# The Dilemma of the African Development Bank: Does Governance Matter for the Long-Run Financing of the MDBs?

**Nancy Birdsall**

## Abstract

Does governance matter for the long-run financing of the multilateral development banks? The structure of governance of the legacy MDBs (the World Bank and the four major regional development banks founded in the twentieth century) ideally should minimize any tradeoff between the confidence of creditor shareholding countries, on which an MDB's own financing depends, and the sense of ownership, legitimacy, and trust of borrowing countries, on which the MDB's effectiveness in supporting development in those borrowing countries depends. Among the five legacy MDBs, the African Development Bank stands out as the one where the governance arrangements, including the distribution of shares and votes between borrowers and non-borrowers, most favors borrowers. Indicators of the AfDB's relative financial strength (a measure of creditworthiness based on sovereign members' vote shares, and a measure of the capacity of each bank's members to engage in collective action or cooperation in raising financing) indicate that its current governance is likely to make it less competitive than its sister MDBs in sustaining creditor (or "donor") confidence in its operations over the long run, and thus in raising substantial capital and concessional resources. The governance problem is most obvious in the case of the African Development Bank's African Development Fund, which today has only about 15 percent of the resources the World Bank has for Africa. The creditors of the AfDB have sufficient control to ensure the Bank's financial soundness (and AAA rating), but a collective action constraint in pushing for reforms in the Bank's operations. The paper concludes with ideas for long-run reform of governance at the African Development Bank, modeled more closely on the governance of the Inter-American Development Bank.

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## Contents

## Introduction

In this paper, I explore the question in the subtitle: Does governance matter for the long-run financing and effectiveness the multilateral development banks? Does the system of weighted voting that is peculiar to them (compared to the United Nations and other international institutions), and favors the high-income countries that are the banks' main financiers, matter for their long-run access to financing and their effectiveness as development institutions? Does the voting structure, as well as other aspects of governance, involve some tradeoff between the confidence of creditor countries in the different MDBs,[1] and the sense of ownership, legitimacy, and trust of borrowers? Is that tradeoff reflected in differences in the banks' relative success in raising capital and contributions to sustain their operations, and with what implications for the different banks' development effectiveness in borrowing countries?

There is no way to definitively answer those questions. But among the five "legacy" MDBs founded in the 20th century, the African Development Bank stands out as the one where the governance arrangements most favor its regional borrowers. The dilemma of the African Bank is that its governance arrangements may be making it relatively less competitive than its sister banks in sustaining creditor (or "donor") confidence over the long run, and thus in raising new capital and periodic contributions to allow for grants and cheap credits to the poorest countries in the region. Lack of competitiveness in raising financing a dilemma both for its borrowers and its high-income creditor shareholders, given their shared goal of optimal use of all available resources in promoting higher and more inclusive and sustained growth in Africa.

To the extent that the African Bank has a current or potential comparative advantage in working with African countries in managing tough political reforms, for example, or in developing regional investments in energy or transport involving two and more countries in the region, its shareholders, almost all of which are also shareholders of the World Bank, may not be optimizing in the allocation of their support across the two banks.[2]

In considering the possible tradeoff between "confidence" of high-income creditors and ownership and "trust" of developing country borrowers, I focus primarily on a key aspect of governance, the distribution of votes between and among creditors and borrowers.[3] I refer also to voting rules and customs for selection of the banks' presidents, which vary among

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[1] See Appendix 1 for a list of the acronyms of multilateral development banks.
[2] There is a larger question of why have the World Bank and the other MDBs in the first place, given that many of the MDBs' borrowers, even some of the poorest, are now able to access the global capital market. On the other hand, developing countries still face substantial volatility and high costs of access to market borrowing—as the new round of debt distress across Africa and in Argentina and Turkey as the time of this writing suggests. The MDBs' major advantage compared to other "aid" programs is that they are more leveraged—and for borrowing countries seen as more technical and less political. There is also the general principle of subsidiarity, which would favor the regional banks in at least some areas of support all other things the same.
[3] Voting shares track closely but are not exactly identical to capital shares.

the major MDBs in their implications for whether the presidents are likely to come from a creditor or borrower country.[4]

I focus on the World Bank and five regional multilateral banks: the World Bank, the Inter-American Development Bank (IADB), the Asian Development Bank (the ADB), the African Development Bank (AfDB), the European Bank for Reconstruction and Development (EBRD) and the Asian Infrastructure Investment Bank (AIIB). All but the AIIB were founded in the 20th century. The AIIB was founded in 2015. All six including the AIIB, are creditor-lender institutions, in which financial strength depends heavily on creditors' commitments of capital.[5]

Of the five 20th century "legacy" banks, the nonborrowers hold 50 percent or more of each bank's shares.[6] But at the African Development Bank the creditors hold less than 50 percent of the votes. Also except for the African Development Bank, all the legacy banks were founded with critical leadership from the world's 20th century major creditor country, the United States, and the United States, though it has sold some shares in some of the banks, is still has the largest or shares with one other country the largest holding of capital shares and voting power.

The sixth bank, the AIIB, was founded under the leadership of China, now a major creditor to other developing countries, and the single largest shareholder at the AIIB, with over 30 percent of the capital and 26 percent of the votes. The AIIB has 27 founding members, including the United Kingdom, that have agreed on initial authorized capital of $100 billion. The Chinese also took the lead in the creation of the New Development Bank, in which each of five country BRICS—Brazil, Russia, India, China and South Africa—has agreed on initial authorized capital of $100 billion as well. In both these new banks, China has so far provided the bulk of initial paid-in capital.

There are at least a half-dozen other large multilateral development banks, including the European Investment Bank and the Islamic Development Bank. Some, including the Andean Development Corporation (CAF, the Corporacion Andino de Fomento) and the New Development Bank, are not creditor-owned banks but more like credit cooperatives, in which the majority or entirety of capital is provided by members eligible to borrow. Their members benefit from collective ownership, at least in principle, in the form of lower borrowing costs than otherwise because of variation in the kind of external risks they face and their willingness through the banks to provide a form of implicit guarantees to each other. I refer selectively to governance arrangements at these non-creditor-base banks to

[4] On other aspects of governance see Birdsall and Morris (2016), pp. 25-26 and Appendix 6).
[5] At the AIIB all members including China are eligible to borrow so the borrower-creditor distinction used in this paper is de facto not de jure. In principle the AIIB could become a credit cooperative; that is unlikely since its current articles of agreement limit non-regional (non-borrowing) member countries to 25 percent of shares.
[6] There is also a regional/non-regional distinction in the legacy regional banks. Most regional members are borrowers, but there are exceptions such as Japan at the Asian Development Bank and the US and Canada at the Inter-American Development Bank.

illustrate some points. But these face different challenges and tradeoffs in raising capital to finance their lending and other operations.

In part 1, I present basic information on the assets and other measures of financial strength, and on the current governance arrangements, of the six MDBs on which I focus throughout.

In part 2, I present two measures of long-run financial strength, one a measure of creditworthiness based on sovereign members' vote shares, and the other of the capacity of each bank's members to engage in collective action or cooperation in raising financing and deploying it effectively.[7] Among the six banks, the African Development Bank has the weakest overall measures of financial strength.

In part 3, I compare the situation of the concessional window of the African Development Bank to that of the World Bank. The comparison provides a striking illustration of the likely tradeoff between creditors' confidence in an institution and borrowers' trust and ownership of its policies and operations.

In concluding reflections, I comment on the implications of the tradeoff in the short run for the shareholders of the African Development Bank and in the longer run for likely changes in governance at all the banks.

## Section 1. Background on Financing and Governance of Selected MDBs

### Financial indicators

The six MBDs are all financially sound; triple A ratings provide the basis for their borrowing on good terms in order to lend on good terms relative to the market.

Table 1 shows loans outstanding and current capital stock or equity of each of the six banks; the capital stock includes that for private sector lending. The table distinguishes between the ordinary capital or hard window and the concessional (or soft) windows where relevant.

[7] Special thanks to Alan Gelb.

**Table 1. Loans outstanding and capital stock, six MDBs (nominal US $ millions)[8]**

| Bank | Founding date | Loans outstanding | Capital | | |
|---|---|---|---|---|---|
| | | | Subscribed capital | Hard window[a] | Soft window[b] |
| IBRD | 1944 | 177,422 | 268,937 | 64,848 | 158,720 |
| IADB | 1959 | 89, 082 | 176,752 | 33,692 | Not applicable |
| AfDB | 1964 | 25,378 | 93,276 | 11,340 | 7,434 |
| AsDB | 1966 | 101,008 | 151,169 | 50,269[c] | 2,067[d] |
| EBRD | 1991 | 26,579 | 35,636 | 18,135 | Not applicable |
| AIIB | 2015 | 773 | 95,001 | 18,959 | Not applicable |

[a] Does not include callable capital.

