AGENCE FRANÇAISE DE DÉVELOPPEMENT

Strategy

Financial Systems 2018-2022

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Foreword

AFD Group has been supporting the development of local financial systems since the early 1950s. Today, it is one of the leading donors operating in the financial inclusion sector in Africa. The Financial Systems strategy aims to shed light on the Group's current practices and define the new orientations on providing support to local financial systems for the period 2018–2022, within a single strategic document.

We use the expression "financial systems" to denote "all of the rules, practices and institutions (stock exchanges, banks, etc.) enabling the mobilisation of capital in order to make it available to agents with financing needs[1]". This definition makes it clear that the notion of financial system also designates financial operators as well as the authorities that govern their interactions. The Financial Systems strategy resolutely endorses this dual reading. It covers a broad spectrum of possible interventions as long as these are aimed at supporting local financial institutions, changing their financing practices or reinforcing the operating rules of the financial system. This strategy encompasses the operations headed by AFD as well as its subsidiary PROPARCO,[2] which will both be governed by a single strategy defined for the Group as a whole.

The International Monetary Fund (IMF) reminds us that financial operators are diverse: "A country's financial system includes its banks, securities markets, pension and mutual funds, insurers, market infrastructures and central bank, as well as its regulatory and supervisory authorities."[3] This diversity is coupled with the diversity of AFD Group's intervention contexts. The Financial Systems strategy aims to cover the activities that the Group carries out in Africa, the Mediterranean region, Latin America, Asia and the French Overseas Departments and Collectivities. The reader should remain mindful of the diversity of these intervention contexts when this is not explicitly referred to in the text. In fact, the authors of this strategy have endeavoured to emphasise the converging elements that, in their view, warrant the construction of a single strategy in support of developing local financial systems.

As a last point, the approach presented in the Financial Systems strategy proposes an alignment with the French orientations on official development assistance (ODA) set out within the framework of the French Interministerial Committee on International Cooperation and Development (CICID) of November 2016. It is in complete harmony with the 2030 Agenda and as such contributes to achieving the Sustainable Development Goals (SDGs).

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[1] Definition proposed by the French-language Encyclopédie Universalis (http://www.universalis.fr/encyclopedie).

[2] Activities carried out by the Note-issuing institutions are excluded.

[3] Definition proposed by the International Monetary Fund (IMF): Factsheet, "Financial System Soundness", 2016 (http://www.imf.org/en/About/Factsheets/Financial-System-Soundness).

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Executive Summary

Financial systems have undergone profound changes since the outbreak of the global financial crisis in 2008. Many national financial systems narrowly avoided the collapse of their leading financial institutions, now referred to as “systemic” institutions. The review of the regulatory framework for financial operators has led to an upheaval in the sector’s financial and institutional equilibria. In many developing countries, financial systems are still suffering from the consequences of the financial crisis. The ebb of incoming capital and the degradation of macroeconomic conditions in developed countries have had major consequences for developing economies. Because of their intrinsic fragility, financial systems in developing countries have not always been able to withstand this overall deterioration of the economic environment.

> *Financial systems have undergone profound changes since the outbreak of the global financial crisis in 2008.*

Numerous studies have highlighted the inherent weaknesses of financial systems in developing countries. For instance, access to accounting information on clients’ activity and assets is still limited in some sub-Saharan African countries. A lack of trust in financial systems is also a factor that heightens fragility in a good many developing countries. And the financial institutions themselves are not without weaknesses. At the financial level, they are highly exposed to the instability of some resources that are nonetheless crucial to their development. The stability of their deposit base and the availability of long-term funds are key to their sustainability. The shallowness of local financial markets and the low level of sophistication of the products traded do not always allow financial institutions to harness enough savings via investors. At the level of internal organisation, weaknesses appear in the areas of risk management and governance. Risk assessment methods and tools are often sketchy and the financial institutions’ governance of risk is inadequately structured. Some operators have high rates of non-performing loans that they are not always able to cover satisfactorily with respect to international standards. Moreover, the organisation of decision-making, control and incident-prevention processes do not always make it possible to ward off failures.

The regulation of financial activities is also hampered by a number of limitations. In some countries, the share of non-regulated financial activities is substantial and may induce a systemic risk for the sector. The supervisory authority also lacks resources to ensure regular and effective oversight and, if need be, to impose and enforce sanctions.

In a changing financial environment, new financing models are emerging, geared to making full use of the economies of scale opened up by the digitalisation of processes and data. The expansion of digital technologies in the financial sector is leading to changes in the practices of traditional institutions and fostering the emergence of new models. Digital payment systems, the start-up of crowdfunding platforms or the development of “nano-loans” can all offer future prospects conducive to the take-up of financial services in rural areas, provided that they are appropriately regulated.

> *The expansion of digital technologies in the financial sector is leading to changes in the practices of traditional institutions and fostering the emergence of new models.*

Since the early 2000s, support for financial systems has accounted for nearly 20% of AFD Group’s commitments. Among its many counterparties, the Group has more than 150 partner financial institutions present in over 60 countries where the Group is operating. This activity has grown rapidly over the last decade and greatly benefited sub-Saharan African countries (30% of committed amounts). Mostly comprising loans, guarantees and equity stakes, this support to financial systems is typically characterised by the preponderance of financing not backed by sovereign guarantees. In 2016, AFD Group’s activities successfully catalysed local investment to the extent of 2.3 billion euros and supported more than 11,000 small and medium-sized enterprises (SMEs).

To push this approach further and help to build inclusive, sustainable and responsible financial systems, AFD Group has crafted a new intervention strategy based on three priority objectives.

1. **Promote access to financial systems.** This objective must enable improved access to financial services tailored to the constraints of the household or entrepreneur soliciting the services. Access to these financial products must be provided in a way that ensures adequate legal security and transparency so that equitable, lasting and sustainable access conditions are created for the different categories of customers.

2. **Support the emergence of a new sustainable finance model**. This objective must enable the financial systems to play a pivotal role in the economic, social and environmental transitions to come. In the combat against climate change, in education, housing or the opportunities opened up by digital technology for example, financial systems can play an active role in quickening the changes already underway and identifying the most promising initiatives.

3. **Consolidate the financial systems.** This objective must enable support geared to consolidating the internal governance of the financial actors, while reinforcing the underpinnings of the institutional and regulatory framework set for their operations. In fact, guaranteeing the implementation of appropriate regulations, securing financing operations and protecting clients are all missions for which the actors of financial systems also bear responsibility. Further, more

structured financial markets will help financial institutions to diversify their resources.

These three objectives form the basis of AFD Group's strategic vision on support for local financial systems. They are intended to guide operational activities, intellectual output and the advocacy that the Group will construct as of 2018. In line with this vision, the Group has chosen seven priority actions to define its programme of activities. These will serve as discriminating markers for AFD Group's operations until 2022.

1. Serve populations excluded from financial systems

2. Support financing for micro-, small and medium-sized enterprises by diversifying the Group's range of instruments

3. Combine financial support and technical assistance to encourage the development of new financial practices

4. Structure an approach geared to the community of public development banks and which affords AFD Group a lead role

5. Provide the financial actors with resources adapted to their development

6. Establish a structured operational approach to strengthen the regulation of financial systems

7. Support the emergence of new financing vehicles and new tools

All of AFD Group's financing and technical tools will be mobilised to reach these set objectives. Its lines of credit, guarantee tools, equity stakes as well as public policy loans and grants will allow the Group to adapt its operations to national contexts and meet its partners' needs.

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Introduction

Financial systems have undergone profound changes since the outbreak of the global financial crisis in 2008. Many national financial systems narrowly avoided the collapse of their leading financial institutions, now referred to as “systemic” institutions.

To address this crisis, massive public resources needed to be mobilised within a stabilisation and restructuring process which, itself, helped to trigger a cycle of sovereign debt crises. What’s more, the economic stimulus packages put in place failed to produce the expected results and, in developed countries, economic growth only began to bounce back to positive levels ten years after the onset of the crisis. It is doubtless still too soon to take full stock of the changes that the crisis brought about in the financial sector.

> *A number of studies have recalled the key role of financial systems in supporting development dynamics, notably in low- and middle-income countries.*

Yet, the crisis opened up an exceptionally broad-based cycle of reflection and debate: myriad studies have helped to pinpoint the factors capable of triggering and spreading a financial crisis, and its consequences not only for the real economy, growth and employment, but also for the role of central banks or the financial institutions’ economic model.

By contrast, a number of studies have also recalled the key role of financial systems in supporting development dynamics, notably in low- and middle-income countries. Whether this involves supporting a company’s growth or a household’s acquisition of a dwelling, or promoting international transfers, financial systems are one of the essential cogs in the machinery of a modern economy. Credit makes it possible to finance corporate investment and the acquisition of movable or immovable property. In this respect, it helps to support growth of the productive capital and individual wealth of economic agents.[4] It also supports financing for trade and thus enables firms to capture new markets. When savings are insufficient, credit can make liquidities available to clients who are facing unexpected expenses, as, for instance, those incurred by an equipment failure. It also helps to finance services where access costs need to be paid over time. As a result, access to credit remains a major challenge in geographies where the AFD Group operates, particularly in sub-Saharan Africa. According to the World Bank, in developing countries in sub-Saharan Africa, only 16% of companies on average use a bank to finance their investments.

At the macroeconomic level, the function of financial systems is to channel an economy’s available savings into productive investments.

However, in the bulk of AFD Group’s intervention areas, developing economies typically lack domestic savings. These economies are heavily dependent on international savings and thus exposed to the factors that determine how these savings move around the globe (monetary policy in the developed countries, commodity prices, the perception of “emergent” risks, etc.). Concomitantly, schemes for mobilising domestic savings (bank savings products, securities, life insurance, etc.) need consolidating so as to effectively funnel these savings into productive investments. According to the World Bank’s latest Global Findex study, only 15.9% of the over-15s in sub-Saharan Africa had saved at a financial institution in 2014, compared to 51.6% of those residing in an OECD country.[5]

Finally, the activity of financial operators is a full-fledged economic activity. As a relatively labour-intensive service activity, banking generates a substantial share of gross domestic product (GDP) in a number of developing countries.[6] Its contribution to GDP growth is more stable as it is less exposed to fluctuations in commodity prices or export sectors. Furthermore, the financial sector requires highly qualified personnel, which in turn fosters the mobility of professionals working in the sector. Continuing education for the labour force is a crucial challenge for a sector whose model and practices are regularly being renewed. The fact that new players frequently enter the market (microfinance institutions, telecom operators, digital platforms, etc.) indicates that the entry barriers are not so high as to impede the emergence of new models. These new players, who temporarily escape the regulations governing incumbent operators, force the market to regularly take on board commercial, procedural or organisational innovations.

[4] For the current state of the literature relating to the consequences of financial sector development on growth and poverty reduction in developing countries see for example J. Zhuang, H. Gunatilake, Y. Niimi, M. E. Khan, Y. Jiang, R. Hasan, N. Khor, A. S. Langman-Martin, P. Bracey, and B. Huang, "Financial Sector Development, Economic Growth, and Poverty Reduction: A Literature review", No. 173, ADB Economics Working Paper Series, 2009. For a characterisation of the causal link between the development of financial systems and growth, see M. Kabir Hassan, B. Sanchez, J-S. Yu, "Financial development and economic growth: New evidence from panel data", The Quartely Review of Economics and Finance, 2011.

[5] The Little Data Book on Financial Inclusion, World Bank Group, 2015.

[6] The data on the contribution of financial services (banking and insurance) to GDP are still difficult to access, but this sector accounts on average for between 1% and 5% of GDP. For example, it represents 1% in Gabon compared to 5% in Brazil. This sector may account for over 30% of GDP in countries with limited diversification (notably, the Gulf countries).

1.

A DECADE OF PROFOUND CHANGES IN A SECTOR MARKED BY PERSISTENT FRAGILITY

The 2008 global financial crisis served as a reminder that all of the issues linked to the workings of financial systems need to be tackled through a consistent approach. Certainly, a key feature of this economic sector is the interdependence of the financial operators. The financial system is a network of operators that includes notably financial institutions, the central banks, market operators, the regulator and the supervisor. Interlinkages exist between each of these actors, who also weave ties with similar international operators. One actor's vulnerability is likely to have repercussions on the other network members and thus on the whole of the network to which it belongs.

Structural weaknesses hobble the sustainable development of financial systems

Numerous studies have highlighted the inherent fragility of the financial systems in developing countries. These weaknesses impact the structuring of financial operations, the financial institutions that put them in place, and the authorities supervising these institutions.[7]

The role of financial systems is basically to support the readiness of economic actors to plan for the future. Staggering the cost of expenditure, making an investment or building up savings are all steps that cannot be taken with support from financial systems. The relationship of mutual trust forged between financial institutions and their clients is decisive both for the sustainability of economic activity and the smooth running of financial systems. This trust nonetheless remains fragile in a good many developing countries. Several factors of uncertainty may undermine this relationship. To name a few, the ability of financial operators to maintain savings deposits and pay these out when the need arises, the security of financial transactions and the costs these incur, as well as the appropriateness and transparency of credit pricing, for example.

Access to accounting information on a client's activity and assets is still limited in sub-Saharan African countries. The dearth of reliable information on a company's activity, financial results and repayment record, its property assets or the size of its potential market makes it difficult to suitably qualify the associated risk. Informational asymmetry sets an intrinsic limit on financing activity and skews the process of resource allocation.

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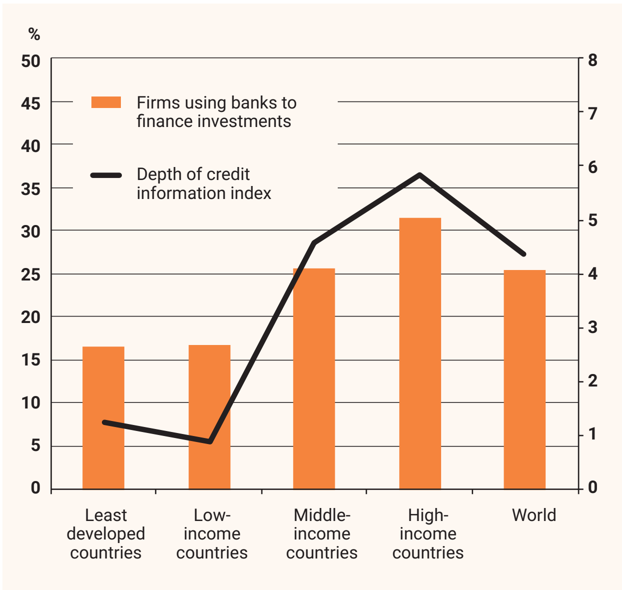
When this asymmetry is too great, the process is entirely hobbled. Viable projects are unable to find funding and, conversely, risky projects obtain finance on terms and conditions that fail to reflect the risk they pose. Moreover, economic actors regularly come up against legal and administrative hurdles when they wish to pursue legal action or enforce a judgement or recover a security for example.

