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Issues paper

Financing Africa's recovery: breaking new ground

I. Objective

1. The present issues paper provides background material for the fifth-fourth session of the Commission and the Conference of African Ministers of Finance, Planning and Economic Development, the theme of which is "Financing Africa's recovery: breaking new ground". It reviews the continent's financing landscape and evaluates the challenges and opportunities associated with enhancing the quality and scale of Africa's development financing to support an enduring recovery from the coronavirus disease (COVID-19) pandemic.

II. Vast and growing financing needs of Africa

A. Context

2. Existing research on the financing needs of Africa consistently demonstrates that the continent requires high levels of financing for improved structural transformation and to achieve the 2030 Agenda for Sustainable Development. Prior to the COVID-19 pandemic, those needs had been estimated at $200 billion per annum.

3. Development financing gaps have widened significantly since the outbreak of the pandemic. The annual Sustainable Development Goal financing gap for developing countries has increased by $1.7 trillion. For Africa, according to estimates by the International Monetary Fund, annual expenditures related to the Goals are expected to rise by $154 billion annually, as a consequence of the pandemic, and by an additional $285 billion for the next five years to ensure an adequate response to COVID-19. The rising financing costs have significant implications for the continent's ability to meet its

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development needs in the critical areas of infrastructure, health, education and climate.

B. Specific areas of focus

1. Infrastructure

4. African infrastructure needs are significant. A substantial number (650 million) of households lack access to energy; internet access is limited (39 users per every 100 persons); and the density of national roads is well below global standards (204 km of roads per 1,000 square km compared to a global average of 944 km per 1,000 square km). As a result, the continent's infrastructure financing gap is estimated by the African Development Bank at approximately $130 billion–$170 billion annually until 2025.

2. Health

5. Africa needs roughly $66 billion annually to meet its health financing needs and achieve the Sustainable Development Goals. These resources are needed, among other purposes, to reduce the continent's disease burden, improve maternal mortality rates (542 deaths per 100,000 live births in 2017, the highest in the world) and enhance access to skilled health personnel, who are in short supply. Investments in intensive care unit beds are also critical, in particular in sub-Saharan Africa, which has only one–five beds per 100,000 people, compared to European and East Asian countries.

3. Education

6. While primary school enrolments in the continent have increased, the quality of education remains low. Africa has the lowest literacy rates (65.6 per cent of people aged 15 and above) and the lowest proportion of teachers that meet minimum training standards (49.8 per cent in 2017) . The estimated annual financing needs to improve access to the quality of education in Africa amount to $39 billion.

4. Climate action

7. Africa contributes less than 4 per cent of global greenhouse gas emissions, yet climate change is a key developmental challenge, owing to the continent's biophysical make-up and weak adaptive capacity, underpinned by socioeconomic vulnerabilities such as a high dependence on rain-fed agriculture and weak climate information systems. The United Nations Environment Programme has projected that, by the end of 2020, between 75 million and 250 million people would be affected by climate-induced water stress, yields for rain-fed agriculture would diminish by up to 50 per cent and global warming of 2º C would place half the continent's population at risk of undernourishment. Responding to climate vulnerabilities costs African countries 3–5 per cent of gross domestic product (GDP) annually and, in some cases, more than 15 per cent. Furthermore, African countries signatory to the Paris Agreement on climate change will require close to $3 trillion in additional resources to finance implementation of their nationally determined contributions. Currently, only $6 billion out of the global total of $30 billion of climate adaptation finance flows to Africa.

5. COVID-19 pandemic

8. The COVID-19 pandemic further widened the development financing gap in Africa as social expenditures increased and revenues declined in the context of a global economic slump, punctuated by supply chain disruptions, declining commodity prices and revenue shortfalls.

6. Prospects for the future

9. Africa needs scaled-up resources to recover from the pandemic, build forward better and regain momentum towards achievement of the Sustainable Development Goals. Public financing is not at a sufficient scale to achieve this objective. Meanwhile, the bulk of global financial assets, currently worth $379 trillion, are held by private sector financial institutions and investors. Mobilizing a significant allocation of these private resources to Africa is imperative to achieve the development financing needs of the continent. Indeed, the growing share of private credit in the African financing landscape reflects this new reality.

III. African financing landscape

A. Low resource mobilization capacity

10. The African financing landscape has been shaped by the structure of its economies, which has in turn influenced the quality and composition of its external and domestic financing. Primary commodity dependence, coupled with limited value addition, has heightened vulnerability to commodity price shocks, with adverse implications for export revenues, inclusive growth and decent employment growth. Limited opportunities for decent employment, in turn, have nurtured informal sector growth and weakened the tax base.

11. In parallel, the prevalence of tax incentives, coupled with weak tax administration capacities, have further reinforced weaknesses in domestic resource mobilization and heightened dependence on external financing. By 2019, the tax revenue to GDP ratio in Africa was 14.9 per cent, well below the average of Latin America and the Caribbean (23.1 per cent) and that of the States members of the Organisation for Economic Co-operation and Development (OECD) (34.3 per cent). Low levels of domestic resource mobilization have been compounded by high levels of illicit financial flows, which are estimated to cost African economies $83 billion in lost revenue annually.