[b] The EBRD and the AIIB have never had their own concessional funds. The AsDB and the IADB have recently put their soft window on a single balance sheet with their hard window.

[c] Includes what was concessional "equity" (discounted reflows) of about $38 billion in 2015 (Birdsall and Morris, p. 35).

[d] Contributions to a newly constituted AsDB grants-only fund.

Sources: Annual Reports, Financial Statements, and Press Releases

The IBRD (International Bank for Reconstruction and Development), now widely called the World Bank, is the oldest and largest of the six (Table 1). It was the first MDB to create, in addition to its ordinary capital lending window (the IBRD), a window for lending to the private sector (in the interest of development), the IFC (International Finance Corporation), in 1956, and a concessional window for the poorest countries, IDA, in 1960.

Until the 2008–09 global financial crisis, the World Bank was as large as the Inter-American, Asian and African banks combined, measured in terms of total capital to support ordinary lending. The financial crisis increased the demand for lending from all the banks leading to capital increases ("recapitalizations") in 2011 at all the legacy banks except the EBRD. The increases were relatively larger at the three regional banks than at the World Bank, probably reflecting the greater interest of their regional borrowers in "their" banks. The creation of the AIIB in 2015 added further to the share of the regional banks in total MDB (paid-in) capital; they now constitute more than 50 percent of total MDB capital (Table 1).

Even given the 2018 capital increase of $60 billion ($7 billion paid-in) at the World Bank, the long-run trend appears to be relatively faster growth of the regional banks, where the middle-income countries have a relatively greater role and greater sense of "ownership,"

[8] Note that the IBRD's gearing ratios (loans outstanding divided by capital stock) at about 2.7 is high compared to the legacy regional banks, presumably reflecting its more diversified portfolio. Shareholders at the regional banks get lower leverage (or "headroom") for their capital. The IADB has the highest gearing ratio among the regional banks. The major MDBs have recently agreed on exposure swaps which have increased the headroom for the African Development and Inter-American Development Banks. See http://www.worldbank.org/en/news/press-release/2015/12/22/development-banks-optimize-balance-sheets

particularly considering the two new MDBs founded with leadership from China.[9] This is particularly interesting given that the higher "gearing ratio" of the IBRD, reflecting its age and its globally diversified portfolio, makes it a more efficient user of shareholder capital than the regional banks.[10] That is not surprising. It reflects the rise of emerging market and other developing economies as a share of total global GDP, from about one-fifth to more than one-third[11] in the last two to three decades. The trend may also reflect the past resistance of World Bank management and its large creditors, particularly the United States, to calls from China and other emerging markets for larger recapitalizations there in the last two decades, possibly due to their own domestic budgeting concerns.

In contrast to the increase in the size of the regional banks for ordinary lending compared to the World Bank, the latter has and continues to dominate the other MDBs in its financial capacity on the concessional side—suggesting confidence of the traditional Western donors in the effectiveness of its operations in the low-income countries.[12]

The most extreme example of dominance on the concessional side is in the Africa region. The World Bank's latest IDA replenishment in 2017 was about $75 billion to cover the 2018–2020 period, including not only new contributions, but high reflows of over $20 billion, and for the first time for any concessional window, borrowing on the capital market of over $22 billion. IDA documents refer to the likelihood that at least $45 billion of the $75 billion will be allocated for grants and lending in the Africa region.[13] For the same period, the replenishment of the African Development Fund of the AfDB was less than $7 billion, meaning the footprint of IDA in Africa is likely to be as much over six times greater in the next three years than that of the AfDB.

The confidence of the traditional donors and high-income creditors in the World Bank is also evident in their contributions to trust funds housed and managed at that bank. Trust

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[9] See Morris and Gleave (2015) on this issue, pp. 7–8, including Box 1: "The creation of the AIIB and New Development Bank followed repeated calls from major World Bank borrowers for more capital in the bank. Those calls were rejected by World Bank management and were met with silence from key non-borrowing shareholders. Having concluded that more capital would not be mobilized through the World Bank, the Chinese in particular moved to mobilize additional capital in new institutions (see Box 1)." See also Birdsall and Morris (2016, pp. 2–3); and Xu, 2017, p. 255.

[10] The gearing ratio refers to the ratio of loans outstanding to hard window capital. The IADB's gearing ratio is relatively high among the regional banks; that may be associated with the relatively total credit score of its borrowers, weighted by borrowers' shares, as shown in Table 6 below.

[11] Market-based exchange rates. The share of emerging markets and developing countries is greater in purchasing power parity (PPP) terms.

[12] Also, its large size permits the World Bank to put considerable staff and other resources into the process of persuading its donor members to contribute to IDA. Before if not as soon as one replenishment is negotiated, staff begin the analyses and discussions with donors for the next replenishment.

[13] Report from the Executive Directors of the International Development Association to the Board of Governors: Additions to IDA Resources - Eighteenth Replenishment (English) http://documents.worldbank.org/curated/en/348661486654455091/pdf/112728-correct-file-PUBLIC-Rpt-from-EDs-Additions-to-IDA-Resources-2-9-17-For-Disclosure.pdf. See also World Bank, 2017: http://www.worldbank.org/en/news/press-release/2017/03/19/world-bank-group-announces-record-57-billion-for-sub-saharan-africa

funds now finance almost 40 percent of the staff and other costs of preparing and supervising lending and advisory services the Bank provides to borrowing countries.[14]

Overall, the World Bank remains primus inter pares among the major MDBs as a financier (as well as policy force), while as a group the regional banks are growing as fast or faster. Among the regional banks, the African Development Bank is still the smallest of the legacy banks, and relative to the World Bank on the concessional size, its African Development Fund is vastly smaller than the World Bank's IDA window in Africa. I turn to that issue in more detail in Section 3 below.

## Governance

The MDBs' use of weighted voting, based heavily on the proportion of total capital or equity its members provide, is what most distinguishes them from other international institutions, including the United Nations and its agencies, that for the most part rely on voluntary contributions to finance the costs of support they provide to developing countries.[15] Though individual loans and many other decisions at the banks are traditionally agreed on the basis of "consensus," voting does matter because behind consensus on contentious issues there is often critical negotiation with and between coalitions of creditors and of borrowers.

At the same time, the voting structure of the banks varies considerably. Table 2 shows for each of the six banks the voting shares of non-borrowers (mostly high-income) and borrowers.[16] In the case of the AIIB, China, its major creditor, is included as a non-borrower;[17] at the ADB and the IBRD it is included as a borrower.[18]

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[14] See page 14 (17 in pdf), Table 4 of Management's Discussion & Analysis and Financial Statements (Fiscal Year 2017), June 30, 2017, retrieved from https://openknowledge.worldbank.org/bitstream/handle/10986/27986/211119v2.pdf

[15] Even "mandatory" contributions, e.g., to the United Nations, were originally agreed voluntarily, in the context of negotiated agreements.

[16] Voting shares are not identical to authorized capital provided among other reasons because in most banks every shareholder is entitled to a fixed number of "basic votes."

[17] This paper treats China as a non-borrower at the AIIB because China is the major creditor, providing over 30 percent of authorized capital (and with 26.6 percent of votes, which ensures it a veto on some decisions). China had received $250 million of loan approvals from AIIB out of a portfolio of $4.4 billion as of June 2018. If China borrows substantially more from the AIIB, or its major borrowers acquire significantly more shares, the AIIB it might become a "mixed" MDB (see below).

[18] Appendix 2 lists the top five shareholders by voting power.

**Table 2. Current vote shares: borrowers[a] and non-borrowers**

| Bank | Non-borrowers | Borrowers |
|---|---|---|
| IBRD | 61.3 | 38.7 |
| IADB | 50.[c] | 50.[c] |
| AfDB | 40.6 | 59.4 |
| AsDB | 60.3 | 39.4 |
| EBRD | 85.5 | 14.5 |
| AIIB[b] | 65.2 | 34.8 |

[a] Eligible borrowers are not always defined; for the last available fiscal year, any country that has had a loan approved is considered a borrower, as are countries in which disbursements occurred.
[b] All members are eligible to borrow. China is included here as a creditor, reflecting the current though not necessarily the future situation.
c It is 50.02 for borrowers and 49.98 for non-borrowers.
Sources: Annual reports and vote share disclosures.