Yet, for financial institutions, the provision of collateral is a crucial component for assessing credit risk, particularly in the case of small and medium-sized enterprises.

Figure 1: Availability of credit to businesses

(Source: World Bank, World Development Indicators)

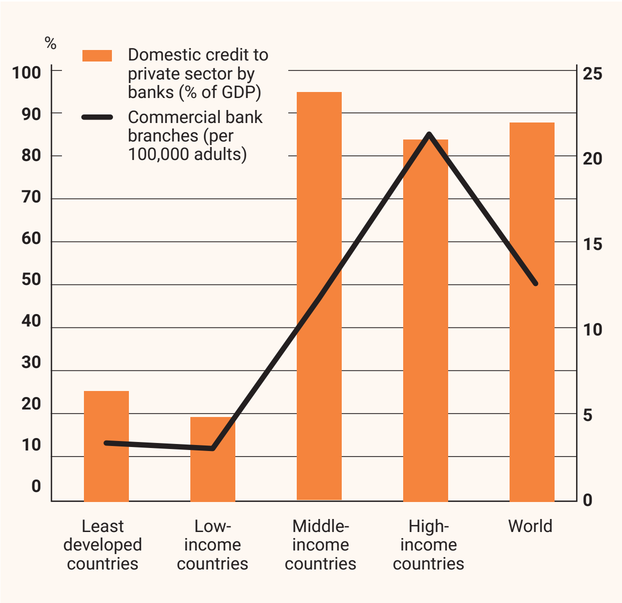


[7] For a general review of the banking sector in Africa, its main weaknesses and ongoing changes, see notably T. Beck, R. Cull, "Banking in Africa", Policy Research Working Paper, The World Bank, 2013 and M. Mecagni, D. Marchettini, R. Maino, "Evolving Banking Trends in Sub-Saharan Africa, Key Features and Challenges", IMF, African Department, 2015.

These different shortcomings skew risk assessment, create price distortions and ultimately result in a sub-optimal allocation of available financial resources. Figure 1 shows that the quality of credit information is still remarkably low in the least developed countries and low-income countries. In these countries, only around 16% of formal businesses use bank financing to finance their investments, whereas in high-income countries this rate exceeds 30%. It is also in these countries that private sector credit is the lowest as a percentage of GDP: it reaches almost 90% as a world average, whereas it does not exceed 20% in low-income countries, for example (see Figure 2).

Figure 2: Depth of the banking sector

(Source: World Bank, World Development Indicators)



Distortions can also emerge when a formal financial system exists alongside informal financial operators. This duality typically entails heterogeneous financial practices (security of savings, recovery, pricing, guarantees, etc.) that lead to a socio-economic segmentation of the market. The lack of any regulatory framework applicable to the informal sector also tends to reinforce this segmentation. While this in itself is not harmful, the segmentation of financial systems can further lock in practices that are sometimes at variance with international standards. In some cases, reforms designed to promote the convergence of formal and informal financial sectors may in fact entail high social costs (liquidation of structures that are unviable even though they are firmly established in some regions, withdrawal of licences, account closures, etc.).

The financial institutions themselves are not immune from vulnerabilities. At the financial level, they have a high demand for long-term resources (equity and debt) to improve their balance sheet, which is very largely composed of short-term funds and receivables (deposits and credits). In some countries, there is also a shortfall of short-term resources needed to meet a fast-growing demand for financing. The availability of financial resources to support the growth of financial institutions is thus also a major challenge in sub-Saharan Africa. Apart from in South Africa, most banking groups have no choice but to call on foreign finance to support their growth. The shallowness of local financial markets and the lack of sophistication of the products traded do not always allow financial institutions to harness enough savings via investors.

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> *The availability of financial resources to support the growth of financial institutions is also a major challenge in sub-Saharan Africa.*

With respect to internal organisation, the areas of risk management and governance show some fragility. Financial institutions inevitably expose themselves to different types of risks depending on the allocation choices that they make, the foremost risk obviously being that the borrower will not repay the financial institution that accepted him as their client. Yet, financial institutions are able to mutualize the risks that they take on. This capacity is crucial to maintaining a financing activity, even though events likely to impact the repayment capacity of some borrowers may occur regularly. In some developing countries, the concentration of economic activity in a few key sectors limits the financial operators' ability to diversify their risk and exposes them to the effects of an overall deterioration of their assets (the fossil energy sector, agriculture, etc.). However, the methods and tools used to assess risks are often sketchy and the financial institutions' governance of risk is inadequately structured. Some operators have high rates of non-performing loans that they are not always able to cover satisfactorily with respect to international standards. The rate of non-performing loans in low-income countries stood at 11% on average between 2004 and 2014, whereas it was only 3% in high-income countries and the world average was 5%. The deteriorating quality of their assets puts a strain on the profitability of financial institutions, which struggle at times to mobilise the expertise and resources required to carry out the necessary organisational and procedural reforms.

In some cases, the governance structures of financial institutions also have vulnerabilities. The composition of their boards of directors, the organisation and mandate of their internal committees, or their decision-making processes do not always allow decision-makers to make decisions that are the most beneficial to the institution they manage. In this setting, the investment strategy of financial institutions is not always clearly defined. Accordingly, a key challenge in some developing countries is to reinforce their internal control, inspection and strategic management functions.

Lastly, the regulation of financial activities suffers from a number of limitations. Although regulations are updated regularly, their scope of application sometimes excludes activities that are nonetheless expanding rapidly (cross-border activities, special-purpose vehicles, digital finance, transfer platforms, etc.). The fast-paced growth of regional financial groups in Africa raises

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the question, for example, of regulatory harmonisation and centralised supervision for this type of actor. In some countries, the share of non-regulated financial activities is substantial and may induce a systemic risk[8] for the sector.[9] Most often, the regulator struggles to adapt in real time to a fast-evolving environment and practices. In parallel, effective enforcement of regulations is still a major weakness in developing countries: in fact, this requires efficient and reliable collection of information, regular controls and, when appropriate, the proper application of sanctions. National supervisory authorities lack the necessary resources to ensure these different tasks. Supervision is often carried out on the basis of systematic administrative control, and too rarely on the basis of upstream risk-mapping. Some supervisory authorities do not have enough resources or leeway to impose a sanction (penalties, withdrawal of license, liquidation, etc.).

Liquidity management in the financial system can also come up against a number of problems in developing countries. In fact, the monetary policy tools used by the central banks to regulate available liquidity in the domestic financial system sometimes see their effects limited by the instrumental or macroeconomic constraints inherent to developing economies. In some particularly fragile developing countries, the central bank's capacity to exercise its mandate to regulate domestic liquidity is heavily dependent on the national and international economic environment. The legitimacy of the central bank, its internal technical capabilities and the appropriateness of its tools may put further brakes on a sound management of liquidity in the financial system. Excess liquidity may arise and cause booms and busts in those sectors with a low absorption capacity (mainly real estate, tourism).[10] Conversely, the credibility of the central bank as lender of last resort sometimes does not suffice to maintain the actors' confidence in the system. The capacity of the central bank to avoid a sudden erosion of liquidity and, more generally, to fight against the spread of a financial crisis, be it of exogenous or endogenous origin, is nonetheless crucial.

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Financial crises: local causes and global consequences

Financial crises in developing countries can spring from different sources. An exogenous price shock may suddenly destabilise a key economic sector (mining, agriculture, etc.) and thus lead to the simultaneous deterioration of a substantial portion of the assets of several financial institutions. When the shock is particularly severe, it can also heighten the fragility of the country's macroeconomic balances. The sensitivity of Nigerian banks' assets to fluctuations in oil prices illustrates this type of vulnerability.[11]Developing economies are also exposed to the sudden withdrawal of international liquidities.[12] These unpredictable and potentially large-scale movements have significant consequences on financial institutions and on the often shallow and illiquid local financial markets. These movements can be driven, for example, by a change in monetary policy in industrialised countries or by a change in the perceived risk associated with often little-known markets. They create problems for short-term refinancing for entities that obtain funding on the international financial markets or from their parent company.[13] Although these phenomena affect the least developed countries to a lesser extent since these are weakly integrated into the global financial system, they do represent an important factor of fragility for middle-income and emerging countries.

Financial crises can also have endogenous roots. They can spring from an economic slowdown or a dynamic of unsustainable indebtedness on the part of public or private agents. In both cases, they materialise as a deterioration in the quality of risky assets held by financial institutions and as a sudden credit squeeze. If the quality of a bank's assets deteriorates, this can lead to its default, and in turn that of its creditors. This sudden erosion of confidence in the financial system may also trigger a massive run on deposits and threaten the liquidity of the financial institutions concerned.[14] Broadly speaking, the 1997

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[8] Systemic risk can be defined as the risk that a given event will bring about a chain reaction with substantial negative effects across the whole financial system, possibly causing a generalised crisis for its functioning. Systemic risk also typically produces heavy negative consequences for non-financial agents.

[9] The IMF regularly recalls the wide extent of non-regulated activities in China's financial system and the underlying systemic risk: see notably "China: Financial System Vulnerabilities – Shadow Exposures, Funding, and Risk Transmission", IMF Country Report – Selected Issues, 2016.

[10] For an analysis of the linkage between accelerated credit growth and financial crisis in developing countries and for a decoding of the 2009 Nigerian banking crisis, see D. Marchettini, R. Maino, "Systemic Risk Assessment in Low Income Countries: Balancing Financial Stability and Development", IMF Working Paper, 2015. For an analysis of how mechanisms for financial information-sharing impact the prevention of credit booms, see notably S. Guérineau and F. Léon, "Information Sharing, Credit Booms, and Financial Stability", FERDI Working Paper, 2016.

[11] For an analysis of the effects of oil price fluctuations on the Nigerian financial market and the role of the exchange rate as a counter-cyclical policy, see notably Terfa W. Abraham "Exchange Rate Policy and Falling Crude Oil Prices: Effect on the Nigerian Stock Market", Central Bank of Nigeria, Journal of Applied Statistics, 2016. For a theoretical analysis of the impacts of a negative commodity price shock on the financial sector in an exporting country, see for example Tidiane Kinda, Montfort Mlachila and Rasmané Ouedraogo, "Commodity Price Shocks and Financial Sector Fragility", IMF Working Paper, 2016.

[12] Movements corresponding to an abrupt halt of capital flows are referred to as "sudden stops", which in turn lead to deep recessions. For a theoretical characterisation, see notably G. Calvo, "Capital Flows and Capital-Market Crises: The Simple Economics of Sudden Stops", Journal of Applied Economics, 1998. For its application to the 2008 crisis, see notably "Quels pays émergents ont été victimes d'un arrêt brutal des entrées de capitaux pendant la crise ?", Direction Générale du Trésor 2010.

[13] For an analysis of the consequences of the interruption of international credit on growth in Latin America, see for example H. Kamil, K. Rai, "The Global Credit Crunch and Foreign Banks' Lending to Emerging Markets: Why Did Latin America Fare Better?", IMF Working Paper, 2010.

[14] For a study of the transmission channels and information conditions that lead to a sudden deterioration of depositor confidence, see for example Martin Brown, Stefan T. Trautmann and Razvan Vlahu, "Understanding Bank-run contagion", Macroprudential Research Paper, European Central Bank, 2014.

financial crisis in Asia or the so-called “subprime” financial crisis in 2008 illustrates the extent to which financial crises can become contagious.[15]

The capacity of public authorities to deploy emergency measures to curtail the expansion of the crisis is still often limited in developing countries. The limited effectiveness of tools for managing financial crises (maintenance of inter-bank liquidity, fight against bank runs, etc.) often makes it difficult to preserve minimal stability in the financial system. In most cases, the depositors’ lack of confidence is heightened by the absence or inadequacy of measures to guarantee deposits. Once the crisis has spread, restructuring the affected assets – which often requires wide-sweeping reform – has a lasting impact on the financial sector’s performance if it is not implemented rapidly. Programmes designed to restructure the sector will only see the light of day if backed by a strong political will, given that they often mobilise hefty fiscal resources.[16]

Fast-paced change in the sector since the global financial crisis

The revision of the regulatory framework for financial operators (banks and insurance) is the most visible change in terms of prudential regulation. The Basel III principles are primarily designed to enhance the quality of the financial institutions’ capital base, to review the risk assessment framework and provide better control over the risks of insolvency and illiquidity, notably for the largest financial institutions.[17] In sub-Saharan Africa, for example, all the banking groups consider that they are Basel I-compliant, whereas less than half consider themselves to be compliant with Basel II standards and about one in five compliant with Basel III.[18] As for the regulation of financial systems, it should also be noted that central bank mandates have been adapted and now include the maintenance of financial stability among their explicit objectives.[19] Although the modalities for exercising this new mandate are still to be defined, this evolution confirms, if any proof were needed, the importance of promoting financial stability in order to maintain economic and social equilibria.

As an extension of these regulatory developments[20] and in a favourable macroeconomic environment (ample liquidity, low interest rates, etc.), thought is now being given to how the liquidity available on financial markets can be more fully mobilised. New market-based products now make it possible to channel the liquidity held by national and international investors seeking economic, social or environmental impacts. Green or social impact bonds are foremost examples of these new investment vehicles designed to funnel this ample and low-cost liquidity into various types of project. The expansion of such vehicles will certainly mean that the eligibility criteria for the underlying investments will need to be standardised at some future time.

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New market-based products now make it possible to channel the liquidity held by national and international investors seeking economic, social or environmental impacts.

Moreover, if these vehicles are to become a permanent feature of the financial landscape, they will doubtless need to send out a truly differentiating signal (price signal) in addition to the favourable signals that they already emit in terms of more sustainable development.

