Summary Report
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IDEV conducts different types of evaluations to achieve its strategic objectives.
Executive Summary

Introduction

This report summarizes the findings of the independent evaluation of the African Development Bank’s (AfDB or Bank) Country Strategy and Program in South Africa for the period 2004 to 2015. The evaluation is intended to inform the next country strategy paper (CSP) due in 2018; and to contribute to accountability and learning. To provide solid evidence for its findings, the evaluation included thorough project assessments as well as review of the broader portfolio of strategies and of non-lending activities. It answers questions about how the Bank is managing itself, what it has achieved, and the lessons learned based on what has helped or hindered performance. Finally, it proposes recommendations designed to help the Bank improve its future performance in South Africa.

Overview of key findings

The evaluation found a Bank that is learning to adapt to the developed, competitive South African market. It highlighted the fact that while the scope and scale of Bank operations cannot make a significant national impact, they are nevertheless important for the Bank. The findings showed that the Bank was moving in a relevant direction given its objectives, but that gaps exist in key areas and that ambitions were ill matched to available resources, instruments and demand. The evaluation raised concerns about efficiency (timeliness and processes) and effectiveness (in relation to Bank targets). The findings and conclusions indicate that current policies and practices are inadequate if the Bank wants to remain relevant and grow its portfolio in South Africa. A more tailored approach, appropriate resourcing of the team and a broader menu of innovative funding facilities, are required.

The evaluation themes provide insights for future business development in South Africa, and possibly in other MICs. These include better identifying the Bank’s comparative advantage and competitiveness, the suitability of its financing instruments and activities. The experience in South Africa around energy, leveraging finance, syndication and lines of credit could also serve operations elsewhere.

How the Bank has managed its operations in South Africa

The evaluation found that the Bank set ambitious, relevant objectives. However, it has not been able to deliver on all of them. Objectives were aligned overall to the Bank’s strategic priorities and those of the Government of South Africa (GoSA). However, they did not integrate the important issue of ensuring inclusive growth in a highly unequal society, which is a priority that both the Bank and South Africa have made explicit. The Bank was unable to deliver a portfolio that transformed all its strategic priorities into operations and activities, although the volume of its portfolio grew overall. The Bank did not effectively judge its comparative advantage in the South African context, especially regarding the competitiveness of its private sector finance and the government’s willingness to provide sovereign guarantees. The Bank’s expansion was blocked as a result, particularly in water and transport, as were its capacity and resources to be more than a financier in areas such as knowledge work and capacity development. The portfolio in South Africa focused on infrastructure (mainly energy) and finance by default as much as by design (see Portfolio Focus), which affected the Bank’s ability to produce results across all of the areas that its strategies identified as priorities (see Effectiveness).

The Bank’s approach to partnership has been selective. The focus has been to build a close relationship with the National Treasury (NT), to develop business opportunities rather than to target policy...
changes or to build closer alliances with other development partners (DPs) at the strategic level. Relations with the private sector and other DPs have not been pursued with equal energy. This reflected the limited human resources as well a deliberate, strategic decision about where the Bank was likely to generate business (see Partnerships).

The Bank has sought to innovate in its approach and to leverage additional funding. While the positive examples of leverage did not yet amount to a systematic, fully successful approach they did provide a rich source of learning, highlighted the potential added value that the Bank and its staff can have in this area, as well as management’s interest. Clients acknowledged and appreciated the Bank’s willingness to be the first at the table and to attempt to leverage other finance. With regards innovation, there is scope for the Bank to do more within its operations (see Innovation and Leverage).

The Bank has not realized its aspiration to be more than a financier in South Africa, nor has it added value by generating and sharing knowledge or supporting capacity development. Stakeholders see the Bank as a financier, not as a knowledge producer or supporter of their capacity. Significant strategic ambitions regarding capacity development and knowledge generation and sharing were not resourced, and the Bank did not identify a comparative advantage and the relevant tools or expertise to help it perform in these areas. (See Knowledge and Policy Advice and Effectiveness).

With regards monitoring and managing for results, the picture in South Africa resembled the picture elsewhere. With a few exceptions in infrastructure operations, the focus of monitoring remained implementation and financial data rather than progress towards development results. The advances of the last five years in approaches to monitoring public sector projects have not been mirrored in private sector projects. For example, public sector log frame indicators were more focused and required clearer monitoring data from clients than in the private sector. The approach to understanding and reporting the
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results of lines of credit (LoC) in particular was found wanting (see Managing for Results).

Assessing Bank achievements and performance

The evaluation addressed four standard areas that were rated on the basis of evidence and assessments at project, sector, and country levels. (See Annex B, six-point rating scale). Figure 1 summarizes the ratings for projects comprising 76% of the portfolio. These ratings were a crucial building block for the overall rating (Figure 2). Both project and overall ratings indicate that efficiency and effectiveness were the two main areas of weakness.

The evaluation found the program, its strategies and the individual projects, to be broadly relevant and well aligned with the priorities of the Bank and of the Government of South Africa (GoSA). However, this high degree of relevance in what the Bank was seeking to achieve was not always reflected in the design of the pipeline of operations or individual projects in terms of their appropriateness, quality, and appraisal. Consequently, they were rated moderately satisfactory (see Relevance).