The African Development Bank is again an exception among the six banks. At all the other banks, except the AfDB, the non-borrowers have 50 percent (at the IADB) or more of voting share.[19]

Table 3 indicates the voting rules that affect whether the presidents of each bank are likely to come from a creditor or borrower member country. At the legacy banks the president is also the chair of the board, which makes him (so far always him) less obviously accountable to the board. The presidents are powerful because they can take initiatives; they have positive power compared to the boards of directors, and even to the ministerial level boards of governors (which meet only once a year).[20] They can institute major internal reforms, push through higher administrative budgets and changes in operational and financial policies, and most important initiate and negotiate increases in capital and in contributions. The power of sovereign shareholders is, in contrast, primarily negative power. They can stop or slow initiatives, including for new capital and new contributions, and (in rare cases) refuse to approve loans—but even their negative power relies heavily on their engaging in coalitions with others—an issue of collective action to which I turn below. For that reason, the major creditors and donors have a vital and ongoing interest in who becomes president of every MDB.

The World Bank is the only one of the five 20th century legacy banks where the president is chosen solely on the basis of a majority of the *weighted* votes, which ensure creditors (and up

[19] The 60/40 split does not function for all decisions. Approval of loans from ordinary capital (hard window) requires 66/2/3 of votes and from the AfDF (soft window) a higher percentage is needed. Most decisions in the board, including lending decisions, are made by consensus as in all the MDBs; where decisions are contentious, however, even the appearance of consensus is likely to reflect the reality of voting power.
[20] I argue that the president of the World Bank is powerful in this 2012 blog post: Does it Matter Who Runs the World Bank?

to now the largest creditor, the United States[21]), control the process. At the other banks some system of double majority voting applies, in which a candidate also needs a majority of all members or of regional member country unweighted votes. Double majority voting ensures that coalitions of borrowers and of non-borrowers can veto the other's favored candidate, assuming they are able to form and hold coalitions.

**Table 3. Selection of president**

| Bank | Majority of what/whom | Effective eligibility |
|---|---|---|
| World Bank (IBRD) | Weighted votes of members | Up to now United States |
| IADB | Weighted votes of members and majority of unweighted votes of regional members. | Likely to be from borrower country |
| AfDB | Weighted votes of members, and majority of weighted votes of regional members. | Regional member country national, and likely from borrower country |
| AsDB | Weighted votes of members and majority of unweighted votes of members. | Regional member country national, up to now Japan |
| EBRD | Weighted votes of members, and majority of unweighted votes of members. | No nationality requirements |
| AIIB | Two-thirds support from governors, representing at least three-fourths of total voting power | Member country national; most likely to be China |

At the Inter-American and African banks, the presidents have come from borrowing countries because the successful candidate requires a majority of the *unweighted* votes of regional members, almost all of whom are borrowers. At the Asian Bank, the double majority of regional member votes and weighted votes has ensured that the president has been Japanese, and similarly that the president of the EBRD has been a western European. At the AIIB, a super-majority of weighted votes is likely to ensure that a Chinese national will be president.

The bottom line on governance (Table 4, which also shows board chairs) is that of the six banks, the African Development Bank is the only one that is borrower-dominant, that is where both weighted votes and the presidency (and its location in the Africa region) give borrowers a clear sense of ownership of policy and day-to-day operations. At the IADB

[21] Along with weighted voting, "custom" (and global power) have so far meant the president has been an American. The IMF selects its managing director on the basis of weighted votes only, in my view with long-run risks to legitimacy and ownership similar to the situation at the World Bank: https://www.cgdev.org/blog/put-double-majority-voting-back-table-imf

there is a balance of power and influence; I label it as a "mixed" bank.[22] (Other MDBs are added for comparison.)

**Table 4. What type of MDB? Creditor- or borrower-dominant, or "mixed" or co-op?**

| | Creditor-Dominant | | | Borrower-Dominant | | | |
|---|---|---|---|---|---|---|---|
| Banks | Weighted shares | Board chairs | Presidency | Weighted shares | Board chairs | Presidency | Creditor, borrower, mixed, or co-op |
| IBRD | ✓ | ✓ | ✓ | | | | Creditor |
| IADB | 50 | | | 50 | ✓ | ✓ | Mixed |
| AfDB | | | | ✓ | ✓ | ✓ | Borrower |
| AsDB | ✓ | ✓ | ✓ | | | | Creditor |
| EBRD | ✓ | ✓ | ✓ | | | | Creditor |
| AIIB | ✓ | | ✓ | | ✓ | | Creditor[a] |
| | | | | | | | |
| EIB | ✓ | ✓ | ✓ | | | | Co-op[b] |
| NewDB | | | | ✓ | ✓ | ✓ | Co-op |
| IsDB | | | ✓ | ✓ | ✓ | | Mixed |
| CAF | | | | ✓ | ✓ | ✓ | Co-op |

[a] Counting China as a creditor. See footnote 4 and table 2 notes.
[b] The EIB is a co-op among its European members; a creditor for countries outside of the European Union.

## Section 2. Does Voting Structure Matter for Long-Run Financial Strength?

In this section I look at the possible relationship between financial strength of the different banks and their governance structure. I use two measures: one focused on the banks' creditworthiness relative to each other, and the second based on their relative capacity for collective action in the process of both raising their financing and deploying their financing effectively and efficiently—which in the long run has some influence on subsequent rounds of raising financing.

### Creditworthiness

Of interest for financing *of* the banks are the voting shares of the non-borrowers, or creditors, since in the global capital market it is the creditors whose own credit standings provide the key financial backing for each bank. Table 5 provides for each bank the total percentage of shares of the top non-borrower shareholder); of the top five non-borrower shareholders; and of all non-borrowers.

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[22] See Birdsall, 2003 (link)

**Table 5. Vote shares of top non-borrowers**

| Bank | Vote share of top non-borrower | Vote share of top five non-borrowers | Vote share of all non-borrowers[a] |
|---|---|---|---|
| IBRD | 16.0 | 34.5 | 61.3 |
| IADB | 30.0 | 42.9 | 50.0 |
| AfDB | 6.1 | 23.5 | 40.6 |
| AsDB | T-12.8[b] | 39.3 | 60.3 |
| EBRD | 10.1 | 44.5 | 85.5 |
| AIIB | 26.6[c] | 41.2[c] | 65.2[c] |

[a] Includes some HIC borrowers
[b] Two-way tie between Japan and the United States
[c] Counting China as a non-borrower, and including China with all non-borrowers
Sources: Annual reports and vote share disclosures.

Not surprisingly, the borrower-dominant African Development Bank has the lowest percentage of shares in all three categories. The "mixed" IADB has the advantage from the creditworthiness pint of view, that the United States, the top shareholder overall, has 30 percent of the total votes.

Table 6 ranks the banks using a creditworthiness "score" for each that permits comparisons among the MDBs beyond the common AAA ratings of the six banks qua banks. The creditworthiness scores are the sum of individual members' sovereign credit scores weighted by their (differing) proportions of voting shares in each bank. The sovereign members' scores are standardized to numbers between 0 and 100 using Standard and Poor, Moody's and Fitch ratings—see Appendix 2—and only sovereigns with at least a score of 80 are included). In the case of the World Bank, the US's credit "score" of 100 is multiplied by its voting share of 16.0 percent; in the case of the ADB by 12.8 percent; in the case of IADB by 30.0 percent and so on.

**Table 6. Average credit score, weighted by vote share**

| Bank | 1<br>Non-borrowers | 2<br>Borrowers | (1+2) =<br>Average credit score, weighted by vote share | Ranking of the six MDBs |
|---|---|---|---|---|
| IBRD | 55.2 | 17.4 | 72.6 | 3 |
| IADB | 47.2 | 23.3 | 70.5 | 4 |
| AfDB | 36.5 | 18.7 | 55.2 | 6 |
| AsDB | 54.7 | 19.3 | 73.6 | 2 |
| EBRD | 70.6 | 7.9 | 78.5 | 1 |
| AIIB | 30.3 | 34.1 | 64.4 | 5 |
| | | | | |
| EIB[a] | | 83.8 | 83.8 | |
| NewDB[a, b] | | 59.0 | 59.0 | |
| IsDB[a] | | 54.1 | 54.1 | |
| CAF[a] | | 48.1 | 48.1 | |

[a] See Appendix 2 for detailed methodology.
[b] All voting members are also borrowers.
Sources: Sovereign credit ratings from publicly available credit scores, and annual reports.