In parallel to these developments, new financing models are emerging, geared to making full use of the economies of scale offered by the digitalisation of processes and data. The Central Bank of West African States (BCEAO) estimates that, in 2014, 34.5% of adults in the West African Economic and Monetary Union (WAEMU) held an account at a formal institution (bank, microfinance institution, savings bank or post office). If users of digital financial services are added to this, the proportion reaches 61.7%.[21] The World Bank’s 2013 *Global Findex Survey* estimated that digitalising financial services would cut their cost by 80–90%. Cash deposit and withdrawal services seem to be the main sources of these cost savings.[22]

[15] For an analysis of systemic risk and a review of the responses that could be envisaged at the level of supervision, regulation and resolution of crises, see notably Jean-François Lepetit, *“Rapport sur le risque systémique”*, La Documentation Française, April 2010.

[16] For an analysis of the restructuring of the Indonesian financial sector in the wake of the 1997 crisis and the lessons learnt for developing countries, see notably M. Pangestu, “The Indonesian Bank Crisis and Restructuring: Lessons and Implications for other Developing Countries”, G-24 Discussion Paper Series, United Nations Conference On Trade and Development, 2003. See also E. Detragiache and G. Ho, "Responding to Banking Crises: Lessons from Cross-Country Evidence", IMF Working Paper, 2010.

[17] For the state of play on changes in regulation and supervision, as well as a comparative analysis of financial systems that were affected or unaffected by the crisis, see for example Martin Čihák et al., “Bank Regulation and Supervision around the World: A Crisis Update”, Policy Research Working Paper 6286, World Bank Group.

[18] See EIB, “Banking in sub-Saharan Africa”, November 2016.

[19] For a review of the stakes linked to the evolution of the central banks’ mandate in the wake of the global financial crisis, see notably “Issues in the Governance of Central Banks”, a report drafted by the Central Bank Governance Group, Bank for International Settlements, 2009.

[20] For a review of the consequences of the Basel III reform relating to the restriction of the activity of financial institutions and for an identification of their strategies in response to higher capital requirements, see for example M. Andrle, V. Tomšík and J. Vlček, “Banks’ Adjustment to Basel III Reform: A Bank-Level Perspective for Emerging Europe”, IMF Working Paper, 2017. For an analysis of the consequences of the challenges of Basel III in developing countries and emerging markets, see for example the Basel Consultative Group “Impact and implementation challenges of the Basel framework for emerging market, developing and small economies”, Bank for International Settlements, 2014.

[21] See CGAP, “Market System Assessment of Digital Financial Services in WAEMU”, Working Paper, 2016.

[22] See notably R. Voohries and J. Lamb, “Fighting poverty, Profitably”, Bill and Melinda Gates Foundation, 2013.

One possibility proposed by emerging models brings a potential investor closer to a project-owner via a crowdfunding platform. The investor makes his own choice on the platform, which enables him to contribute to funding a project through a grant, loan or capital injection. Other financial service operators use digital technology to offer their clients the possibility of managing a mobile wallet to make electronic transfers or secure online payments, with no cash being exchanged. As a result, telecom operators have broken into the retail finance market by mobilising their subscriber networks. Apart from the mobile phone or telecom operators, e-money issuers, retailers or post offices can also become digital finance providers.

> *As a splendid opportunity to extend access to credit, changes in digital finance nonetheless raise questions regarding transparency, regulation and client protection.*

The development of digital finance[23] is also sparking key changes within traditional financial institutions. The financial institutions are developing a raft of services and applications for their clientele. These tools make it possible to reach populations in remote areas and thus make up for the sparse coverage of branch networks.[24] Digitalisation (automatic credit rating, knowledge about the client, etc.) also helps to reduce the operational costs of some processes.[25] This cost reduction facilitates the launch of new products that previously lacked the characteristics to ensure minimal profitability. The development of the "nano-loan" is part of this dynamic and allows financial institutions to reach new population segments by proposing more attractive financial conditions. As a splendid opportunity to extend access to credit, these changes nonetheless raise questions regarding transparency, regulation and client protection.

[23] Digital finance is defined as the offer of digital financial services (DFSs), delivered through mobile telephony or an automated teller machine (ATM). This offer includes digital services for transfers, payments, e-money, savings, insurance and credit.

[24] For a demonstration of the positive link between the growth of digital transactions and economic growth, as well as wider, more transparent and diversified access to financial services, see for example the World Bank Development Research Group, "The Opportunities of Digitizing Payments: how digitization of payments, transfers and remittances contributes to the G20 goals of broad-based economic growth, financial inclusion, and women's economic empowerment", Better Than Cash Alliance, Bill & Melinda Gates Foundation, 2014.

[25] On this count, in addition to the increasing development of financial services, digital credit has grown substantially in recent years. Credit risk is automatically assessed using available digital data (mobile phone records). Several questions remain unanswered and need to be addressed through new standards (prerequisites for delivery of credit, minimal access to telecom infrastructure, limitation of risks for the client, etc.). For an analysis of the functionalities of digital credit, see, for example: B-H Hwang and C. Tellez, "The Proliferation of Digital Credit Deployments", CGAP, 2016.

2.

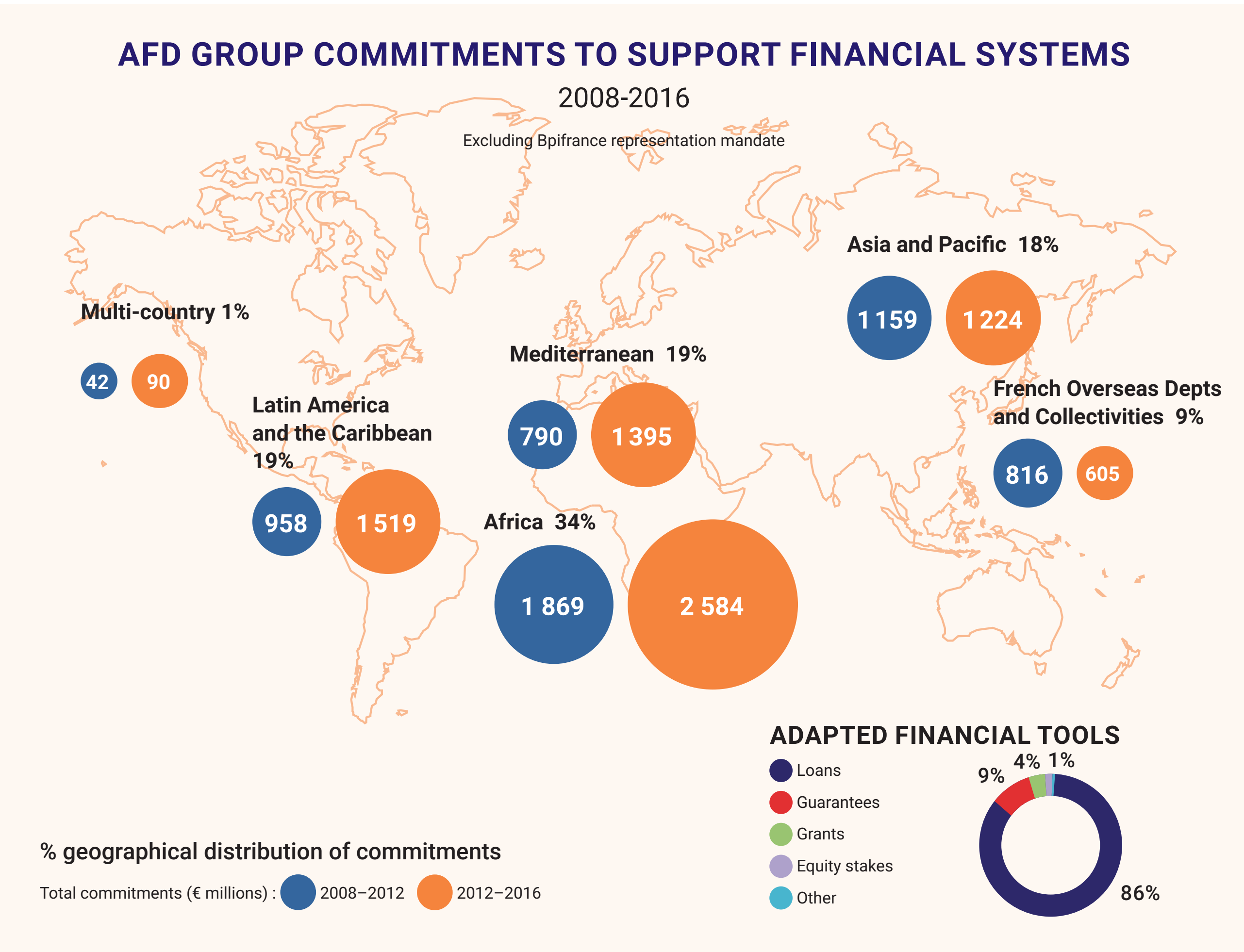
AFD GROUP, TOGETHER WITH LOCAL FINANCIAL SYSTEMS, HAS BUILT EFFECTIVE RESPONSES TO THE CHALLENGES OF SUSTAINABLE DEVELOPMENT

A dynamic activity focused on continental Africa

AFD Group's activity in support of financial systems has averaged 1.2 billion euros in annual commitments since 2008 (see the map below). It grew rapidly over the last decade with a 40% rise between the periods 2008–2012 and 2012–2016. This growth was particularly strong in sub-Saharan Africa (+38%), Latin America (+59%) and the Mediterranean region (+77%). The high degree of capital market structuring in Asia limits de facto AFD Group's activities in this region, which increased by no more than 6% over the period.

The geographical distribution of operations reflects AFD Group's intervention priorities. Sub-Saharan Africa concentrates over 30% of committed amounts. The activity is then equally distributed across the Mediterranean, Latin America and Asia, at around 20% each. The activity in French Overseas Departments and Collectivities represents 9% of the Group's activity but continues to show relatively strong fluctuations; the liquidity conditions in the different overseas intervention areas greatly influence AFD Group's involvement.

Loans are the main tool mobilised by the Group in support of local financial systems (on average, 85% of committed amounts). In sub-Saharan Africa, grant and guarantee tools are often mobilised in conjunction with the loan tool. Guarantees represented on average 21% of commitments in sub-Saharan Africa between 2012 and 2016. Grant commitments remained relatively low (4% of total commitments, equivalent to an annual 50 million euros on average) but their catalytic role is crucial. Grant funding is focused on countries that are a priority for French assistance, notably in West and Central Africa, fragile countries, the Maghreb and some Asian countries.



Direct financing of local financial institutions – AFD Group's innovative positioning

Over the past ten years, AFD Group has developed a direct financing activity to benefit local financial institutions. Whether in the form of loans or guarantees, this activity is an important hallmark for the Group's identity with respect to other donors. This activity makes it possible to tailor financing operations to the needs of local actors and, in partnership with them, to build programmes targeting specific client categories. By working directly with these clients and supporting their financial autonomy, this type of operation also helps to establish long-term trust among the partner financial institutions and build in-depth knowledge of the dynamics inherent to local capital markets. AFD Group works directly with upwards of 150 private and public financial institutions in over 60 countries for a total level of exposure in excess of 5 billion euros at the end of 2016 (see the figure below).

> *AFD Group has developed a direct financing activity to benefit local financial institutions.*

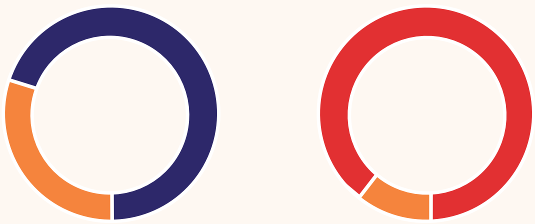
AFD

DIRECT FINANCING TO FINANCIAL INSTITUTIONS
End 2016

32 geographies

104 partner financial institutions

€3bn exposure



30% Private financial institutions*

70% Public financial institutions*

19% MFIs**

81% Banks**

*in volume

** in number of counterparties

PROPARCO

HIGHLIGHTS IN 2016

€400m Committed to financial institutions

Nearly **160** Partner financial institutions

+60 Intervention countries

€200m Committed to climate change

23 New projects

DIRECT FINANCING TO FINANCIAL INSTITUTIONS

€2.3bn exposure

€32m invested in dedicated investment funds

€200m exposure (equity & Tier 2)

A catalytic effect to achieve the Sustainable Development Goals

The programmes deployed by AFD Group have helped to channel investments towards the sustainable development goals. Through its range of tools, AFD Group was able to catalyse 2.3 billion euros of private investment in 2016. In particular, AFD Group supported financing for local productive sectors mainly composed of small and medium-sized enterprises. On average, more than 12,000 SMEs benefited from AFD Group financing each year between 2014 and 2016.

The programmes deployed by AFD Group have helped to channel investments towards the sustainable development goals.

Through its dedicated lines of credit, AFD Group also contributed to adapting the energy mix and funding the agricultural and rural sector in its partner countries. Around 1,200 farms received indirect funding from AFD in 2016. Financing from AFD Group also helped to install new capacities for renewable energies, finance energy efficiency and connect numerous households to the power grid. For example, in 2016, more than 180 megawatts of additional renewable energy capacity were installed thanks to the financial and technical support programmes provided by AFD Group. The figure below summarises all of these contributions between 2014 and 2016.

