce Extérieur	BMICE	Tunisia	North	GENDEV	No	No
Infrastructure Development Bank of Zimbabwe	IDBZ	Zimbabwe	South	GENDEV	No	Yes
Banque Nationale d'Investissement	BNI	Côte d'Ivoire	West	GENDEV	Yes	Yes
Caisse de Dépôts et de Consignations de la Côte d'Ivoire	CDC-CI	Côte d'Ivoire	West	GENDEV	Yes	Yes
National Investment Bank Ltd	NIB	Ghana	West	GENDEV	No	No
Tamwil El Fellah	GCAM	Morocco	North	AGRI	No	Yes
Société Tunisienne de Banque	STB	Tunisia	North	GENDEV	Yes	Yes
Fonds de Promotion de l'Industrie	FPI	DRC	Central	MSME	No	No
(unknown) ¹⁸		Senegal	West		No	No
Development Bank of Zambia	DBZ	Zambia	South	GENDEV	No	No

¹⁸ The AADFI member bank did not fill out identifying details in the survey. As such while we have used the responses in our analysis, we have not identified the institution.

Table 6 List of interviewed banks for case studies

Institutions	Acronym	Country
Caisse de Dépôts et de Consignations de la Côte d'Ivoire	CDC-CI	Côte d'Ivoire
Banque Nationale d'imports – Côte d'Ivoire	BNI-CI	Côte d'Ivoire
National Investment Bank Ltd	NIB	Ghana
Agricultural Finance Corporation	AFC	Kenya
Malawi Agricultural and Industrial Investment Corporation	MAIIC	Malawi
Development Bank of Nigeria	DBN	Nigeria
Development Bank of Seychelles	DBS	Seychelles
Development Bank of Southern Africa	DBSA	South Africa
TIB Development Bank	TIB	Tanzania
ECOWAS Bank for Investment and Development	EBID	TOGO
Société Tunisienne de Banque	STB	Tunisia