The ranking of the six MDBs is similar, not surprisingly, to the ranking based simply on the share of votes of non-borrowers in each bank). The African Development Bank once again ranks at the bottom of the six legacy banks, and in cardinal terms, notably so.

## Collective Action Capability

Next consider the capacity of each bank's members to work together and in creditor/borrower coalitions to maximize the amount of resources raised (primarily from HICs and creditors) and thus to have substantial resources to deploy (a key interest of MICs and LICs/borrowers).

Two assumptions matter in assessing collective action capability within the two groups.

> First, coalition building within the two groups (non-borrowers, borrowers) is easier the greater the concentration of shares within the group; concentration invites following the lead of the largest shareholder or small number of large shareholders – in effect free-riding to a common coalition view.
>
> Second, collective action capability matters more for any coalition obtaining "yes" on new initiatives or new policies, than for ensuring "no" on issues a coalition rejects.

On this second distinction, an example of "no" power is in the case of double majority voting for an MDB president; a big enough coalition of borrowers can block a candidate the non-borrowers might approve (so that such candidates are less likely to be nominated than they are at the World Bank and IMF with simple weighted voting).[23] In the case of the African Development Bank, the "no" power of the non-borrowers is greater than it appears because loan approvals require 66 2/3 of votes. This is not an accident but a "fix" to the low voting of non-borrowers to give non-borrowers "no" power; it means that in addition to the potential 60 percent of all "borrowers" and "regional" African votes, another 6 2/3 votes must come from non-regional non-borrowers if a loan is to be approved.)

In contrast, collective action capability is central or fundamental to "yes" power, i.e., to taking a new initiative, pushing for a new policy, or negotiating a new recapitalization or new replenishment. (One reason MDB presidents are powerful is that once in office they have immense "yes" power compared to shareholders represented by large boards.)

The shares of the top and top five non-borrower votes in each bank are shown in table 5 above; the African Development Bank has the lowest concentration of non-borrower vote shares among the six banks. The shares of borrower votes are in table 7 below. In all the banks, the total shares of borrower votes are low compared to non-borrowers, reflecting the MDB model in which non-borrowers are in effect providing the benefit of their high sovereign credit ratings with borrowers. In terms of collective action potential among the borrowers, the IADB does particularly well with the highest vote shares of its top borrowers (Brazil and Argentina) and of its top five borrowers. The top five borrowers, with 36.5 percent of all votes have almost as many shares as the top five creditors—for a healthy balance between creditors and borrowers as well as within each group in this "mixed" bank. The AfDB does not have the same advantage of a single large borrower in terms of votes, but its top five borrowers have a healthy 28.1 percent of shares.

**Table 7. Vote shares of top borrowers**

| Bank | Vote share of top borrower | Vote share of top five borrowers |
|---|---|---|
| IBRD | 4.5 | 14.1 |
| IADB | T-11.4[a] | 36.5 |
| AfDB | 9.3 | 28.1 |
| AsDB | 5.5 | 20.2 |
| EBRD | 4.0 | 8.2 |
| AIIB[b] | 7.7 | 21.1 |

[a] Two-way tie between Brazil and Argentina.
[b] Counting China as a non-borrower.
Sources: Annual reports, investor presentations, and vote share disclosures.

[23] Paul Wolfowitz was nominated by the George W. Bush administration as president of the World Bank, and elected in 2005; if a majority of votes of all member countries had been required (in addition to a majority of weighted votes) many borrowing members might have joined in resisting his election because of his association with the US intervention in Iraq, in which case the US would have turned to an alternative nominee. He later resigned under pressure, though not because of his views on Iraq.

A more revealing indicator of collective action capability is the ease with which the two groups of shareholding countries in each bank, the creditors and borrowers, can manage the process of cooperation *within* their groups, particularly in raising rounds of financing, but also in deploying the resulting resources effectively. Appendix 5 table: Collective Action Indicators, shows the Herfindahl-Hirschman Index of concentration for the non-borrowing countries and borrower countries in each bank.[24] Table 8 below uses those results to rank the six MDBs on the index and the other indicators of collective action capability.

Concentrating on the indices of concentration (the higher the concentration the easier it is to engage in collective action), the regional banks all do better on the non-borrower side than the World Bank—except the AfDB. The IADB ranks as the highest or high on most indicators, and the AfDB the lowest on the non-borrower side (see its much lower index compared to the other banks in cardinal terms in the appendix table). The IADB's high concentration indices for both non-borrowers and borrowers reflects the very large percentage shares of the United States, and on the borrower side its relatively few large borrowers compared to the other regions.

The AIIB also has a high concentration index for non-borrowers, with China included with the non-borrowers. That may change over time. China's leadership in the founding of the AIIB mirrors the role the United States took in the late 1940s at the World Bank. As more countries join over time, perhaps the AIIB's concentration index will decline as has been the case at the World Bank.

China's role in the AIIB as both the largest shareholder and a borrower allows it to form coalitions with either creditors or borrowers depending on its interests. In that sense, the AIIB is not so much a regional bank as a global vehicle to signal China's drive for global leadership and influence, akin to the original and abiding influence of the United States at the World Bank.[25]

The AfDB's low rank among the MDBs on the collective action indicators for non-borrowers reflects in part its history, discussed below, as the only one of the legacy banks founded as a cooperative "regional" bank, originally owned solely by African members. It is the only bank in which the top creditor or creditors is not the top shareholder, but a borrower, Nigeria (itself with a small 9.3 percent of the votes). Only two creditors, the United States and Japan, are among its top five shareholders, with just 11.6 percent of votes

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[24] The conventional use of the Herfindahl-Hirschman Index is as a measure of concentration of firms within industries, with greater concentration implying less competition in the industry as the larger firms cooperate on pricing. In the case of the banks, we take the square of each creditor member's and each borrower member's voting share and sum the results for each group.
[25] For example, at least one non-regional member has gained access to credit: Egypt has received $210 million in loan approvals already and it is reasonable to expect that the other African member, Ethiopia, will also have access to credit soon as well. Likewise, prospective non-regional members include Kenya, Madagascar, South Africa, and Sudan. The extension of the AIIB's financial influence into Africa suggests it may be a potential competitor for the AfDB and IBRD as well in Africa.

together. The former colonial powers, the United Kingdom and France, have only 1.8 and 3.8 percent of votes, though each is still a significant bilateral donor in the region (as is the US), and each continues to play a substantial role on security issues, in trade, and as major sources of foreign investment.

**Table 8. Collective action rankings**

| | Non-Borrowers | | | Borrowers | | |
|---|---|---|---|---|---|---|
| Legacy banks | Rank by vote share of the top non-borrower | Rank by vote share of the top five non-borrowers | Rank by Herfindahl concentration ratio for non-borrowers | Rank by vote share of the top borrower | Rank by vote share of top five borrowers | Rank by Herfindahl conc. index for borrowers |
| IBRD | 3 | 5 | 5 | 5 | 5 | 5 |
| IADB | 1 | 2 | 1 | 1 | 1 | 1 |
| AfDB | 6 | 6 | 6 | 2 | 2 | 2 |
| AsDB | 4 | 4 | 4 | 4 | 4 | 4 |
| EBRD | 5 | 1 | 3 | 6 | 6 | 6 |
| AIIB[a] | 2 | 3 | 2 | 3 | 3 | 3 |

[a] Counting China as a non-borrower.
Source: Author's calculations based on data from other tables.

The Herfindahl Hirschman index for borrowers at the AfDB is high because it has so many borrowing members. The number of African regional members is high (54) compared to the other regional banks (a maximum of 49 at the Asian Development Bank); ironically, because so many of the African members are small economies, the borrowers' influence as a group is highly diffused.

In summary of Section 2, the simple indicators suggest that the structure of governance does matter for the relative financial strength of the six MDBs.[26] Three points stand out:

> First, the borrower-dominant African Development Bank is weak compared to the other major regional banks and the World Bank on both market credibility for raising resources and on indicators of capacity to cooperate in doing so.
>
> Second, the "mixed" Inter-American Development Bank, though weak on weighted sovereign creditworthiness, is very strong on collective action capability both of creditors and of borrowers.

[26] This is probably true of the MDBs as a group relative to the UN and other international institutions that do not have weighted voting.