SOME OF THE IMPACTS

DEDICATED CREDIT LINES AND ARIZ GUARANTEES (AFD)

	2014	2015	2016
Amount of investments supported in the private sector (€ millions)	631	1 155	1 903
Number of companies (SMEs) having received AFD support or financing	10 664	15 553	11 108
Number of family farms supported by AFD-funded programmes	na	na	1 200
New installed capacities of renewable energies (MW)	20	238	187
Number of individuals connected to the power grid or with access to electrification	na	2 565	17 000

AFD indicators

New tools tailored to the needs of partner financial institutions

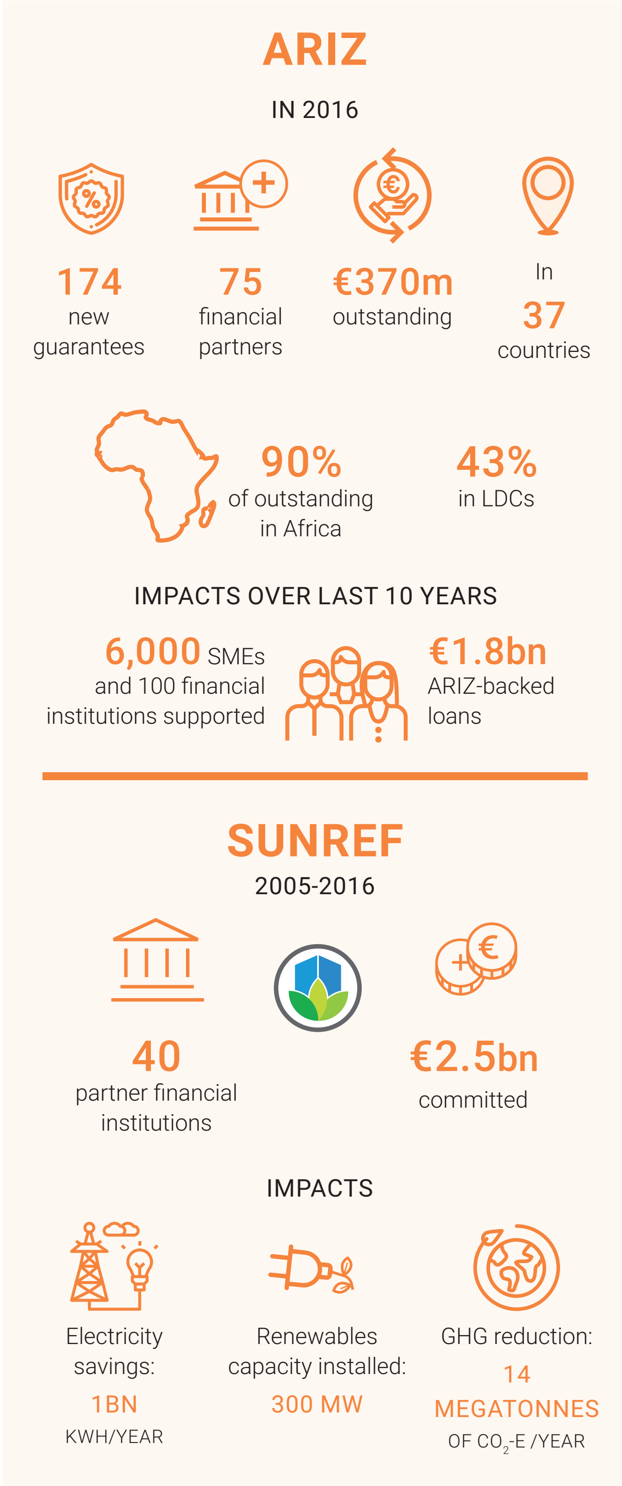
To deliver the best support to its partner financial institutions, AFD Group has developed financial and technical tools that target specific beneficiary categories or specific investments.

For instance, **ARIZ** is a risk-sharing facility designed to facilitate access to finance for micro-, small and medium-sized businesses, professionals and microfinance institutions (MFIs). By offering financial institutions a range of guarantees, ARIZ aims to promote the creation and development of companies and MFIs, and thereby stimulate the growth of a dynamic production base.

This support instrument enables:

- businesses, ranging from small craft businesses to structured SMEs, to more easily obtain investment loans in local currency,
- banks to: (i) reduce the risk incurred, (ii) increase their portfolio of loans to MSMEs without having to bear a foreign-exchange risk, and (iii) improve their solvency ratio thanks to AFD's rating,
- microfinance institutions to access banking resources more easily.

> *By offering financial institutions a range of guarantees, ARIZ aims to promote the creation and development of companies and MFIs.*



At the end of 2016, over 70 financial institutions had benefited from the ARIZ guarantee facility in 37 intervention countries (see the accompanying figure). Ninety per cent of ARIZ guarantees were granted in Africa.

AFD Group has also designed **SUNREF** (Sustainable Use of Natural Resources and Energy Finance), a product aimed at developing the financial systems' capacity to support the ecological transition and the fight against climate change. To promote investment in renewable energies, energy efficiency and depollution, the SUNREF product combines a financial and technical approach. The financial side involves making long-term resources available to local financial institutions through sovereign or non-sovereign loans. The barriers to investment and the depth of the "green" finance market are analysed to ensure that the financial conditions attached to these loans are suitably adapted. In addition to the loan offering, a financial incentive scheme involving, for instance, investment premiums can complement this tool. These premiums, paid to different market actors, help to trigger the investment decision and reduce the overall cost of the targeted investment.

On the technical side, the purpose is to offer market actors technical assistance to support the maturing of "green" projects. Depending on circumstances, it can provide project owners with support both for the development of their investment plan and for the period when the project is maturing (feasibility studies, funding applications, equipment certification, etc.). It can also assist banks to further fine-tune their credit procedures, build

> *To promote investment in renewable energies, energy efficiency and depollution, the SUNREF product combines a financial and technical approach.*

dedicated financial products or develop their commercial strategy to promote the marketing of a "green" credit offering. In addition, it can support local technical partners (engineering firms, technical agencies, consultants) in developing a local supply of high-quality technical expertise to support project owners and banks. Lastly, it can support local authorities in their role of regulating the market for "green" investment financing (equipment certification, the setting-up of an enabling regulatory framework, controls, etc.). Since 2005, SUNREF has been rolled out in some forty financial institutions and has helped to avoid the emission of 14 million tonnes of CO_2 equivalent (see figure).

Lastly, **the Financial Inclusion Facility** enables AFD Group to intervene in fragile situations to support financial institutions, primarily those microfinance institutions keen to develop activities that benefit vulnerable populations. This Facility, backed by grant resources, helps to set up financing and technical assistance programmes for AFD Group partners and involves an average 12 million euros a year. These programmes can be funded by grants or local currency loans. Importantly, the Financial Inclusion Facility has enabled financial support to income-generating activities in rural areas and agriculture. It has also helped to support innovative initiatives that fund housing and sanitation or education and health. The Financial Inclusion Facility has also delivered support to develop health micro-insurance and digital finance, for example. Lastly, it has provided support for the modernisation of the regulatory and prudential framework for microfinance.

Between 2004 and 2016, 70 projects were financed by the Financial Inclusion Facility. These projects directly benefited 36 MFIs in 20 countries, as well as national structures promoting or supervising this sector in 7 countries. The Financial Inclusion Facility has allowed AFD Group to position itself as a landmark donor in the area of financial inclusion. Its flexibility has made it possible to develop operations that are adapted to the most fragile contexts and to assist partner MFIs in adapting to the different challenges they are facing (extended geographies, skills enhancement, digitalising processes, etc.).

Continuous improvement for AFD Group's operations

The programmes implemented by AFD Group are regularly and independently evaluated ex post. This means that achievement of development results can be measured and, if necessary, the structure of future operations can be adjusted. These evaluations have highlighted the following factors for improvement.[26]

The importance of capacity-building

When the Group's operations set out to transform the practices of the financial actors, they can more easily attain their objectives if a tight linkage exists between the financing and capacity-building components. Any time lag when implementing these components impairs the programme's effectiveness. As far as possible, the capacity-building component should benefit the financial partner and the ministries or technical structures associated with the programme. When the programme aims to serve particularly vulnerable categories of population, the capacity-building component should also be able to benefit these client segments.

Selection of financial partners

Among the lessons learned from the ex post evaluations, the profile of AFD Group's partner financial institutions is another point deserving attention. Often AFD Group's partners are institutions with relatively low-risk profiles. They are frequently backed by international banking groups. This positioning allows AFD Group to mitigate its risk-taking but sometimes limits the deployment of programmes in underserved or unserved areas (rural areas) or for populations excluded from financial systems. AFD Group must to be able to work with financial partners that have the most extensive territorial network possible and which are directly in touch with clients in reputedly riskier categories (SMEs, informal sector, rural areas, etc.).

Provide associated support to advance the regulatory framework and public policies

A third observation is that AFD Group would benefit from a more systematic structuring of programmes that support financial system regulators. In addition to its direct financing operations, AFD Group should be able to support the modernisation of the regulatory framework applied to the financial institutions with which it works. Although AFD Group's mandate did not until recently allow for the deployment of proactive actions in the area of governance, the Group's action to support regulation of microfinance activities in the Maghreb and in West Africa has been commended. The evaluations confirm that this type of support, in conjunction with funded projects, fosters the achievement of objectives aimed at systemic transformation (restructuring of the financial system, changes in the actors' practices, improved resilience, etc.).

[26] See notably B. Crépon, F. Devoto, E. Duflo and W. Parienté "Evaluation de l'impact du microcrédit en zone rurale au Maroc", (2012), and J.-D. Naudet and S. Oktar, "Méta-évaluation des projets 'Lignes de crédit'", (2012).

Additionality and impacts

The ex-post evaluations also highlight the importance of the way in which support programmes for financial systems are structured at the outset. The questions of additionality and subsidiarity, in particular, are points that require constant vigilance. The introduction of a grant component must go hand in hand with lasting changes in the partner financial institution's practices. The grant component may also help to speed up financing for specific investments or serve those client segments that are averse to seeking resources from the financial sector. In all cases, these programmes should be closely monitored so as to avoid any deadweight effect.

Finally, financial system support programmes exhibit specific features that must be taken into account by the evaluation framework for these programmes. Some development results are not systematically reviewed for want of an adapted methodology (transformation of the partner financial institution, spill-over effects resulting from the financial incentive scheme, multi-actor aspect of the programmes, etc.). AFD Group will contribute to any reflection that could lead to improving the robustness of methodology for evaluating financial system support programmes.

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> *The introduction of a grant component must go hand in hand with lasting changes in the partner financial institution's practices.*

3.

AN OVERARCHING STRATEGY FOR FINANCIAL SYSTEMS

To extend the actions already underway, AFD Group intends to set its support to financial systems at the core of the responses that it wants to bring to the challenges of sustainable development. **For the period 2018–2022, the strategy to support financial systems has the overarching goal to contribute to building inclusive, sustainable and responsible financial systems.** The intervention strategy will be structured around three priority objectives. These three objectives must enable the Group to support those of the sector's changes that make the most substantial contributions to mitigating vulnerabilities of individuals, promoting a more sustainable development and consolidating the financial systems.

Access: Promote access to financial systems

This objective must help to promote access to financial services adapted to the needs of the household or entrepreneur soliciting them. Access to this financial offering must be under conditions that provide a level of legal security and transparency sufficient to create the conditions for equitable, long-term and sustainable access for different client categories.

Transition: Support the emergence of a new sustainable finance model

This objective must enable financial systems to play a pivotal role in the economic, social and environmental transitions to come. In the combat against climate change, in education, housing or digital technology, for example, financial systems can play an active role in quickening the changes already underway and identifying the most promising initiatives.

Consolidation: Consolidate the financial systems

This objective must contribute to supporting the development of the financial actors, while consolidating the underpinnings of the institutional and regulatory framework in which they are operating. In fact, guaranteeing the implementation of adapted regulations, securing financing transactions and protecting clients are all missions for which the actors of the financial systems also bear responsibility.

All of AFD Group's operations will be undertaken in line with the principles of financial operators' responsibility, of transparency and of client protection. The box (p. 39) describes the policy relating to the financial intermediaries' responsibility, which is a policy that AFD Group applies to its operations in support of local financial systems

> *AFD Group intends to set its support to financial systems at the core of the responses that it wants to bring to the challenges of sustainable development.*

Access: Promote access to an adapted and diversified financial offer

Orientation 1

Encourage financial intermediaries to offer households solutions enabling them to access essential services and guard against economic shocks

With respect to financial services, the needs of households in developing countries relate to keeping and accessing liquidities (deposits, current accounts), to payment facilities and short- or long-term credit enabling them to stagger a large payment or smooth the seasonality of some of their income. These resources help households to access essential services providing basic necessities such as energy, water, housing or health and education services. In sub-Saharan Africa notably, a broad swathe of the population is still excluded from formal financial services; only 34.2% of the population had access to an account in 2014 – including 29.9% of the female population – which is barely half of the world average, which stood at 61.5% that same year.[27] What's more, the territorial network is largely deficient, which makes it difficult to provide the rural world with an adapted product offering. Coverage is better in urban areas, but accessing a loan to cover expenses that are not directly productive (housing, healthcare, school fees, etc.) still greatly depends on the borrower's capacity to provide adequate repayment guarantees (mortgages, a steady income, formal-sector activity, etc.).

> *In sub-Saharan Africa, a broad swathe of the population is still excluded from formal financial services. Only 34.2% of the population had access to an account in 2014, which is barely half of the world average, which stood at 61.5% that same year.*

[27] Global Findex, World Bank Group, 2015.

AFD Group will propose support to financial intermediaries wanting to diversify their service offering to the benefit of essential services, such as housing, energy, water, health or education. Additionally, AFD Group will support its financial partners wanting to broaden their scope of action to remote areas where financial system coverage is scarce or absent. AFD Group also has a role to play in facilitating the construction of a financial offer to benefit the most vulnerable populations. In the framework of the operations undertaken for the benefit of these recipients, AFD will seek to promote financial operator responsibility principles and client protection principles as laid out by the Smart Campaign, for example (transparency, responsible pricing, mechanisms for complaint resolution, etc. See box on p.39). In addition to savings and credit products, AFD Group will support the development of a guarantee, insurance and micro-insurance offering in priority sectors delivering basic necessities.

> *AFD Group has a role to play in facilitating the construction of a financial offer to benefit the most vulnerable populations.*

Orientation 2

Encourage financial intermediaries to support enterprises at all stages of their business development

According to a survey conducted by the International Finance Corporation (IFC), the estimated financing gap for MSMEs in developing countries stood at between USD 2.1 and 2.6 trillion in 2013, equivalent to 30 to 36% of outstanding credit to this segment. The study also estimated that between 200 and 245 million formal and informal enterprises had limited or no access to loans or overdrafts.[28] Micro-, small and medium-sized enterprises still largely fund their productive investment using own resources. In this context, the modernisation of equipment to adapt to new standards or changes in demand is often not implemented at a fast-enough pace. Companies struggle to grasp the opportunities offered by the opening-up of new markets, integrate new value chains and, in the long run, ensure the sustained profitability of their business and create jobs.