The evaluation of efficiency examined cost efficiency, profitability and timeliness. The picture was mixed. The evaluation found some positive stories in individual projects but there was insufficient information to assess the cost effectiveness of the program as a whole. The story was more negative regarding timeliness: Major delays occurred at various stages of the project process from appraisal through implementation. The factors affecting timeliness were recurrent: long, bureaucratic processes and under-resourcing of task managers and of relevant support department staff (e.g. legal, disbursement, etc.). While there was considerable variation across the portfolio, delay was a perennial issue across the portfolio (timeliness has been poor for small grant approvals (Middle Income Country Trust Fund [MIC TF] and for major project execution). Furthermore, clients and stakeholders, and even Bank staff complained that Bank processes were too slow. The Bank is not perceived to be the nimble partner that South African institutions want, which contributed to an overall efficiency rating of moderately unsatisfactory (see Efficiency).

Effectiveness was considered at output and outcome levels, by the results achieved in the portfolio and in other non-lending activities. The levels of achievement varied by sector. In infrastructure, output delivery was generally solid albeit often late. In the energy sector, for example, project delays, among other things, thwarted the expected increase in power generation to prevent load shedding, which was not averted as planned but projects are on track to deliver the expected level of power at a later date. The picture was more mixed in the finance sector – with considerable variation in project outcomes. Some less well performing projects had inappropriate indicators while others missed the strategy’s outcome focus of developing SMEs. With regards knowledge work and capacity development, high ambitions were not tethered to a solid analysis of the Bank’s comparative advantage, to the existence of appropriate tools or to the necessary expertise or resources. Overall effectiveness was rated moderately unsatisfactory (see Effectiveness).

Sustainability was considered from a financial, technical, environmental, and social perspective. It was found to be less of a concern than in some other country programs, although data was limited. Monitoring reports often lacked the information needed to assess the likelihood of sustainability,
but the lack of environmental and social detail at the sub-project level is acute for LoCs. Nevertheless, based on available information, environmental and social sustainability were judged to be at least moderately satisfactory in most cases. In terms of ongoing profitability, the nature of the finance sector projects was such that the Bank itself took on little risk. However, some loan portfolios included non-performing sub-project loans, although their size was limited in most cases. With regards to infrastructure projects, high technical quality bodes well for sustainability although there was some variation on the environmental side. The environmental impacts of the Medupi Power Station, for example, were especially challenging. The extent to which the CSPs examined sustainability improved somewhat over time. Sustainability was rated as moderately satisfactory (see Sustainability).

Mainstreaming crosscutting issues remained challenging. The Bank’s work in South Africa did not explicitly integrate gender or inclusive growth issues – yet shared growth is a stated priority for both the Bank and GoSA. By contrast, the strategy and portfolio improved over time in terms of considering environmental and green growth issues and compared favorably with other countries. Regional integration was central to the most recent CSPs but was only partially evident in the design of program operations and activities (see Crosscutting issues).

Broader themes based on experience to inform a future approach

Finding the right niche in the South African context. Two interlinked themes emerged with respect to strategy and to finding the right niche for the Bank in the competitive South African context.

First, there was a mismatch between the Bank’s ambition and the resources that it allocated, with respect to its capacity and expertise for developing new business and for achieving objectives such as knowledge generation, capacity development, and gender mainstreaming. The Bank seeks to be more than a financier yet it has not organized itself to make this a reality.

Second, strategic objectives and the planned portfolio were based on an inadequate understanding of where the Bank could add value, including with respect to competitive pricing in local currency in a context where there are few sovereign guarantees and dynamic local bond markets. The Bank has thus fallen into a niche dominated by lending (i) to a small number of SOEs, and (ii) in foreign currency for on lending outside of South Africa. Both areas are valid for continued investment. However, there is only limited room to further expand the Bank’s portfolio if it maintains the same approach.

Striking the balance between good banking and good development banking. The Bank was successful in deploying funds to third countries without taking on risk, through its lines of credit. However, that was rarely an explicit objective of the regional LoCs. In reality, these operations were used to build up an initially slim portfolio and to make inroads into the South African market. The increase in profitable, low-risk lending was generally successful (over the period, the finance sector accounted for over 800 million UA). However, it is much harder to demonstrate success from a development banking perspective of ensuring that funds contributed to inclusive and green growth by creating jobs, etc. Linked to this was the difference between what the Bank argued that it wanted to achieve with its LoCs during appraisal, and what the loan agreements stated. This made it difficult to monitor against original objectives especially where borrowers were unaware of the Bank’s explicit objectives. Furthermore, there was no link with CSP objectives of job creation and small and medium enterprise (SME) support in South Africa in the LoCs that are used only outside the country. Intermediaries were interested in working together to improve results reporting, but the Bank has not yet taken advantage of this mutually beneficial opportunity (see Efficiency and Effectiveness).