> Third, except for the African Development Bank, the regional banks "compete" well compared to the older and larger World Bank, particularly on the collective action indicators.[27]

One additional note is useful before summarizing this Section 2. Governance is not the only factor that matters for financial strength. For any immediate recapitalization or replenishment, the then-current views of the "performance" of an MDB, including its development effectiveness and its efficiency in using resources (on the part of its management and staff) matter; these are almost always on the agenda in negotiating new financing. Absorption capacity of the MDBs' borrowers also matters (though with a region will be common to the World Bank and relevant regional bank or banks). However, these are short-term not long-term structural issues, and in the long run, they may well be as much an outcome (or endogenous to) the structure of an MDBs' governance itself. Moreover, they may fail to reflect the *long-run, potential* comparative advantage of one or another MDB; the 2016 high-level panel report recommending shareholders concentrate major new lending capacity on the regional banks, reflected the view in the next section that the regional banks have greater ownership of borrowers, which may strengthen their effectiveness in encouraging politically difficult economic reforms.[28]

## Section 3. Why Is the African Development Fund So Small?

In this section, I turn to the possible tradeoff in raising and deploying resources from the market between the confidence of major non-borrowing or creditor shareholders in the different MDBs, and the sense of ownership, legitimacy, and trust of the shareholding borrowers. I focus on the dilemma of the AfDB, given the indicators above, and on how its history and current governance structure appear to limit its country shareholders' willingness to contribute to its concessional window, the African Development Fund—particularly compared to the World Bank.

I assume that confidence on the part of the major creditors is a function of their sense of control and influence in each bank (related to their power in the form of votes and other indicators of governance), and in the long run matters as it affects their willingness to put money on the table. Trust and legitimacy on the part of borrowers are a function of their sense of ownership in the banks as institutions, and their satisfaction at the country level with each bank's approach to lending and policy dialogue. The latter matters to the long-run effectiveness of the banks, including to their creditor members, who are accountable to their constituencies at home for the effective use of MDB resources.

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[27] Among them, the IADB is weaker than the Asian Development Bank on the market creditworthiness indicator, but stronger on the collective action indicators. And vice versa.

[28] Birdsall and Morris (2016), especially for infrastructure (Chapter 2). See also footnote 9 above.

## The African Development Fund: Now Six to Seven Times Smaller than the World Bank's IDA in Africa

The Africa region currently has the largest number of borrowers to the African Development Bank compared to other regions with their respective regional banks, and more relevant, the highest portion of its borrowers (currently 25 of 37 borrowers) that are eligible to borrow in part (blend countries) or completely on highly concessional terms from the World Bank and the African Development Bank.[29] These borrowers rely on funds at the banks that are "replenished" every three years, primarily by donors' direct contributions.

In Section 1, I noted that the World Bank's IDA is likely to be six to seven times bigger in terms of the value of loans in the 2018-2020 period in Africa, expected to be about $45 billion,[30] than the African Development Bank's African Development Fund, expected to be at most $7 billion.

In addition, there is a kind of ineluctable momentum guaranteeing future that the growth of IDA in Africa will be faster, for at least two reasons. First, IDA will continue to receive higher reflows to relend in each of the next several three-year replenishment periods. In the current period, reflows are projected to be almost $20 billion to IDA and perhaps $600 million to the AfDF;[31] one reason is that IDA continues to receive reflows from China, India and other countries outside Africa that no longer borrow from IDA or borrow only limited amounts. Second, IDA now has its own AAA credit rating, separate from that of the IBRD, and for the first time has borrowed on the capital market. Its own borrowing of as much as $25 billion will not necessarily increase every three years (the number of countries eligible for highly concessional lending should continue to decline), but other demands for concessional resources, for refugees, for natural disaster relief, possibly for debt relief could rise). But even if the amounts decline, they will be large compared to any possible borrowing by the AfDF, given that the "equity" of the AfDF in terms of expected future reflows is so much smaller.

The AfDF depends almost entirely on the traditional donors for contributions. Figure 1 compares the growth of the two funds since 2002. Since such a large proportion of lending from IDA goes to Africa, the two are roughly comparable in terms of "need" and absorption capacity from the point of view of the donors. The absolute decline in the size of the last two AfDF replenishments suggests that the donors prefer ensuring growth at IDA, even ultimately for lending to African members, over growth at the much smaller AfDF.

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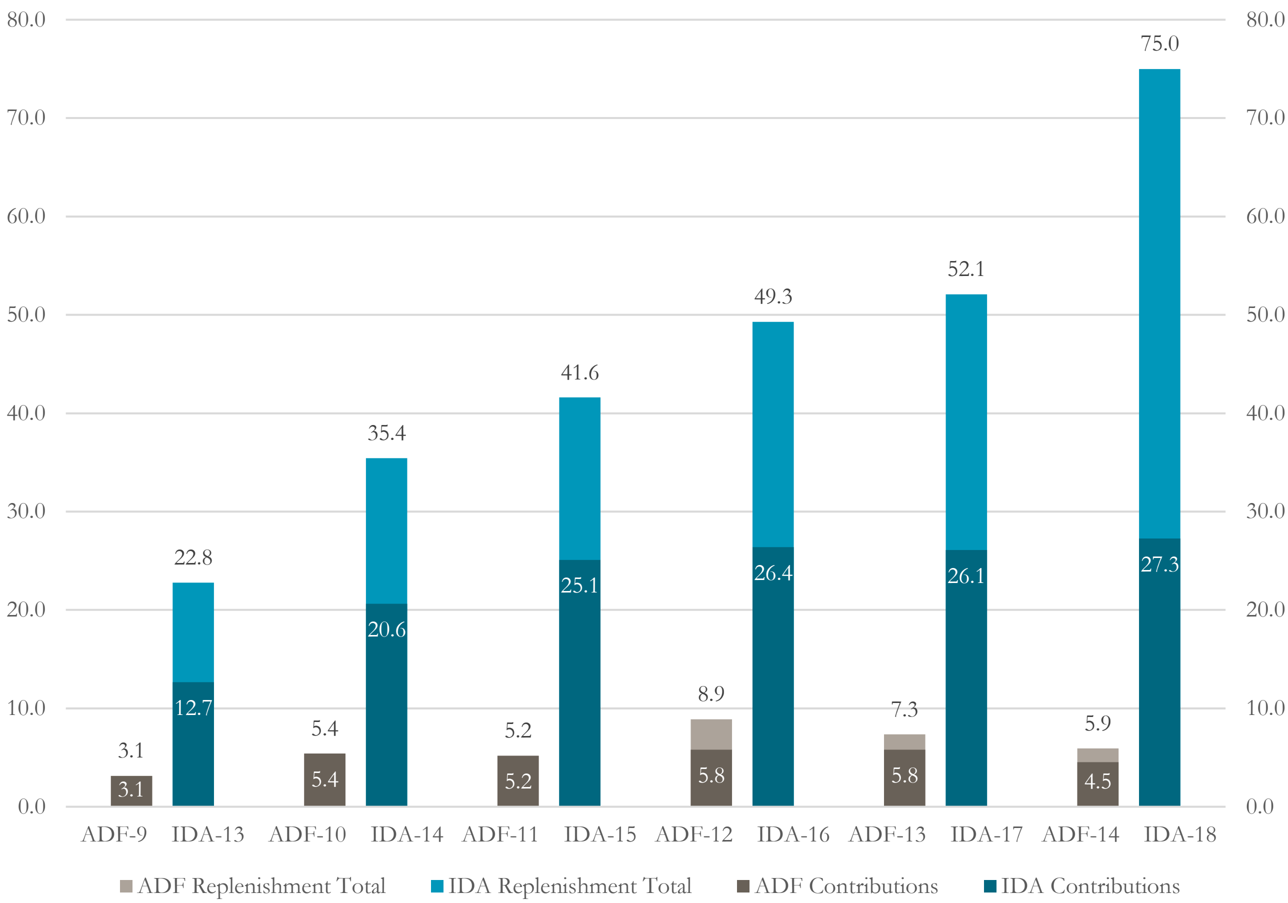
[29] AsDB is close, with 23/38 = 61 percent borrowing countries as IDA or blend eligible.

[30] This includes the $2 billion to the IFC for lending and other operations in low-income countries, most of which are in Africa.

[31] AfDF-14 report, and AfDF Compendium of Statistics, 2017. The $1 billion over three years is a generous estimate; average annual reflows in 2015 were less than $100 million.

**Figure 1. IDA and AfDF replenishments in comparative perspective (nominal USD billions); new contributions are shown in a darker color**




Sources: Replenishment data from IDA and ADF reports and press releases, and converted using historic exchange rates data from IMF and AfDB

Other factors besides governance matter in the decisions of MDB shareholders about funding of MDB resources. At any one point in time, those decisions are affected by high-income shareholders' own fiscal situations, and by the perception of and measures of the relative effectiveness of the different MDBs. Still, the contrast now between the size of IDA and of the AfDF, and the (small) decline in recent contributions to the latter, is notable. The situation suggests there is a tradeoff for the shareholders of the AfDB between governance arrangements that minimize the influence of the high-income country creditors and their own access to financing from their own regional bank.