Moreover, the financial offer for companies in their seed or start-up phase is often very limited in AFD Group's countries of operation. In fact, the instruments that support research and private-sector innovation, venture capital or private equity investment, although making strong headway, are still underdeveloped. The projects are seen as too risky for the banking sector, which does not tailor its guarantee requirements to maturing companies. This nascent productive fabric nonetheless holds key potential for creating skilled jobs, diversifying the economy and stabilising incomes for urban populations. To support the consolidation of this productive fabric, what is needed are financing tools tailored to the needs and the risk profile of these entrepreneurs (debt, "patient" capital, guarantees, advice, etc.).

Finally, access to financial systems for small and medium-sized enterprises remains hobbled by a number of administrative and regulatory prerequisites (registration, authorisation, production of financial accounts, etc.), and it is the public authorities alone that can soften the induced exclusionary effects of these requirements. According to the World Bank, only 20% of formal enterprises in sub-Saharan Africa and 22% in East Asia and the Pacific used a bank to fund their investments in 2015, compared to 30.5% of enterprises in OECD member countries.[29] The removal of administrative, legal and technical obstacles that still constrain small companies' access to finance can only be achieved through a proactive public policy in support of financial inclusion. Organising activities into sectors or value chains will also help to consolidate the creditworthiness of entrepreneurs and facilitate the financing of an entire economic sector (in agriculture, for instance).

By acting simultaneously on the financial products for companies, on public policies fostering financial inclusion and on the demand from potential clients for financial services, AFD Group will strive to promote the development of a financial offer tailored to the needs of companies, particularly the smallest. AFD Group also sets itself the ambition to support the integration of local companies into international trade. This support will notably entail supporting financial institutions that develop trade finance tools.[30]

> *AFD Group will strive to promote the development of a financial offer tailored to the needs of companies, particularly the smallest.*

[28] P. Stein, O. Pinar Ardic and M. Hommes, "Closing the credit gap for formal and informal micro, small, and medium enterprises", International Finance Corporation, World Bank Group, 2013.

[29] World Development Indicators, World Bank Group.

[30] "Trade finance" is the term used to denote documentary remittance, documentary credit as well as the related international guarantees.

AFD partners…

The Social Performance Task Force (SPTF) is a non-profit organisation based in the United States whose mission is to promote good practice in social performance management for microfinance.

Created in 2005, in 2017, the SPTF had over 3,500 members from all inclusive-finance stakeholder groups (financial and technical service providers, associations, investors, consultants, audit agencies, etc.).

The SPTF groups together the main initiatives geared to client protection and social microfinance audits (Smart Campaign, CERISE, TrueLift, rating agencies, etc.). In 2012, the SPTF launched the Universal Standards for social performance management, a comprehensive set of standards and good practices designed to help financial service providers place their clients at the centre of their strategic and operational decision-making.

While the approach is today focused on the microfinance sector, the intention is to broaden it out to include all financial systems. The SPTF is a key partner for AFD, who has had a seat on its Board of Directors since 2016. AFD gives the SPTF financial support, mainly through the "Responsible Microfinance Facility", a technical assistance facility headed by the SPTF in collaboration with the Smart Campaign and designed to strengthen the capacities of microfinance institutions in managing their social performance, mainly in Africa.

The Consultative Group to Assist the Poor (CGAP) is a trust fund that brings together all public and private funders active in the area of financial inclusion in developing countries. The CGAP has 37 members including bi- and multilateral agencies (World Bank, IFAD, UNDP/UNCDF, European Commission, the French, British, German and other country cooperations, etc.), international finance institutions (AFD, EIB, IFC, FMO, and KfW), development banks (AfDB, ADB, EBRD) and private foundations (Gates, MasterCard). The CGAP has three key roles assigned to it:

i) contribute to shaping norms and standards in the microfinance sector and advising donors, governments and finance institutions on their implementation,

ii) provide information and analyses of sectoral data through research programmes and publications,

iii) support and test new initiatives that spur innovation.

The CGAP is a major forum for dialogue on the subject of financial inclusion in developing countries: a locus of influence, sharing and dialogue in the field of financial innovation at the service of development, it is the main platform for coordinating and monitoring emerging trends in this domain. AFD is founding member of CGAP, contributes to its funding and sits on its executive committee.

Transition: Support transformation of the financial actors' practices to promote a sustainable finance model

Orientation 1

Contribute to the development of financial systems so that they can play a pioneering role in the transition towards sustainable finance models

As current growth models over-consume raw materials, particularly fossil fuels, they are producing a diversity of irreversible economic, social and environmental damage. Climate change is one example of damage whose consequences are visible on a planetary scale. Moreover, these development models exhibit myriad fragilities (wealth inequality, poverty, conflict situations, etc.) that public policy and international solidarity are struggling to attenuate. Yet, most economies still depend on fossil resources for power generation and transport. According to the World Bank, the share of fossil fuel-based energy consumption in 2013 was 98.6% for countries in the Middle East and North Africa, 74.2% for countries in Latin America and the Caribbean and 38.8% for countries in sub-Saharan Africa.[31] The Paris Climate Agreement signed in 2015 evidences a broad consensus among States on the unsustainable nature of these models. Furthermore, these development models raise geopolitical and humanitarian challenges. The weakening of some States, the persistence of income inequality and the entrenchment of international terrorism in some regions where there is little or no administration are fuelling health-related, social and political crises of major importance.

Given the role that they play in promoting development dynamics, financial systems bear a crucial responsibility to support the

[31] World Development Indicators, World Bank Group.

shift in current growth models.[32] The transition to be carried out must involve funding practices not only for infrastructure, trade, productive sectors and housing, but also and notably health and educational systems. It must promote more sustainable consumption models, more environment-friendly modes of transport and foster the development of digital tools. It must also help to reduce social and gender inequality, promote more stringent social standards in the workplace[33] and lessen the degree to which communities are exposed to economic, social and environmental shocks.

AFD Group is already supporting financial institutions in developing countries that wish to promote more sustainable development models. It assists them in diversifying bank products for sectors such as renewable energies and energy efficiency, sustainable agriculture, water or sanitation. AFD also supports its partners when it comes to implementing strategies dedicated to the fight against climate change and to measures for adapting to its consequences. It also supports its partners in establishing and implementing systems to manage environmental and social risks for the projects they finance.

In contexts where these social, economic and environmental shifts are not yet or only partially in progress, AFD will support its financial partners in launching a transition towards less resource-intensive and more resilient development models. It will do this by supporting pioneering financial institutions, and also seeking to engage a dialogue with the public authorities. It will be particularly attentive to whether a set of favourable indicators exists conducive to triggering a decisive shift in the growth trajectory of the countries concerned (choice of intervention sectors, commitment of the public authorities and the financial system, etc.).

> *AFD will support its financial partners in launching a transition towards less resource-intensive and more resilient development models.*

> *Given the role that they play in promoting development dynamics, financial systems bear a crucial responsibility to support the shift in current growth models.*

Orientation 2

Support financial systems to ensure an accelerated transition towards sustainable development models

Financial systems are ideally placed to give direction to investment dynamics. Using different channels (political, monetary, pricing and guarantees, investment selectivity, etc.), they must be able to send sufficiently clear and incentivising market signals to foster the emergence of some emblematic investment categories. Large-scale funding of these new investment categories and the redirecting of private and public financial flows will not come to pass without a change in the investment priorities of the key national and international finance institutions.

The formulation of these new investment priorities must be able to rely on the emergence of an incentive-driven regulatory environment. Sectoral public policies are, of course, an important vector for attracting investment flows. These policies must contribute to clarifying the legal framework for investment, mitigating the technical and financial risks inherent to investment and, if necessary, putting in place financial incentives (tax-related measures, grants, etc.).

Setting a new direction for investment priorities also depends on the evolution of financial operators' procedures and processes. The tools enabling lasting modification of the nature and characteristics of funded investments include systematically applying environmental and social criteria to project selection and designing internal scoring systems for projects (introduction of non-financial criteria linked to climate, social impacts of projects, for example).

Beyond project financing, mainstreaming these new financing tools also requires the implementation of awareness-raising actions for economic and political actors on the one hand, and for the general public on the other. In fact, some of the challenges have such a political and societal resonance that no shift in current development models can take shape without commitment from the political and social spheres.

[32] See for example the speech of M. Carney, governor of the Bank of England and chairman of the Financial Stability Board, "Breaking the Tragedy of the Horizon – climate change and financial stability", September 2015.

[33] AFD Group supports, for example the Turkish bank Türkiye Sinai Kalkinma Bankasi (TSKB) to further companies' compliance with Turkish regulations in health and safety at work, and also to raise the awareness of firms, particularly SMEs, on issues relating to women's employment and gender equality in the workplace.

To sustain the momentum of this transition, AFD Group will support financial operators wanting to modify their investment strategy so as to produce a multiplier effect and thus promote the mainstreaming of new financing practices. AFD will support operations geared to key financial actors wanting to develop their internal analytical and decision-making processes. AFD will also support operations aimed at strengthening public policies designed to facilitate emblematic investment financing in order to disseminate these practices more extensively.

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The redirecting of private and public financial flows will not come to pass without a change in the investment priorities of the key national and international finance institutions.

The financing of transitions can only be engaged within a coalition of financial and technical stakeholders that share common investment objectives and strategies. At its own scale of operations, AFD Group contributes to structuring this stakeholder coalition around themes related to the energy and environmental transition on the one hand, and sustainable agriculture on the other. On these two themes, AFD Group regularly proposes to its financial partners in the global South seminars and workshops designed to compare different types of approaches, identify successful experiences and list the main pitfalls. These expert communities enable AFD to build a strategy of influence whose core objective is to mobilise local financial actors to support these transitions.

AFD partners…

The **International Development Finance Club (IDFC)** is a network of national and regional development banks from both the global South and North that share common objectives and principles for action. IDFC members have committed to supporting the momentum begun within the framework of the Paris Agreement on the fight against climate change, and to supporting the financing of the Sustainable Development Goals (SDGs). Overall, the members of the IDFC network have set themselves the goal of moving forward the practices of local and international financial institutions in view of promoting finance for more responsible development models.

For instance, the network contributes to setting a common benchmark for climate finance. The network, whose presidency was assumed by AFD in October 2017, also wields considerable influence in international debates on development finance. AFD Group will rely on this network to insist on the pivotal place of local financial systems in financing more sustainable development models. It will actively contribute to the network's reflection on how to speed up the dissemination of SDG-compatible financing practices. The Group will also strive to build technical and financial partnerships with the public development banks that are IDFC members, in order to drive the catalytic role that these play in national financial systems.

Making Finance Work for Africa (MFW4A) is an African platform for cooperation and experience-sharing set up on the initiative of Germany at the Heiligendamm G8 in 2007. AFD is among the 12 founding partners of the platform, whose secretariat is hosted by the African Development Bank. In the framework of themed focus groups, MFW4A mobilises institutional partners, decision-makers and actors in the private sector on questions focused on strengthening the development of Africa's financial sector. The platform also serves as a key lever for building up a strategic and technical dialogue with donors. AFD has financed the initiative since its inception and sits on the platform's executive committee alongside the EIB, AfDB and the German and Dutch ministries responsible for development cooperation.

Consolidation: Strengthen the architecture of the financial system to ensure its stability

AFD Group intends to commit to helping consolidate the architecture of local financial systems. Stable and reliable financial systems allow savings to be efficiently channelled into the productive sector, secure settlement transactions and absorb eventual factors of vulnerability. A stable and efficient financial system must have the following characteristics:

- The financial institutions that compose it must be able not only to assess and mitigate the risks inherent to their activity, but also withstand eventual exogenous or endogenous shocks.
- The financial operations set up by these institutions must go hand in hand with appropriate risk mitigation tools (particularly guarantees).
- The operating rules governing interactions between the central bank, the financial institutions and their clients must be clear and adapted to the context.
- Finally, the supervisory authorities must be able to discharge their mandate in full independence and be endowed with sufficient resources to ensure that controls and sanctions are effective.

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> *AFD will support initiatives emanating from regulators and supervisors that wish to enhance their skills and tools and consolidate their resources*

Orientation 1

Strengthen the regulation of financial activities

The higher the risk of contagion for financial crises, the more crucial it is that financial systems be regulated. Regular controls and effective sanctions are two fundamentals of the supervisor’s action. Any shortcoming in this area may well allow fragile institutions to prosper, even though they would lack the capacity to withstand an adverse change in market conditions, albeit only a slight one (a change in interest rates, economic slowdown in a sector, etc.). The technical expertise and resources required to ensure effective supervision are sometimes lacking in developing countries. Furthermore, the supervisor is not always vested with sufficient power to impose sanctions (licence withdrawal, curatorship, etc.), demand a change in the financial institution’s internal policy (recapitalisation, portfolio restructuring) or impose changes in its governance. The changes provided for under the Basel III recommendations at last include the aim of strengthening the requirements for information from the supervisory authority, who must be able to process and control the quality of the data produced.

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> *Stable and reliable financial systems allow savings to be efficiently channelled into the productive sector, to secure settlement transactions and absorb eventual factors of vulnerability.*

In addition, regulations must be sufficiently adaptable to keep pace with the emergence of new models or new institutions that temporarily slip through the regulatory net. Although unregulated finance poses no systemic risk in many countries, it can represent a substantial portion of active financial assets. Whether it is telecom operators, public or private investment fund operators, or operators of special-purpose investment vehicles, the supervisor and regulator must, at the very least, be able to ensure careful monitoring of the market, anticipate the emergence of new players and counter the risks that their model poses for the system as a whole.[34]

Moreover, the exchange of financial information is insufficient in some countries. When this exchange is efficient, public or private information-sharing tools (credit information exchange,[35] credit bureaus,[36] etc.) help to limit the frequency of non-performing loans and reduce the risk of over-indebtedness. Implementing these tools requires the adoption of regulatory texts that are sufficiently binding so as to ensure not only that data is automatically reported by all financial institutions (mandatory participation), but also that management of these data is reliable and that the entire sector can access them. These tools are most effective when they deliver reliable and honest financial information on borrowers.