Organizing resources and processes effectively and efficiently. The Bank’s decentralization in the
South Africa context has been insufficient: It leaves gaps in capacity, in available expertise, in due diligence and business development. Headquarters did not act upon previous requests to enhance capacity of the Southern Africa Resource Center (SARC). Looking forward, the implementation of the Bank’s new business development model can benefit South Africa program especially if it addresses key bottlenecks in capacity such as business development, disbursement, legal, operations assistance, and (if these remain central to the next strategy) the resources to work on knowledge and capacity (see Knowledge and policy advice). Timeliness, which was identified as one of the weakest areas portfolio-wide, has affected the delivery of results and the Bank’s reputation with clients. Such reputational damage is serious in the South African context given that the Bank is a small player looking to gain ground in a highly competitive market.

Recommendations to improve Bank performance

The evaluation proposes the following recommendations on the basis of its findings and conclusions. Management should consider implementing these recommendations within the next CSP cycle.

1. Initiate steps to ensure that the next CSP is based on a more detailed analysis of the (i) Bank’s comparative advantage and constraints in South Africa; (ii) the resources required to deliver in selected areas of focus. In particular the review could cover:
   - Key areas of new business development and of repeat business, based on a thorough analysis of where and when Bank funding instruments will be competitive. This means resisting pressure to add sectors that may interest the Bank but for which it has no comparative advantage and it means thinking innovatively about competitive funding instruments.
   - Whether or not the Bank has a comparative advantage in (i) knowledge generation and sharing and; (ii) capacity development, and if it does, in what specific areas.
   - Consider a more systematic appreciation of client capacity and options so that the Bank can help develop capacity in the areas that are key to operations delivery.

2. Address the mismatch between the implicit and explicit objectives of LoCs and between appraisals and loan agreements in private sector operations by adopting a more coherent, realistic approach which is also aligned with the objectives of the next CSP. This will require frank discussions with the Board and senior management on the banking/risk-sharing role of LoCs versus their development potential, and designing operations that strike the right balance. All objectives should be stated in the appraisal to allow for a fuller understanding and to acknowledge success with respect to objectives such as risk sharing. Closing the appraisal and loan agreement gap may require more upfront work, but it should reduce the lag that frequently occurs between approval and signature.

3. Build on the South African experience to inform revisions to the Bank’s approach to private sector operation design and monitoring, to allow for better understanding of results. Current project status reports and back to office reports (BTORs) lack information about progress towards development results, which also stems from the initial design and appraisal procedures. The approach for LoCs in particular needs to be revisited to ensure that the necessary reporting data from clients is known upfront and that measurable indicators are used. In South Africa, the Bank has an opportunity to collaborate with existing clients to develop a more robust approach that would benefit both
the intermediary and the Bank by enhancing the ability to understand, track, and report results. A new approach can also draw from experience in the Bank’s public sector supervision revisions and from the International Finance Corporation (IFC) and other partners.

4. **Use the South Africa experience to support the Bank in identifying new flexible funding mechanisms better suited for MICs.** Different types of risk participation may be one avenue to explore, more targeted LoCs may be another. This could be done jointly with a range of departments and be central to the business development strategy.

5. **Ensure a complete decentralization process and business process streamlining.** The experience in South Africa is symptomatic of a broader issue that Bank management is now seeking to address through a new business model. SARC would benefit from in-house disbursement and legal skills and from expertise linked to a given strategic focus (e.g. more business development officers on the group for private sector operations), especially if it wants to continue to pursue the knowledge agenda. In terms of delegating approval authority, the current situation has not allowed the Bank to be the nimble partner it wants to be. The experience of the MIC TF makes it clear that delegating this and other small grant facilities would be an obvious, helpful step.

6. **Share the lessons from South Africa’s experience in the energy sector.** South Africa’s experience in investing and diversifying its energy sector as well as the Bank’s engagement are rich with lessons relevant to other RMCs. Given its continental mandate and its prioritization of energy, the Bank is well placed to facilitate a learning exchange that can cover (i) different types of energy generation; (ii) public and private (independent power producer) roles; (iii) tariff setting and the role of a strong regulator; (iv) contract and project management for new building and refurbishment, and (v) community relations and management in major infrastructure development.
About this Publication

This evaluation examines the African Development Bank’s engagement and support to South Africa, through its programs and strategies during the period 2004–2015. The assessment sought to provide credible evaluative evidence on the development results of the Bank’s assistance. It also identified factors both internal and external that affect good or poor performance while drawing lessons from the performance to inform future operations in South Africa and potentially in other middle income countries. The Bank’s programs in South Africa over the period covered two main pillars: infrastructure (especially energy) and finance (mostly lines of credit). The operations involved the use of both the public and private sector windows of financing. The Bank’s strategies also included emphasis on non-lending products such as knowledge work.

The assessment draws on different sources of information (such as desk reviews, extensive consultation with key stakeholders, and field visits), and uses both qualitative and quantitative analytical methods. Overall, the assessment revealed, among others, that the Bank is learning to adapt to the developed, competitive South African market. The findings and conclusions indicate that current policies and practices are inadequate if the Bank wants to remain relevant and grow its portfolio in South Africa. Hence a more tailored approach, appropriate resourcing and a broader menu of innovative support, are required going forward.