## History Matters: Why Africans Cite Their Own Bank as Their Preferred, Trusted Partner

The African Development Bank was founded in 1964, in the early days of post-colonial independence of African countries. It is the only one of the six banks that was founded and originally "owned" by its regional member African countries only. Unlike the other legacy banks, it began with a governance structure closer in spirit to the the credit cooperatives owned by middle-income countries, the New Bank and the CAF.

Until 1982, countries outside of the Africa region could not join as full members of the Bank. Even today, the AfDB, despite a relatively large number of non-regional shareholders compared to the Asian and Inter-American banks, has a voting structure in which its African members have the majority of votes (59.4 percent). Its history and its current governance make it very much an African bank.

Because so many of the Bank's borrowers were and are low-income countries, by 1972 the logic of creating a window similar to IDA at the World Bank to provide highly concessional funding to the poorest countries, had become clear. In that year, the African shareholders asked the donors to help create and fund a concessional window. Currently, 38 of the 54 African borrower members of the AfDB depend entirely or in part on financing from the concessional window (the AfDF or the "Fund"), suggesting how fundamental the Fund is to the overall work and effectiveness of the Bank.

It was agreed, presumably in response to a demand of the donor shareholders, that the African members of the Bank would be represented in the Fund solely through their ownership of the Bank, that is by the Bank itself holding 50 percent of votes in the Fund and the donors the other 50 percent. The Bank made a nominal contribution of $5 billion, less than 10 percent of total contributions of $87 billion to the original Fund size, thus becoming formally a donor to the Fund. African countries, including middle-income countries, were excluded from ownership and influence except through the Bank itself, and thus excluded from the separate Board of Governors for the Fund which the donors negotiated.[32]

In fact, the governance set-up of the Fund was much like the original and even current official governance of IDA, where IDA borrowers (middle-income members of the Bank), until and unless they became major contributors, have been represented as observers only in discussions of allocations of IDA funding and of operational policies and procedures in general.

The donors on which the funding of the AfDF depends acquired critical control of the use of the concessional funds, and acquired influence they did not have before in management and on operational policies in the African Bank as a whole.[33]

But the starting point was markedly different in the Africa Bank. Duarte (2016) describes a contentious debate about the original governance of the AfDF, in which African shareholders saw the new and separate Fund as inconsistent with the origins of the Bank as a

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[32] As a result, countries like South Africa and Nigeria had no incentive to make contributions and thus acquire more influence in the Fund and the Bank as a whole (so that for example Nigeria set up a separate Trust Fund in 1976 as a mechanism to contribute).

[33] As at the World Bank. See Kapur (2006) on the policy influence exerted by the donors to IDA on the World Bank as a whole.

truly and completely African institution, while the donors, not unreasonably, wanted substantial control of the resources they would contribute, and an arrangement closer to that of IDA.

History may also have played a role in current AfDB articles of agreement that specifies a 60/40 vote split between regional and non-regional members (which is largely between borrowers and non-borrowers). The result of the split is that recent and any future new non-regional members must "buy" shares from existing non-regional members within the 40 percent envelope. That limits the ability of China, Korea, Brazil and the wealthy oil economies of the Middle East to acquire substantial shares without reducing even more the AfDB's low concentration ratio of non-borrowers.[34] This also limits the incentive for recent and new members of the Bank to make large contributions to the AfDF, as it does not necessarily increase their presence or influence in the Bank as a whole.

## Confidence of Creditors vs. Trust of Borrowers; Control of Creditors vs. Ownership

Woods and Martin (2012), based on surveys and extensive interviews of African officials, describe the importance of the Bank's African identity to its African members; and conclude that its "Africanness" explains in large part why its African borrowers rank it as a "preferred development partner" compared to the World Bank and other multilateral and bilateral donors.[35] [36]

This suggests there is a tradeoff, at least in the long run, between the confidence of creditor shareholders (in the fiduciary role of the MDBs for example) in the creditor-dominant banks, and the trust and sense of ownership of borrowing shareholders in the borrower-

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[34] Spain and Brazil are members but have tiny vote shares and did not contribute to the last replenishment of the AfDF. That would make possible an overall increase in capital larger than otherwise—with little if any real diminution of the "Africanness" of the Bank. (At the IDB having "only" 50 percent of the votes—and a president from the region—gives borrowers considerable influence on administrative budgets and operational policies and programs.) In addition, in return for greater engagement and influence at the Bank, new members on the creditor side could contribute well above proportionately to the concessional window. (The AfDF process may have also stiffened resistance of African member countries in reducing their own percentage of shares in the African Bank from its present 60 percent.)

[35] Woods and Martin, 2012, p. 41. "The Bank is a 'preferred partner' for almost 100% of African government stakeholders and 80% of all African stakeholders, among the range of all bilateral ad multilateral agencies fund African development." (p. 4). A 2016 report of an eminent panel on the future of the African Development Fund (I was a member) emphasized the critical role of the African Development Fund as a "trusted partner" in the pressing need for an "Enhanced Policy Dialogue" or a kind of tough-love approach, with borrowers from the Fund. The sub-title of the report is revealing in itself: "Reinvigorating African Concessional Finance: Report of the High Level Panel on Transforming Trust in the AfDB Group into Influence." (African Development Bank Policy Innovation Lab, 2017).

[36]The AfDB has been primarily a "project" bank; perhaps it is more trusted because its borrowers do not associate it with the conditionality of typical World Bank policy (formerly structural adjustment) loans. In the case of the Inter-American Development Bank, on the other hand, the extensive use of conditionality beginning in the 1990s, appears to have increased the IADB's influence without loss of "trust" and sense of ownership of Latin borrowers.

dominant (and "mixed" and "co-op") banks. The former is likely to affect the ability of the banks to finance their lending; the latter is likely to affect the effectiveness of lending in supporting policy change linked to good investments. The World Bank has the confidence its major creditors; the regional banks have a greater sense of ownership on the part of their borrowers.

The "signal" about the tradeoff appears to be more important in the case of concessional funds, on which borrowers as a group are more dependent on "partner" (in aid-speak) non-borrowers or creditors. In the case of concessional funds, creditors are in effect "donors" and want substantial control over the use of their contributions. The World Bank has at least two advantages, including in raising concessional funds destined primarily *for Africa*, over the African Development Bank. It is the oldest (first mover) and biggest MDB and therefore more influential. It has therefore become a key global forum on policies toward the poorest and most fragile states, and the creditors' donor ministries and agencies want to be engaged and heard from in that forum. Its creditors control the presidency, and on policies and lending to the poorest countries, day-to-day implementation under management is seen as fundamental to avoid "giveaways."

## Concluding Reflections

### On the African Development Bank

The dilemma of the African Development Bank is a structural one: its governance arrangements are not conducive to raising money to finance the Bank's activities. Borrowers have more votes on many operational decisions, and the presidency is held by a borrower; that makes it hard for the non-borrowers to take initiative on operational policies without working together; working together is hard because no single non-borrower or small group of non-borrowers has much skin in the game. The non-borrowers have more control of the concessional (AfDF) fund, because they are the major contributors; but for the major bilateral donors to Africa (the UK, the US, and France), contributions to the AfDF are far more expensive in cash terms (and less leveraged, and customarily repeated every three years) than new paid-in capital associated with a new recapitalization is.[37]

With less easily exercised control and influence than they have at the other MDBs;[38] they end up with substantial "no" power but limited "yes" power. Though they can block presidential candidates and particular loans[39], and they can balk at large recapitalizations and replenishments of concessional money, in comparison to their influence at the World Bank,

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[37] The AfDB members are currently negotiating a recapitalization to be agreed, it is hoped, next year (2019).
[38] In addition to the influence associated with their role as major contributors to the concessional fund.
[39] Approval of loans requires 66 2/3 of votes, requiring one or more non-regional members (non-regionals members are all non-borrowers) to approve; and major decisions, including changes in governance, require approval by 2/3 of non-regional members.

they cannot so easily insist on new initiatives or shape ongoing policies and lending programs.

There lies the Catch-22. The creditor non-borrowers have sufficient influence to say "no" to poor use of the AfDB resources, but lack incentives to push for "yes" on additional resources— particularly given they have other avenues for support to Africa as a region. In the absence of incentives to push for major changes, and in Europe perhaps aware of their colonial era misdeeds, the non-borrowers are content to go along and get along.