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[34] For an analysis of the new risks linked to digital financial inclusion, as well as a contextualisation of future challenges, see for example K. Lauer and T. Lyman, “Digital Financial Inclusion: Information for Customers, Regulators, Supervisors and Standard-Setting Bodies”, CGAP Brief, 2015.

[35] The body in charge of recording all types of loans granted to a beneficiary when the commitment exceeds a set ceiling. On the basis of this threshold, banks are able to know their client’s overall level of debt. The credit information exchange also transmits to the monetary authorities information on the distribution of credit for each reporting institution.

[36] Organisations that collect and compile individual credit histories. On the basis of this information, the lending financial institutions are able to assess risk more effectively and thus grant credit in line with the borrower’s real situation.

As part of its activities to promote effective and responsible governance, AFD will support initiatives emanating from regulators and supervisors, if need be at a regional scale, that wish to enhance their skills and tools and consolidate their resources to ensure regular controls and effective sanctions. AFD will also support these same entities in their efforts to modernise financial regulations so as to take new players into account, guard against the materialisation of already identified risks and anticipate the emergence of new risks. Finally, AFD Group will support the initiatives designed to promote information-sharing among the financial institutions on the quality of borrowers.

Furthermore, economic actors in developing countries rarely use financial markets to access funds. These markets are often stunted, illiquid and relatively lacklustre,[37] notably in sub-Saharan Africa. The number of issuers is relatively limited (most often, the State and a few large companies), while the traded securities often have relatively short maturities. The State does not always fulfil its role as the market's benchmark issuer and investors have scant tools available to anticipate market conditions and decide on their investment strategy.[38] Although financial markets are more structured in emerging countries, in middle-income and low-income countries they offer a narrow spectrum of instruments (weak presence of securitization products or derivatives, etc.) and, to boot, some of them are highly volatile. In these circumstances, economic actors are few and far between on local financial markets, be it the bond or stock market.

Orientation 2

Guarantee the availability of long-term financial resources and support the diversification of financing instruments

Deposits and retail savings products are the chief source of financing in developing countries, particularly the least developed ones. The deposit base is for the most part made up of demand deposits, whereas time deposits and savings products are underdeveloped. However, these short-term financial resources are sometimes insufficient to meet the demands of fast-growing financing activities, especially in sub-Saharan Africa. The capacity of financial operators to mobilise short- and long-term financial resources at an affordable cost is still limited in some countries. The perception of macroeconomic, political and financial risk at times curbs the flow of investment to the most vulnerable countries in the South. Yet, financial operators have an absolute need for stable financial resources (sound deposit base, equity and long-term debt) to fund their development. The insurance sector does not always fulfil the stabilising role that it ensures in developed countries by making long-term resources available to financial institutions. Developing this sector is nonetheless a key issue in an overall context where prudential rules for financial institutions are being reinforced. In fact, the evolving financial regulation is tending to tighten solvency requirements (equity and quasi-equity) and, above all, liquidity requirements (matching the maturities of liabilities and assets).

To promote the sustainable development of financial systems, AFD Group will provide long-term resources to operators wanting to play a prominent role in financing the economy. The Group will also support the matching of liquidity supply and demand in financial markets. To do so, AFD Group will give its support to any initiative that can help to broaden the issuer or investor base on a given market, promote the diversification of available products or facilitate the listing of these securities. AFD Group will nonetheless avoid supporting initiatives that would encourage volatility on financial markets or foster the development of tools unable to meet the needs of non-financial agents. On the other hand, AFD Group will be able to support the emergence of domestic investment vehicles that will enable financial institutions to mobilise long-term resources in local currency. Lastly, AFD Group will support institutional investors (insurance firms, pension funds, etc.) wanting to promote financing for productive investment by making local long-term savings available to the market.

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> *AFD Group will provide long-term resources to operators wanting to play a prominent role in financing the economy.*

Orientation 3

Support the modernisation of risk management tools and governance structures of financial institutions

Risk management is a core activity for financial institutions. By nature, they are exposed to financial risks (credit risk, liquidity risk, market risk, etc.), to operational risks, legal risks and reputational risk. Moreover, environmental and social risks and, increasingly, climate-related risks are becoming more important for risk analysis in financial institutions in the global North and global South. Should one of these risks, however small, materialise in a financial institution, this is likely to impact other financial institutions and, in some cases, the economic and financial ecosystem as a whole.

These different risk categories are part and parcel of financing activities, but they must be reliably assessed before a financing operation is set up, and then regularly monitored thereafter. Some of these risks, notably credit risk, liquidity risk and operational risk, are heightened in developing countries. Moreover, the

[37] For a presentation of the positive linkage between the development of financial markets and economic growth, see for example T. Beck and R. Levine, "Stock markets, banks, and growth: Panel evidence", Journal of Banking and Finance; 2004. For an analysis of the causal links between Douala's capital market development and economic growth in Cameroon, and a presentation of the priority actions to promote the development of the local financial market, see for example B. Ake and R. Wouono Ognaligui, "Financial Stock Market and Economic Growth in Developing Countries: The Case of Douala Stock Exchange in Cameroon", International Journal of Business and Management, 2010.

[38] For example, the yield curve – a key tool for building an investment policy on bond markets – often only shows a few credit ratings for short maturities. The low level of liquidity on some markets also means that this is a highly volatile tool of little practical use.

governance of risk is sometimes inadequately structured within financial institutions. It often prevents an integrated risk management system from being developed. Risk assessment methods sometimes need modernising (scoring, automatic rating, etc.), while various planning and forecasting tools (risk mapping, stress tests, etc.) could be used to identify areas of vulnerability and avoid certain failures.

In some cases, the governance structures of financial institutions suffer from a number of weaknesses. The weaknesses may be inherent to the leadership team, to decision-making processes, to the functions of control or to detection and alarm mechanisms, for example.

In the framework of the direct financing operations that it puts in place, AFD supports the evolution of the procedures of its partners who want to consolidate their risk management systems and their governance structure. In terms of risk prevention, this support can involve financial risk management (credit risk, market risk, liquidity risk, etc.), the prevention of risks relating to money-laundering and financing of terrorism, the assessment of environmental and social risks, as well the integration of climate risk. AFD Group will strive in parallel to promote among its partners governance structures that comply with international best practices.

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In the framework of the direct financing operations that it puts in place, AFD supports the evolution of the procedures of its partners who want to consolidate their risk management systems and their governance structure.

AFD partners…

The **World Bank** and the **International Monetary Fund** have a historical mandate concerning financial stability in developing countries. In this context, they have developed substantial expertise in financial systems regulation and support for structural reforms in the sector. To make this expertise available, they have set up various dedicated funds (notably the FIRST trust fund) that provide finance for the technical assistance needed to design and implement these reforms. AFD will thus work in close collaboration with the World Bank and, to a lesser extent, with the International Monetary Fund to develop diagnostic capacities and build adapted intervention tools to strengthen the regulation and supervision of financial activities.

The **Caisse des Dépôts et Consignations** and its subsidiary **Bpifrance** are key actors in the French financial system. They are experienced in collecting and managing savings, SME financing, and guarantees. Under the strategic partnership that it has formed with AFD, the CDC and its subsidiaries will bring their expertise to partners who are seeking for ways to more actively mobilise available savings with a view to building a financing offer or guarantees for local economic actors (product offerings, governance, risk management, SME rating tools, etc.). Among these partners, the Caisses des Dépôts established in countries where AFD Group operates are key interlocutors for AFD Group, given their mandate and activities.

AFD Group also operates in French Overseas Departments and Collectivities…

AFD Group's operations in support of developing the financial systems in French Overseas Departments and Collectivities fulfil specific objectives. The structuring of financial systems in these Overseas Departments and Collectivities does not call for massive support from the Group provided that the banking penetration rates are high and only if the financial actors encounter major difficulties, in exceptional circumstances, to mobilise commercial funding.

In these conditions, the action of AFD Group focuses on the following missions:

- The provision of long-term financial resources to the financial institutions who request them. AFD Group thus supports the activity of **SOCREDO**, the leading bank in French Polynesia, and in which AFD has a 35% shareholding. The Group also supports the **Crédit Agricole in New Caledonia** to facilitate the purchase of agricultural equipment. In addition, AFD Group is ready to respond to possible requests in the event of a structural deficit regarding long-term resources or a local liquidity crisis.
- AFD Group also supports the expansion of **microfinance** in the French Overseas Departments and Collectivities. AFD' Group's operations to promote microfinance in French Overseas Departments and Collectivities aim to encourage employment and economic value creation by funding start-up and microenterprise projects.
- AFD Group also supports the development of risk-capital schemes. The Group can notably intervene by participating in investment funds or directly investing in company equity. The Group participates in two venture capital funds (FCPR) in Réunion Island.
- Lastly, AFD Group manages the **SOGEFOM** (French Overseas Guarantee Fund Management Company) which operates in the Pacific region (mainly New Caledonia and Polynesia), the **Saint-Pierre-et-Miquelon Interbank Guarantee Fund** (FGSPM), the **Guarantee Fund for the agricultural, fishing, timber and aquaculture sectors** (FOGAP) in the French overseas departments and, in its capacity as local service provider for Bpifrance Financement, appraises the applications for credit guarantees issued by banks in the French overseas departments.

4.

INTERVENTION PRIORITIES TO OPTIMISE IMPACTS

The operational application of the three strategic objectives presented in the previous section will be grounded in the strengths, experience and tools already available within AFD Group. Building on these acquis, the Group intends to develop these new ambitions and adapted operating methods to support the changes underway within financial systems. The seven operational priorities presented below are reminders of the main features of the existing operational system and define how it is set to evolve.

ACTIVITY No.1

Serve populations excluded from financial systems

AFD Group undertakes operations to promote access to financial systems for certain categories of vulnerable populations. In partnership with microfinance institutions, AFD Group promotes, for example, financial products that are made available to population groups living in remote areas. It can also support the development of a financial activity benefitting rural areas or women. Some programmes also target young segments of the population to promote start-ups or the growth of income-generating activities. With its Financial Inclusion Facility, AFD Group annually earmarks grant funding worth 10–15 million euros to finance operations targeting populations excluded from financial systems. This Facility makes it possible to build operations that are of particular benefit to populations with little or no access to financial services. Through its ARIZ guarantee instrument (see p. 18), AFD Group makes it easier for microfinance institutions to obtain refinancing from local banks and is thus able to support the deployment of microfinance activities across a whole territory.

In parallel, AFD Group wishes to adopt an ambitious approach to support financing for the agricultural sector by offering financing vehicles, technical assistance and guarantees in countries where a clear and proactive public policy will so permit. AFD Group will develop an integrated programme, much like SUNREF (see p. 18) , to finance the agricultural sector. Depending on the needs, this will propose financing products for financial actors, capacity-building actions and, in some circumstances, the offer of a guarantee.

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> *AFD Group undertakes operations to promote access to financial systems for certain categories of vulnerable populations.*

AFD Group will also be involved in identifying and supporting the emergence of new models or technologies likely to promote access to financial systems for excluded populations. The development of digital finance (mobile banking, fintech) will be one of the important aspects of this activity. This will mean working with partners who are particularly effective in these areas (notably the Bill & Melinda Gates Foundation).

AFD Group supports…

Created in 1998, the French NGO **Entrepreneurs du Monde** stands out in the landscape of financial inclusion actors as its approach is firmly directed towards producing the greatest possible social impact. Its interventions primarily target the most vulnerable or excluded population groups (those living in extreme poverty, single women, people suffering from HIV/AIDS or handicaps, etc.). Entrepreneurs du Monde is currently providing technical support through a dozen microfinance programmes in ten African and Asian countries and in Haiti, and reaches 150,000 beneficiaries. To meet its partners’ financing needs, Entrepreneurs du Monde has set up the **Microfinance Solidaire** company, which is a financing vehicle enabling it to provide loans and equity to support the microfinance institutions that also receive other assistance from the NGO.

In 2016, AFD granted a €4-million loan to Microfinance Solidaire, allowing it to scale up activities with its African partners (microfinance institutions and energy programmes in Benin, Burkina Faso, Ghana, Madagascar and Togo) and support the creation of new structures in several countries (Senegal, Guinea, Chad, Sierra Leone and Liberia, and possibly Niger). AFD also supports Entrepreneurs du Monde through a €1.8 million grant to finance the NGO’s technical support activities for partner microfinance institutions. This support will also help to finance training in financial and non-financial subjects for clients who are beneficiaries of these microfinance institutions.

The project aims to improve the living conditions of vulnerable populations or those living in precarious situations. The project’s final beneficiaries will be mainly women, who account for 88% of the beneficiaries under programmes supported by Microfinance Solidaire. .

ACTIVITY No.2

Support financing for micro-, small and medium-sized enterprises by diversifying the Group's range of instruments

AFD Group primarily supports corporate financing via targeted financing tools. Credit lines dedicated to MSMEs can, for example, provide financial resources and technical assistance to banks wishing to roll out a downscaling programme so as to penetrate or consolidate their position on the MSME market. Other financial institutions, such as specialised financing societies (leasing companies)[39] or microfinance institutions can also provide solutions adapted to this category of entrepreneurs. AFD Group will continue to support these actors via different tools (equity, loans, guarantees, etc.).

> *AFD Group intends to develop a more comprehensive range of tools to enhance companies' access to bank financing.*

In tandem, AFD Group deploys guarantee tools to catalyse financing for small and medium-sized enterprises: the ARIZ guarantee facility enables eligible financial institutions willing to finance MSMEs to share counterparty risk with AFD under set conditions. Similarly, in the French Overseas Departments and Collectivities, the distribution of BPI products or the deployment of AFD guarantee funds (SOGEFOM, FOGAP, etc.) can help to enhance the prospect of accessing credit for this corporate target.

Finally, investment funds are also able to bring useful solutions for SME financing. In conjunction with long-term resources, they often contribute finance dedicated to capacity-building for the beneficiary companies.[40] To support these actors, the FISEA fund, owned by AFD and managed by PROPARCO, invests in Africa on the basis of an investment policy that takes on board the risk-patient capital duo: the fund invests as much in microfinance institutions as in investment funds that themselves invest in SMEs.[41]

In parallel and on a more ad hoc basis, AFD is able to support the activity of local guarantee funds through financing tools and technical assistance.[42]

Yet, the fact is that the bulk of formal and informal sector MSMEs are still not always able to access the financial system, particularly in sub-Saharan Africa. In this context, AFD Group intends to develop a more comprehensive range of tools to enhance companies' access to bank financing. This approach will lead AFD Group to pursue the deployment of existing tools (mainly ARIZ and lines of credit), and also to work on rolling out new tools.

AFD Group will strive to support the development of vehicles such as seed funds, venture capital funds and private equity funds in the countries in which it operates.[43] In parallel, AFD Group will work on further developing the ARIZ tool. Among the expected changes is a broader spectrum of eligible countries, and increasing the quota-share of risk borne by the Group will extend its outreach to new financial partners and allow financing for new entrepreneurial categories. If need be, AFD Group can mix a financing product with a guarantee when the local context presents particularly tight constraints for MSME financing. In this case too, the programmes to be implemented by AFD Group will enhance the accounting and reporting skills of MSMEs in order to facilitate access to formal financial services. To support financing for small and medium-sized enterprises whose income is often in local currency, AFD Group will make a particular effort to build a financial offer in local currency or, failing that, structure mechanisms to cover foreign-exchange risk. In any event, AFD Group will see to it that the MSMEs targeted by the programmes that it intends to implement are not exposed to foreign-exchange risk. At the institutional level, AFD will promote the creation and development of credit information exchanges and credit bureaus.

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[39] Specialised financing companies can also play a role in supporting the development of bond markets insofar as they regularly raise funds on these markets to meet their financing needs.

[40] In this perspective, AFD Group supports the investment fund of Investisseurs & Partenaires, as well as Business Partners.

[41] Examples of projects supported by the FISEA fund are available on the investment fund website: http://www.proparco.fr/Accueil_PROPARCO/fisea-proparco

[42] For instance, since 2010, AFD Group has supported the Malagasy guarantee fund Solidis, dedicated to local SMEs, through technical assistance geared to structuring the fund and reinforcing the operational team, with an initial funding in quasi-equity and a counter-guarantee.

[43] Pilot initiatives have already been undertaken with the Carthage Business Angel fund, for example.

ACTIVITY No.3

Combine financial support and technical assistance to bring about change in financing practices

As in the case of SUNREF, AFD Group is one of the pioneering donors in building a combined (financial and technical) offer for the financial sector. By using a grant component to back a line of credit or guarantee, AFD Group is able to offer financial institutions and their clients technical assistance services (training, advisory support, communication, etc.) that enable financing practices to change and certain markets to mature. The grant component can help to fund technical assistance services, make the financing conditions of some investment categories acceptable when this aspect is clearly an impediment to market growth, or set up incentive-based or risk-sharing schemes. At the institutional level, the grant component can also help to structure an emerging sector by contributing to the definition of ambitious public policies or by mobilising supporting intermediary structures (industry associations, investment promotion agencies, technical agencies, etc.). These different actions must be conducive to creating new markets and structuring immature markets.

Given its robust experience, AFD Group now wishes to replicate this type of approach in order to accelerate the transition towards more sustainable growth models. Financing the transition to development models that exploit natural resources less intensively and are less vulnerable certainly requires changes in the asset allocation processes that currently guide financial operators in both the public and private sectors. Public authorities must provide effective and unambiguous market signals to promote these transitions. In addition, the policies on investment, governance and risk management within financial institutions must evolve in order to promote the most catalytic investments. On this count, AFD Group will combine a financial offer with a technical offer whenever the targeted sector requires it. This approach will mainly be designed to support financial institutions wanting to adapt their investment policy by deploying methods and dedicated analytical tools, to acquire additional expertise in key areas (renewable energy, water and sanitation, sustainable agriculture, housing, education, resilience to climate change, etc.), to develop their product range or to reach a more vulnerable public. AFD Group will implement this type of approach as a priority to accelerate the energy and environmental transition, support sustainable agriculture and promote people's access to essential services.

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> *AFD Group is one of the pioneering donors in building a combined (financial and technical) offer for the financial sector.*

ACTIVITY No.4

Build an approach geared to the community of public development banks, enabling AFD Group to play a lead role

AFD Group wishes to foreground the leading role of public development banks in changing the practices of financial operators, in targeting some emblematic investments and in contributing to the financing of key economic and social infrastructure. Public development banks are often able to make changes to their investment policy more rapidly and more flexibly than commercial banks. Their balance-sheet structure is also more suited to granting long-term loans, which makes them potential vectors for structural change.

They also have the capacity to develop a broader range of financial tools (loans, equity stakes, guarantees) that can be mobilised to set up financial operations tailored to the needs of each project. Their mandate also makes them a key contributor for the implementation of public investment programmes. Lastly, their size, the quality of their portfolio and their close ties with States very often enable them to mobilise international financing under favourable conditions. As such, they are also potential vectors for developing new financial products.[44]

Yet, public development banks represent a very heterogeneous category. Some are state-owned and only operate in a given country or region (BNDES in Brazil, BDMG in Brazil's Minas Gérais region), whereas others are owned by a college of

[44] For example, Project Bonds are issued to fund an infrastructure project and are redeemed using the revenue streams generated by the project. Green bonds are debt securities issued by a company or an institution wishing to dispose of resources for the purpose of investing in projects that comply with a number of criteria related to protection of the environment.

> *AFD Group wishes to foreground the leading role of public development banks in changing the practices of financial operators, in targeting some emblematic investments and in contributing to the financing of key economic and social infrastructure.*

member States and thus competent to intervene in a region-wide economic area (TDB in eastern Africa, BOAD in the WAEMU zone, BCIE in Central America, etc.).

Some have relatively limited mandates and can only operate in a specific sector (in Peru, for example, Agrobanco in the agricultural sector and Fondo Mivivienda in the housing sector).

Others have much broader mandates and are given a more structuring role in the economy (TSKB in Turkey, for example). Another key difference lies in the ways that they intervene. Some are second-tier banks and their mission involves providing resources to the commercial bank sector. Others can directly finance various categories of projects in compliance with subsidiarity criteria designed to avoid a crowding-out of the traditional banking sector.

AFD Group has established financial and technical partnerships with a number of public development banks in Africa and Latin America. In Latin America, AFD Group will continue to support these actors in order to speed up the shift in development models. It will encourage them to consolidate their pioneering role chiefly in the fight against climate change. It will promote the incubation of pilot initiatives by providing them with the technical assistance required to grow innovative financing operations, not only in terms of their financial structure but also their intended targets (modernisation of urban infrastructure, climate change adaptation programme, sustainable agriculture, etc.). AFD Group will organise peer exchanges with these institutions, which, in many respects, have built approaches and tools that could usefully serve as inspiration for AFD. The Agency will thus confirm its partnership approach with the IDB and ALIDE, the network of the continent's national development banks.

In continental Africa, the mandate of the major public development banks is focussed more on regional economic integration. AFD will provide support to the institutions wanting to build an investment policy focused on the Sustainable Development Goals and will contribute to financing projects with a high regional value-added. For institutions whose economic and financial model still shows certain vulnerabilities, a targeted capacity-building programme will enable them to strengthen their internal governance and consolidate their positioning as a lead financial actor.

AFD Group supports…

Founded in 1952, the **Brazilian National Bank for Economic and Social Development (BNDES)** is 100%-owned by the Brazilian state and acts under the supervision of the Ministry of Development, Industry and Trade. Its mission is to promote the country's sustainable development, a competitive environment for Brazil's economy, job creation and the reduction of inequalities. It plays a major role in financing the renewable energy sector in Brazil, which ranks as the seventh largest consumer of electric power in the world, and as the first in South America.

AFD Group granted a €165 million loan to the BNDES to enable it to finance investment in energy innovation, energy efficiency and renewable energies. This line of credit provides support for the BNDES' activities to promote renewable energies and energy efficiency in line with local public policies. This project is helping to curb greenhouse gas emissions, while at the same time supporting the country's economic and social development, in a context of high growth and efforts to combat social and territorial inequalities. It also aims to enhance the competitiveness and the innovation capacities of firms operating in these sectors.

A technical support component also helps to develop and enhance the expertise of both Brazilian and French financial institutions in the areas of green energy and energy management. This support is also designed to develop the future thrusts of technical cooperation targeting the fight against climate change. This cooperation will involve Brazil's local authorities, who could, in the medium term, receive financial support from AFD Group.

ACTIVITY No.5

Provide financial actors with resources adapted to their development

AFD Group supports its partners' long-term development strategy by providing them with resources tailored to their needs. Given the structure of its balance sheet, AFD Group is in a position to provide long-term resources in the form of equity or loans – which can be coupled, if need be, with a grace period – to financial institutions wanting to mobilise resources from an international donor. These resources enable local financial actors to finance long-term projects (e.g. infrastructure), invest in new market segments or develop their activity abroad, for example. As a complement, AFD Group can provide resources dedicated to financing international trade and short-term guarantee lines to institutions wanting to plug into international financial systems under favourable conditions while also developing some specific segments of their activity.

To meet its partners' needs and if warranted by the context, AFD Group can also combine the financing that it grants with mechanisms to cover foreign-exchange risk. In some countries where the group operates, this risk is a major factor of vulnerability for financial institutions, especially for those highly exposed to risks relating to households and MSMEs. Among other possibilities, AFD Group can develop this type of coverage in partnership with The Currency Exchange Fund (TCX), in which it has a shareholding.

Lastly, AFD Group will provide the financial and technical resources required to enable local financial institutions to more actively mobilise savings available on local financial markets. More specifically, the Group will work to mobilise investors seeking economic, social and environmental impacts through its support for the structuring of dedicated financing vehicles. AFD Group can also support financial institutions wanting to issue bond securities dedicated to financing projects with a substantive climate impact, for example. This could be done through technical support (capacity building) or, context permitting, through financial support (subscription to bond issues as a benchmark investor, credit enhancement, etc.). Diversifying investment vehicles and broadening the investor base will make it possible to mobilise local savings more effectively in the direction of sustainable productive investment.

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AFD Group will provide the financial and technical resources required to enable local financial institutions to more actively mobilise savings available on local financial markets.

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AFD Group is in a position to provide long-term resources in the form of equity or loans, to financial institutions wanting to mobilise resources from an international donor.

AFD Group supports…

The **Bourse régionale des Valeurs Mobilières** (**BRVM**) is the main stock exchange company operating in the West African Economic and Monetary Union (WAEMU). To encourage expansion of financial markets in West Africa, PROPARCO has approved the allocation of a guarantee on invested capital and return on investment for subscribers to a mutual fund on the BRVM. Set up by the asset management company of Ecobank group, EcoBank Development Corporation Asset Management (EDC AM), this mutual fund will mainly invest in shares (60%) and bonds (30%). It targets institutional investors (mainly pension funds) seeking to diversify their investments with no additional risk. The potential for an increase in asset value along with the capital guarantee when the mutual fund matures (6 years) make this an attractive and much-demanded product.

Through this guarantee, granted for a capital amount of XOF 5 billion (€7.6 million) and a return of XOF 1.33 billion (€2 million), PROPARCO is aiming to stimulate BRVM's activity on this asset class, improve its liquidity and promote the mobilisation of long-term savings from institutional investors. As a result, this operation could enable major regional companies to raise funds more easily to finance their investment plans. A further objective is to promote the diversification of the investment portfolios of regional social security funds and pension funds.

ACTIVITY No.6

Establish a structured operational approach to strengthen regulation of the financial systems

AFD Group is experienced in providing support for the regulation of financial activities. This experience is currently focused on the microfinance and insurance sector. AFD Group thus assists public authorities in modernising the regulations governing financial operators, building a long-term strategy to develop the sector, and reinforcing the supervisor's capacities. These operations were financed by grants. The lessons learned through this activity tend to show not only that it needs to be accompanied by a systemic monitoring of the sector and a high-quality dialogue with the authorities (ministry, central bank, supervisory authority), but also that it is part of a long-term process.

> *AFD Group will also engage in a more systematic dialogue with national public authorities on developments in the financial sector, the sector's weaknesses, and the key ongoing and future reforms.*

In line with the "Governance" mandate conferred on AFD Group in 2016, AFD intends to capitalise on this experience to design structuring guidance in the area of financial systems regulation. AFD Group must acquire a capacity to establish in-depth diagnostic analyses of the financial systems in the countries in which it intends to operate. For this, it will mobilise a network of internal and external, and national and international experts likely to support the Group's intervention approach. Consistent with their mandates, the IMF and the World Bank have undisputed operational experience in the area of financial regulation. AFD Group will deepen its relationship with these partners to forge a strategy and operational collaboration on this theme. AFD Group will also engage in a more systematic dialogue with national public authorities on developments in the financial sector, the sector's weaknesses, and key ongoing and future reforms. This dialogue will enable reinforcement operations to be crafted as soon as the first phases of the planned reforms begin. Lastly, AFD Group will deploy tools, such as public policy loans, that are more adapted to supporting the reform process and able to complement traditional tools. When appropriate, the Group will seek to join the community of donors that often work collegially at local level to support the implementation of financial sector reforms.

AFD Group supports…

The **Conférence Interafricaine des Marchés d'Assurance** (**CIMA –** Inter-African Conference on Insurance Markets) is the regulator for the insurance sector in countries that are members of the West African Economic and Monetary Union (WAEMU) and the Economic and Monetary Community of Central Africa (CEMAC).

Through a €2.5 million grant, AFD Group is supporting this key insurance sector player as well as its national relays (national insurance directorates) to adapt the regulatory framework and strengthen their supervisory capacities with a view to adopting international best practices. The project's goal is to create a framework conducive to insurance market growth that is both sound, more inclusive and more innovative. How? The market will have a sounder footing if its supervisors participate in its consolidation and restructuring, given that it is now highly fragmented and has many insolvent actors who are sometimes unable to pay policyholder claims. The insurance market will be more inclusive if insurance companies have a regulatory framework enabling them to make allocation decisions more effectively and thus develop new insurance and microinsurance products. Finally, the market will be more innovative if the regulatory framework supports the industry's recent developments, as for example, by providing insurance contracts via mobile phones.

The project is headed by CIMA's General Secretariat. The main thrusts (regulatory reforms, development of supervisory practices) will be presented for discussion with the industry's main stakeholders convened within the project's steering committee: CIMA, the five national directorates involved in the project, the Fédération des compagnies d'assurance de droit africain (Federation of African national insurance companies), and the ACPR. Moreover, the technical and financial partners operating in the insurance sectors in the zone covered by CIMA have been invited to attend the steering committee as observers so as to ensure effective coordination of assistance in this area.