It is emblematic that France and the United Kingdom, the former colonial powers with considerable investment and security engagement in Africa, and large aid donors to the region are not among the top five shareholders (with respectively just 3.8 and 1.8 percent of the votes); indeed, no European country is. Nor is the European Union a member.[40]

The bottom line is that as a group, the shareholders—borrowers and non-borrowers—are handicapped. They cannot easily manage the long-run tradeoff between ability to raise capital and contributions from those shareholders that pay the piper, so to speak, and the trust and sense of ownership on the part of those countries that would benefit from the additional resources. Without adequate financing compared to the World Bank, the African Development Bank cannot realize fully its long-run potential comparative advantage as a regional bank in supporting difficult economic and other reforms.

The situation at the AfDB suggests that changes in its governance structure could be critical in the long run to its growth as a financier of development, and as an effective one. Fortunately, as has been the case at all the MDBs, governance arrangements are not inflexible. Governance can be changed (See Appendix 3 for specific ideas for borrowers and non-borrowers on changes, based in part on the experience at the Inter-American Development Bank.)

## On Governance at the MDBs: In the Long-Run

One implication for governance of the 20th century legacy banks treated in this paper is that those once dominated by one or more major creditor countries — the World Bank Group and the Asian Development Bank — are likely to follow the Inter-American Development Bank in becoming "mixed" banks with a balance of voting shares between borrowers and non-borrowers. In a mixed bank, the traditional non-borrowers have enough "yes" as well as "no" power to maintain or increase their financial support, and the borrowers have sufficient influence to take initiative (and make deals) in pushing for additional financing. Coalitions of borrowers and non-borrowers can limit major policy, operational changes, and in some cases, leadership changes, to which they object; and are more likely to be able to promote major changes on which they broadly agree.

[40] The EU is not a member of most of the MDBs; the exception is the EBRD; EU grants often help finance project preparation in in support of EBRD operations.

The 21st century AIIB, meanwhile, might evolve as a "creditor-dominant" bank like the World Bank operating at the global level, with China exercising major control as has the US at the World Bank; or as a mixed bank with a 50/50 vote split and rule changes to make the choices of president more open and transparent), or even as a co-op in which all members are eligible to borrow. How it evolves very much depends on the role China takes.

For the legacy regional banks, the "mixed" model has the advantage of minimizing the tradeoff between non-borrower influence and confidence, and the kind of borrower ownership and credibility that enhance their ability to work effectively with borrowers on regional integration and on tough reforms at the country level, including those that require long-run investments in new rules and institutions.

The African Development Bank, in contrast to the other legacy banks, is already borrower dominated, in terms of vote share, leadership, and location. That has the advantage of strong ownership on the part of borrowers, but a disadvantage as well: it is less competitive with the World Bank group in raising new capital and new contributions to finance its operations. As a result, its shareholders (all of whom are also shareholders of the World Bank) are not optimizing; they are not maximizing the potential of the AfBD as a regional bank as a bank with "trust" in the region, to have "influence" as well.[41]

An increase in the size of the AfDB and of its concessional window the AfDF, relative to the World Bank in Africa, would be consistent with the recommendation of the 2016 report of a high-level panel convened by the Center for Global Development, proposing that the common shareholders of all the banks look to the regional banks to take future leadership "through country and regional operations" and policy dialogue and the World Bank take more leadership in the financing of global public goods with positive spillovers at the global level, in support of its own and the regional banks' operations.[42]

The Center for Global Development panel also proposed that the common shareholders of all the MDBs periodically review the MDBs at the system-wide level, rather than one-at-a-time in the resulting periodic competition for additional financing. That is the setting where the anomalous governance of the African Development Bank might get attention. Still another group, the Eminent Persons Group, has recommended attention of all shareholders of all the MDBs to the advantages of their seeing the MDBs as a system, in which there are options for improving their overall performance through cooperation.[43]

In a changing development landscape, changes in governance at the MDBs (and other multilateral institutions) is difficult but fundamental to their long-run effectiveness. The Africa region is almost certainly the greatest single development challenge of this century, and in the short run the region where the challenge of meeting the Sustainable Development

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[41] See *Reinvigorating African Concessional Finance: Report of the High-Level Panel on Transforming Trust in the AfDB Group into Influence.*

[42] Birdsall and Morris, 2016, p. xi.

[43] See *G20 Eminent Persons Group (EPG) on Global Financial Governance: Update for the G20 Meeting of Finance Ministers and Central Bank Governors.*

Goals is the most daunting. The evidence presented in this paper suggests that in the long run, a shift in the governance structure of the African Development Bank toward a "mixed" system of 50/50 voting shares between borrowers and non-borrowers would make it better armed to help meet those challenges.

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## Appendix 1. Multilateral Development Bank Acronyms

| | |
|---|---|
| AfDB | African Development Bank |
| AfDF | African Development Fund |
| AIIB | Asian Infrastructure and Investment Bank |
| AsDB | Asian Development Bank |
| CAF | Corporación Andina de Fomento |
| EBRD | European Bank for Reconstruction and Development |
| EIB | European Investment Bank |
| IADB | Inter-American Development Bank |
| IDA | International Development Association |
| IsDB | Islamic Development Bank |
| MDB | multilateral development bank |
| NewDB | New Development Bank |

## Appendix 2. Constructing an Average Credit Score, Weighted by Vote Share

Weighted vote share is calculated by first converting each country's maximum sovereign credit rating (across Standard and Poor, Fitch, and Moody's) to a numeric score on a 0 to 100 percent scale (see Table A below). Where ratings agencies differ, I utilize each country's maximum credit rating. For example, the US gets top ratings from Fitch (AAA = 100) and Moody's (Aaa = 100), and an AA+ from Standard and Poor's (AA+ = 95), but the I use the maximum 100 rating.

Next, each country's vote share in each bank is weighted using this numeric credit rating. These weighted vote shares are then summed across borrower status and reported in Table 6.

**Appendix 2 Table. Credit scales alignment**

| S&P | Fitch | Moody's | Corresponding numeric value |
|---|---|---|---|
| AAA | AAA | Aaa | 100 |
| AA+ | AA+ | Aa1 | 95 |
| AA | AA | Aa2 | 90 |
| AA- | AA- | Aa3 | 85 |
| A+ | A+ | A1 | 80 |
| A | A | A2 | 75 |
| A- | A- | A3 | 70 |
| BBB+ | BBB+ | Baa1 | 65 |
| BBB | BBB | Baa2 | 60 |
| BBB- | BBB- | Baa3 | 55 |
| BB+ | BB+ | Ba1 | 50 |
| BB | BB | Ba2 | 45 |
| BB- | BB- | Ba3 | 40 |
| B+ | B+ | B1 | 35 |
| B | B | B2 | 30 |
| B- | B- | B3 | 25 |
| CCC+ | CCC | Caa1 | 20 |
| CCC+ | CCC | Caa2 | 15 |
| CCC- | CCC | Caa3 | 10 |
| CC | CCC | Ca | 10 |
| C | CCC | C | 5 |
| D | DDD | / | 0 |
| | DD | / | 0 |
| | D | | 0 |

Source:
https://en.wikipedia.org/wiki/Bond_credit_rating#Rating_tier_definitions,
which cites this Morgan Stanley publication:
https://archive.li/MLll

## Appendix 3. Ideas for Addressing the Collective Action Constraints of AfDB Governance, in the Spirit of an Open Memorandum to the Shareholders, with a Copy to the President

Governance of the multilateral banks can and has changed. This paper suggests that the African Development Bank would be better positioned for this century if it could move in the direction of the Inter-American Development Bank, retaining its character as a creditor-borrower bank (similar to the World Bank and the other major regional banks), but becoming a 50/50 "mixed" governance bank rather than a borrower-dominated bank (see Table 3 in the text).

In the course of a recapitalization in 1994, the IADB became a 50/50 creditor/borrower bank. That was possible primarily because the United States, a key mover in the founding of that bank, had been willing to sell shares over the years, going from owning over 40 percent of the bank at its founding (37.5 percent of paid in capital, and 41.2 percent of total subscriptions[44]), to 30 percent by the mid-1990s. In doing so, the United States allowed dilution of its majority ownership without giving up its strategic influence as the single largest shareholder. (It also benefited from lower budget outlays at times of recapitalizations.) The freeing up of some owners' shares made it possible for Japan, European countries and other non-borrowers outside the Americas to buy shares, buying disproportionately more shares in "selective" capital increases or recapitalizations, and for some borrowing shareholders in the region to maintain or increase their shares, ensuring the sense of ownership of the bank on the part of its borrowers. Making room for new non-borrowers also opened the door to their making substantial contributions to the concessional window at the IDB, especially for example in the case of Japan in 1994.