ACTIVITY No.7

Support the emergence of new financing vehicles and new tools

The development of fintechs impacts myriad aspects of traditional finance and is helping to drive the emergence of new digital services (money transfer platforms, virtual portfolios, pre-payment systems, automatic credit, etc.). The growth of digital finance tools can help to promote access to financial services for populations living in remote areas. In this setting, AFD Group can support financial partners who so wish – mainly microfinance institutions – to develop digital finance tools to target people excluded from financial systems. AFD Group's operations must help to support the most promising innovations and models, while also contributing to the crafting of an adapted regulatory framework. For instance, concerning crowdfunding, AFD has begun a process of reflection to gauge the development potential of these models. The sector is booming but most of the operators are small-sized and the economic models are still fragile. Even so, some are growing at a particularly fast pace.

In parallel, the regulatory framework for digital finance is currently under preparation in most South countries. One of AFD Group's projects will involve building an operational procedure to support the development of these models under satisfactory conditions in terms of protection and regulation. The Group will be able to draw on the many studies conducted in the evolving context of the related French regulations. The Group's operations in the area of digital finance will be an opportunity to give concrete form to the commitments that the Group has made under its "Digital" strategy.

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The development of fintechs impacts myriad aspects of traditional finance and is helping to drive the emergence of new digital services (money transfer platforms, virtual portfolios, pre-payment systems, automatic credit, etc.).

AFD Group supports…

Launched in July 2007 by Africinvest Capital Partner (ACP – now Africinvest), the **Africinvest Financial Sector** investment fund invests in companies in Africa's financial sector. The fund's investment policy, which has raised more than €60 million, involves limited-sized investments (ranging from €1 to 5 million) to further the growth of financial actors in Africa. The fund notably supports the creation of greenfield financial institutions and also operates an ambitious investment strategy in low-income countries in sub-Saharan Africa. On 31 December 2016, the Africinvest Financial Sector fund approved investments totalling nearly €42 million, representing 20 transactions mainly in Mali, Madagascar, Burkina Faso, Mozambique, Nigeria and Zambia.

Through its FISEA fund, AFD Group provides the investment fund with financial resources as well as technical assistance. The technical assistance programme includes support for a microfinance institution in Mali (**Microcred Mali**) aimed at modernising the institution's tools and diversifying its products. The purpose is to improve the MFI's operations by introducing digitalised access to its products. Technological media (mobile app and web application) have been developed with expert assistance to support the MFI's operational staff (commercial staff, supervisors, agency directors and members of the credit committee). The digitalisation of the process should help to improve the productivity of the MFI's teams and the internal control of operations, make risk management more effective, and enhance the services proposed to clients.

KEY TAKEAWAYS

Policy on the responsibility of financial intermediaries

In the operations that it carries out in the financial sector, AFD Group implements an approach engaging its responsibility vis-à-vis the partners with whom it works. This approach is based on a prior due diligence combined with a support mechanism when shortcomings are identified:

- AFD Group first analyses the financial situation of the institution, its governance and the market environment in which it operates: this analysis aims to identify not only the factors affecting the soundness of the financial institution concerned, but also any potential areas of fragility. AFD Group notably refrains from entering into a relationship with institutions that do not exhibit the minimal characteristics of financial sustainability. If the preliminary analysis of the financial institution reveals certain fragilities, and providing that these pose no threat to the institution's sustainability, AFD Group can support its partner via an appropriate capacity-building scheme.

- AFD Group also undertakes an upstream analysis of the system for managing risks related to money-laundering and financing of terrorism. In particular, AFD Group evaluates the performance of the risk management system implemented by the partner financial institution. If this proves satisfactory in terms of international standards, AFD Group will request that its partner commit contractually to continue operating the existing system. If the system is deemed inadequate, AFD Group can engage with its partner to improve it so that it complies with the relevant international requirements.

- Regarding operations that directly expose AFD Group to risks incurred by the partner financial institution, an analysis of the institution's environmental and social risks procedure is carried out before the transaction for the loan or equity stake is implemented. As above, if this procedure is deemed satisfactory, the financial institution has to commit to implementing it for the duration of the operation contracted with AFD Group. Otherwise, AFD Group can assist its partner in improving the quality of its environmental and social risk management.

Within the framework of operations that directly expose AFD Group to risks posed by the financial institutions, the counterparties are subject to a number of contractual obligations. These obligations notably concern compliance with a procedure that is in line with international best practices for combatting money-laundering and the financing of terrorism, as well as for environmental and social risk management. An exclusion list is among the contractual obligations with which the counterparty must comply. This exclusion list includes various sectors or projects that the counterparty is prohibited from funding (any illegal activity, hazardous materials, trade in animals, production or trade in tobacco and alcohol, prostitution, etc.).

In addition to this policy on responsibility, which is applied to all of the AFD Group's partner financial institutions, microfinance institutions undergo a specific assessment: the social performance assessment of microfinance institutions aims to ensure that they abide by the body of standards that promote responsible financial practices that respect clients. These standards, known as the Universal Standards for Social Performance Management (USSPM), constitute a comprehensive set of standards and good practices designed to help financial service providers adopt a client-centric approach as the core of their strategic and operational decisions.

Implemented by the Social Performance Task Force,[45] the Universal Standards are organised into six dimensions, which break down into 19 standards and 85 "essential practices". The six dimensions provide financial institutions with guidance in defining the management and monitoring of the social repercussions of their activity: (1) define and monitor the social goals of the institution; (2) ensure broad management and employee commitment to social goals; (3) design financial and non-financial products that truly meet the needs of the target populations; (4) treat clients responsibly; (5) treat employees responsibly; (6) balance financial and social performance.

The Universal Standards comprehensively include the seven client protection principles embedded in the Smart Campaign:[46] (1) appropriate product design and delivery; (2) the prevention of over-indebtedness; (3) transparency; (4) responsible pricing; (5) fair and respectful treatment of clients; (6) the privacy of client data; (7) mechanisms for complaint resolution. But beyond these client protection principles ("do no harm"), the Universal Standards help to promote responsible, inclusive and sustainable financial institutions offering products that truly create value for their clients ("do good").

A tool for measuring and monitoring the Universal Standards at the level of microfinance institutions has been developed and disseminated by the French NGO, CERISE.[47] Dubbed the Social Performance Indicator (SPI), the tool is designed for self-assessment, mainly used by microfinance institutions to improve their practices. The "social audits" carried out by specialised rating agencies such as Microfinanza, M-CRIL or MicroRate also rely to a large extent on this tool.

[45] https://sptf.info/

[46] http://www.smartcampaign.org/

[47] http://www.cerise-spi4.org

The Financial Systems strategy logical framework

End goal

Contribute to building inclusive, sustainable and responsible financial systems

Operational goals

ACCESS

Promote access to an adapted and diversified financial offer

Orientations

- Encourage financial intermediaries to offer households solutions enabling them to access essential services and guard against economic shocks
- Encourage financial intermediaries to support enterprises at all stages of their business development

SUSTAINABLE DEVELOPMENT GOALS: 1 NO POVERTY; 2 ZERO HUNGER; 3 GOOD HEALTH AND WELL-BEING; 10 REDUCED INEQUALITIES; 8 DECENT WORK AND ECONOMIC GROWTH

TRANSITION

Support transformation in financial actors' practices to promote a sustainable finance model

Orientations

- Contribute to the development of financial systems so that they can play a pioneering role in the transition towards sustainable finance models
- Support financial systems to ensure an accelerated transition towards sustainable development models

SUSTAINABLE DEVELOPMENT GOALS: 4 QUALITY EDUCATION; 6 CLEAN WATER AND SANITATION; 2 ZERO HUNGER; 15 LIFE ON LAND; 13 CLIMATE ACTION; 7 AFFORDABLE AND CLEAN ENERGY

CONSOLIDATION

Strengthen the architecture of the financial system to ensure its stability

Orientations

- Strengthen the regulation of financial activities
- Guarantee the availability of long-term financial resources and support the diversification of financing instruments
- Support the modernisation of risk management tools and governance structures of financial institutions

SUSTAINABLE DEVELOPMENT GOALS: 16 PEACE, JUSTICE AND STRONG INSTITUTIONS

Activities

- Serve populations excluded from financial systems
- Support financing for micro-, small and medium-sized enterprises by diversifying the Group's range of instruments
- Combine financial support and technical assistance to bring about a change in financing practices
- Build an approach geared to the community of public development banks, enabling AFD Group to play a lead role
- Provide financial actors with resources adapted to their development
- Establish a structured operational approach to strengthen the regulation of financial systems
- Support the emergence of new financing vehicles and new tools

Financial operators' responsibility and client protection

Monitoring and evaluation framework for the Financial Systems strategy

The monitoring of operational activities carried out under this strategy will be organised into a three-pronged approach, as described below:

→ The monitoring of a number of quantitative indicators that follow results. This makes it possible to measure on a yearly basis what the activity contributes against the different strategic objectives proposed, to evaluate the achievement of the ambitions defined in the programme of activities and to measure the results of the operations financed.

Impact indicators of the Financial Systems strategy

Impact indicators	Unit of measure
Number of financial institutions receiving funding from AFD Group	number
Amount of funding granted to local financial institutions (incl. guarantees)	euros
AFD Group-backed investment in the private sector	euros
Number of firms (SMEs) receiving support or funding from AFD Group	number
Number of households receiving support or funding from AFD Group	number

Other indicators measuring results related to investments financed by partner financial institutions will also be monitored on a case-by-case basis.[48] The monitoring framework will be rounded out by qualitative results pertaining, for example, to the creation of new financial services or emerging complementary investment vehicles.

→ A mid-term review will be undertaken in 2020 and will combine the annual indicator monitoring with a synthesis of the key lessons learned from the ex-post evaluations conducted between 2017 and 2020. Depending on the results, a change in the strategy could be proposed at the end of the review.

→ An overall review of the strategy will be proposed for 2023. This overall review will propose the monitoring of results-measurement indicators, a review of the activities programme and a synthesis of ex-post evaluations conducted over the period. The strategy itself will also be subject to an overall ex-post evaluation on this occasion.

[48] The following sectoral indicators can be mentioned by way of example:
- In the energy sector: AFD Group-backed investment in the sector, installed capacity of renewable energies, energy savings , tonnes of CO_2-e saved,
- In the agricultural sector: AFD Group-backed investment in the sector, number of hectares of land developed,
- In the education and health sectors: number of individuals benefiting from additional services,
- In the area of pollution reduction: annual volume of liquid and solid waste treated, emissions of polluting gases avoided.

Acronyms and abbreviations

ACPR .... Autorité de Contrôle Prudentiel et de Résolution *(French prudential supervisory authority)*

ADB .... Asian Development Bank

AFD .... Agence Française de Développement

AfDB .... African Development Bank

ALIDE .... Asociación Latinoamericana de Instituciones financieras para el Desarollo (*Latin American Association of Development Financing Institutions*)

ARIZ .... Accompagnement du risque de financement de l'investissement privé en zone d'intervention (*Support for the Risk of Financing Private Investment in AFD's Areas of Operation)*

BCEAO .... Banque Centrale des Etats de l'Afrique de l'Ouest (*Central Bank of West African States*)

BNDES .... Banco Nacional de Desenvolvimento Econômico e Social (*The Brazilian Development Bank*)

Bpifrance ..... Banque Publique d'Investissement France

BRVM .... Bourse régionale des Valeurs Mobilières

CDC .... Caisse des Dépôts et Consignations

CEMAC .... Communauté économique et monétaire de l'Afrique centrale *(Economic and Monetary Community of Central Africa)*

CGAP .... Consultative Group to Assist the Poor

CICID .... Comité Interministériel de la Coopération Internationale et du Développement (*Interministerial Committee on International Cooperation and Development*)

CIMA .... Conférence Interafricaine des Marchés d'Assurance

EBRD .... European Bank for Reconstruction and Development

EIB .... European Investment Bank

FCPR .... Fonds Communs de Placement à Risques *(Venture capital fund)*

FISEA .... Fonds d'Investissement et de Soutien aux Entreprises en Afrique (*Investment and Support Fund for Businesses in Africa*)

FMO .... Netherlands Finance Development Company

FOGAP .... Fonds de garantie pour le secteur agricole, la pêche, la filière bois et l'aquaculture

GDP .... Gross domestic product

I4CE .... Institute for Climate Economics

IDB .... Inter-American Development Bank

IDFC .... International Development Finance Club

IFAD .... International Fund for Agricultural Development

IFC .... International Finance Corporation

JICA .... Japan International Cooperation Agency

KfW .... Kreditanstalt für Wiederaufbau

MFI .... Microfinance institution

MFW4A .... Making Finance Work for Africa

MSMEs .... Micro-, small and medium-sized enterprises

OECD .... Organisation for Economic Co-operation and Development

PROPARCO .. Société de Promotion et de Participation pour la Coopération Economique

SDG .... Sustainable Development Goal

SMEs .... Small and medium-sized enterprises

SOGEFOM .... Société de Gestion de Fonds de Garantie d'Outre-Mer

SPI .... Social Performance Indicator

SPTF .... Social Performance Task Force

SUNREF .... Sustainable Use of Natural Resources and Energy Finance

TCX .... The Currency Exchange Fund

tCO_2e .... Tonne of CO_2 equivalent

UNDCF .... United Nations Capital Development Fund

UNDP .... United Nations Development Programme

WAEMU .... West African Economic and Monetary Union

XOF .... Franc CFA Ouest Africain

What is AFD?

AFD is an inclusive public financial institution and the main actor in France's development policy. It makes commitments to projects that genuinely improve the everyday lives of people, in developing and emerging countries and in the French overseas territories. AFD works in many sectors – energy, health, biodiversity, water, digital technologies, training – and supports the transition to a safer, more equitable and more sustainable world: a world in common. Its action is fully in line with the Sustainable Development Goals (SDGs). Through its network of 85 agencies, AFD operates in 109 countries and is currently supporting over 3,500 development projects. In 2017, it earmarked EUR 10.4bn to finance these projects.

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