Similarly, the World Bank is moving (slowly and fitfully) toward a 50/50 "mixed" governance structure, with its borrowers' shares as a group having increased as at the IADB through selective recapitalizations, so that borrowers now hold about 47 percent of that bank's shares. A relatively small increase in China's percentage of shares in the early 2000s was also accompanied by increases in China's contributions to IDA, the World Bank concessional window.

At the African Development Bank, the starting point is different. In contrast to the other legacy MDBs, the AfDB was founded by its African sovereign shareholders in the post-colonial era as an African bank. Creditor countries joined the bank in the 1970s when the African shareholders saw the need for more capital – and in particular at the time when they saw the need of the poorest African members for access to highly concessional finance (which would not lead to net income from loans) from the world's major donors – the United States, European countries, and Japan. When creditor countries joined the bank, the African borrowing shareholders diluted their shareholding to two-thirds of the total shares,

[44] Inter-American Development Bank, 1996, p36.

retaining their majority ownership. Since then they have permitted a further dilution and now hold 60 percent of all shares.

The African bank's history as African led and owned makes it difficult to give up the majority position of its African members. But since several African members are not borrowers, the AfDB can capture the benefits of a 50/50 governance structure of borrowers and non-borrowers. It is a more difficult change than has been the case at the Inter-American Development Bank, where it was non-borrowers that over time allowed themselves to be diluted. But it is possible, and could bring substantial benefits in confidence and long-run greater financing from major creditors.

Any reduction of African member shares would ideally be concentrated among the smaller borrowing shareholders in favor of the larger borrowing shareholders, in order to increase the capacity of borrowers as a group to cooperate in negotiations with non-borrowers on capital increases and operational issues. (See the text on collective action indicators.) Reducing the vote share of regional borrowers from 60 percent to closer to 50 percent would require extensive haggling between the large borrowers (Nigeria, Ethiopia) and the 46 small borrowers with tiny percentages (less than 2 percent); it could, however, be accompanied by rules guaranteeing to the smallest borrowers other kinds of minority protections, eg in Board seats or as the case at the IADB, a minimal percentage of annual new lending commitments.[45] It would also require considerable leadership on the part of one or more large borrowers (Nigeria, South Africa, Ethiopia, Egypt), in negotiations with a coalition of tiny borrowers (Liberia, Malawi, Burkina Faso); and almost surely leadership on the part of a former or current president.

The logic would be to enable the borrowers as a group to sell up to 10 percent of their shares to current and possibly future non-borrowers – in turn allowing key European donors (the United Kingdom, France, Germany) to increase their combined shares to at least 10 percent as a group, and/or to allow increases on the part of current or new Asian and other sovereign members (China, Korea, Brazil, India) or the European Union, enabling a larger recapitalization than otherwise and in the long term a governance arrangement more propitious for increasing the resources of the bank, while still protecting the interests of borrowers as a group.

As at the IADB and the World Bank, any increase in the shares of creditor country members can be tied informally to increases in their contributions (and overall sense of responsibility) to the African bank's concessional window.

The current non-borrowers also face options. They could agree to consolidate and concentrate their votes; the US and Japan could sell shares to the British, French and Germans, or the British and all EU members could sell most of their shares to a possible new member, the European Union. A group of Europeans, with 15 percent or more

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[45] At the IADB, the smallest borrowers have traditionally been guaranteed 35 percent of the value of all lending, well above their percentage share of GDP in the region, and one chair of 12.

consolidated shares could take leadership in raising resources and making associated demands on management at the Bank. Leadership would have to come from a coalition of non-borrowers in such an effort; at the time of writing, leadership from France or the UK working with Germany and the European Union makes the most sense.

These kinds of changes would require a major and creative effort, with leadership from one or more shareholders in consultation with the Bank's president, or under the leadership of a former Bank president or other prominent African working on behalf of management of a group of shareholders.

In the medium term, the benefits of selective recapitalizations, in which current creditor countries make disproportionately larger investments in the Bank, are straightforward: additional capital and lending in a region where there are critical investment gaps. In the short term, even more important is increasing the size of the concessional window at the AfDB, the African Development Fund, and thus its potential influence in the region's poorest borrowers, including in many of the world's fragile states. Indeed two recent high-level independent panels have made recommendations to deal with the AfDB's small concessional window. The 2016 report of a high-level panel convened by the Center for Global Development[46] recommends "a gradual shift of concessional funds to the African Development Bank" from IDA over the next 10-15 years, given that "the regionally based institution will be better positioned to achieve sustained development progress in the most challenging environments." A 2017 report financed by the Gates Foundation, "Reinvigorating African Concessional Finance", proposed upfront financing to be managed by the AfDB in the form of a special bond issued by European governments and financed by a slightly higher interest rate on concessional loans to countries eligible for the African Development Fund.[47]

[46] Birdsall and Morris, 2016.

[47] Reinvigorating African Concessional Finance, p. 28. This 2017 panel sponsored by a Gates-funded initiative advised donors to consider special upfront financing for the AfDF to better exploit the trust of borrowers in their regional bank, given the need for a tough "enhanced policy dialogue" to attract investment in regional infrastructure. I was one of five members of this panel, supported by a grant from the Gates Foundation. On the proposed bond, see Birdsall and Okonjo-Iweala, as well as the report itself.

## Appendix 4. Top Five Shareholders in Major MDBs by Voting Power, 2014

| IBRD | | IADB | |
|---|---|---|---|
| United States | 15.9% | United States | 30.0% |
| Japan | 6.8% | Brazil | 10.8% |
| China | 4.4% | Argentina | 10.8% |
| Germany | 3.8% | Mexico | 6.9% |
| France | 3.8% | Japan | 5.0% |
| **AsDB** | | **AfDB** | |
| Japan | 12.8% | Nigeria | 9.3% |
| United States | 12.8% | United States | 6.6% |
| China | 5.5% | Japan | 5.5% |
| India | 5.4% | Egypt | 5.4% |
| Australia | 5.0% | South Africa | 4.9% |
| **EBRD** | | **CAF** | |
| United States | 10.0% | Peru | 18.7% |
| France | 8.5% | Venezuela | 18.2% |
| Germany | 8.5% | Colombia | 18.1% |
| Italy | 8.5% | Argentina | 8.9% |
| Japan | 8.5% | Brazil | 7.8% |
| **AIIB** | | **NewDB** | |
| China | 26.0% | Brazil | 20.0% |
| India | 7.5% | China | 20.0% |
| Russia | 5.9% | India | 20.0% |
| Germany | 4.2% | Russia | 20.0% |
| South Korea | 3.5% | South Africa | 20.0% |

Source: Birdsall and Morris (2016, p.47)

## Appendix 5. Table of Collection Action Indicators

| Bank | Borrower status | Herfindahl concentration index | Vote share of top non-borrower | Vote share of top five non-borrowers | Vote share of top borrower | Vote share of top five borrowers |
|---|---|---|---|---|---|---|
| IBRD | Non-Borrower | 389.0 | 16.0 | 34.5 | 4.5 | 14.1 |
| | Borrower | 56.1 | | | | |
| IADB | Non-Borrower | 957.8 | 30.0 | 42.9 | T-11.4[a] | 36.5 |
| | Borrower | 349.9 | | | | |
| AfDB | Non-Borrower | 136.4 | 6.1 | 23.5 | 9.3 | 28.1 |
| | Borrower | 224.7 | | | | |
| AsDB | Non-Borrower | 424.3 | T-12.8[b] | 39.3 | 5.5 | 20.2 |
| | Borrower | 106.8 | | | | |
| EBRD | Non-Borrower | 548.8 | 10.1 | 44.5[c] | 4.0 | 8.2 |
| | Borrower | 23.5 | | | | |
| AIIB | Non-Borrowers plus China | 799.4 | 26.6[d] | 41.2[d] | 7.7 | 21.1 |
| | Borrowers minus China | 124.6 | | | | |

[a] Two-way tie between Argentina and Brazil

[b] Two-way tie between Japan and the United States

[c] Note: The 2nd through 6th vote shareholders (UK, Italy, France, Japan, and Germany) each have 8.6% of the voting rights such that the Top 6 share is 53.1 percent

[d] Counting China as a creditor

Sources: Annual reports and vote share disclosures.