B. Evolution of public debt over the last decade

12. Multilateral and bilateral credit is currently the dominant source of external financing in Africa. This share, however, has rapidly declined in importance in the last two decades. In 2000, multilateral and bilateral credit accounted for 83 per cent of the continent’s total debt exposure. By 2019, this share was down to 60 per cent. By contrast, commercial borrowing soared from 17 to 40 per cent of total external debt in the same period, driven by Eurobond issuances, which accelerated by 1,170 per cent over the 2000–2019 period partly as a consequence of inadequate public financing and increased access to capital markets. The largest economies in Africa (Egypt, Nigeria and South Africa) account for the bulk of Eurobond growth. But relative to their respective GDPs, issuances by the frontier economies of Angola, Côte d’Ivoire, Gabon, Ghana, Senegal and Zambia have been sizeable.

13. By the end of 2021, African sovereign borrowers had raised $20 billion in the capital markets, including the landmark Sustainable Development Goal-linked bond by Benin in July, and $4 billion financing by Nigeria in September, bringing African sovereign issuance to over $175 billion during the past decade.

C. Impact of debt composition on debt service costs and maturity

14. Increased external financing had elevated the continent's debt levels and heightened debt vulnerabilities even prior to the pandemic, as debt service obligations rose in response to the increased exposure to commercial debt and exchange rate risks associated with foreign currency denominated debt. The continent's total debt-to-GDP ratio increased from 42 per cent in 2014 to 60 per cent in 2019, while the external debt-to-GDP ratio rose from 25.8 per cent to a spike of 42.6 per cent over the same period.

15. In parallel, Africa's debt service payments increased substantially (by 23 per cent) in 2020, when compared to 2019, while interest payments as a share of continental revenue rose from 12 to 19 per cent over the period 2014–2019. On a positive note, increased access to capital markets enhanced countries' abilities to attract long-term financing. For instance, in 2021, Benin, Côte d'Ivoire and Ghana issued Eurobonds with tenors of 31, 27 and 20 years respectively. By contrast, concessional loans from multilateral and bilateral sources have relatively short tenors.

D. Surge in financing needs caused by the pandemic

16. Fiscal indicators further deteriorated after the pandemic as policymakers increased spending and instituted a wide range of measures aimed at reducing the tax burden of households and business, to save lives and restore livelihoods. These measures contributed to the decline in the ratio of tax to GDP from 14.9 per cent in 2019 to 11.9 per cent in 2020. The fiscal balance as a proportion of GDP also deteriorated from -3.5 per cent in 2019 to -7.6 per cent in 2020, while the debt to GDP ratio edged up from 60 to 71.1 per cent in the same period, before improving slightly to 67.7 per cent in 2021.

17. The pandemic also heightened risk perceptions and triggered a retreat of portfolio investments from the continent. Yields on sovereign bonds soared as sovereign bond prices fell in the immediate aftermath of the crisis. For instance, the sovereign bonds of Angola lost 67 per cent of their value between February and April 2020. Yields have since retreated but spreads remain high (see www.bondevalue.com).

18. As the fiscal positions worsened, several African countries experienced credit rating downgrades and the number of countries at high risk of debt distress increased from nine in 2019 to twelve in 2020. Nevertheless, global support measures such as the Group of 20 Debt Service Suspension Initiative may have contributed to the decline in the number of countries in debt distress during this period. This figure improved from seven in 2019 to four in 2021.

E. Global responses to the pandemic

19. Bilateral and multilateral support for recovery efforts in Africa have been helpful but narrowly targeted, leaving out several vulnerable middle-income countries. The Debt Service Suspension Initiative, for instance, only deferred the bilateral debt service payments of low-income countries and, even though the initiative requested comparable treatment by private creditors, the response has been disappointing. Yet, private debt accounts for 40 per cent of total debt in Africa. Failure to make sufficient progress in addressing debt service obligations on the continent's private debt of about $150 billion has weakened the fiscal impact of the initiative (World Bank, 2021).

20. Participation of eligible market-access countries in the Debt Service Suspension Initiative was marred by concerns of credit rating downgrades. By the end of 2020, only 25 of 38 eligible African countries had signed a

memorandum of understanding to participate in the initiative. Similar concerns stalled implementation of the Common Framework for Debt Treatments beyond the Debt Service Suspension Initiative. To date, the three countries (Chad, Ethiopia and Zambia) that subscribed to the initiative are yet to receive debt relief.

21. Besides the Debt Service Suspension Initiative and the Common Framework, development partners committed $89.5 billion in financing to support African countries in the first quarter of 2021. The International Monetary Fund (IMF) provided grants, through the Catastrophe Containment and Relief Trust, to 19 low-income African countries to cover their debt obligations for an initial phase of six months. Eligible African countries received $7.24 billion in COVID-19 related financing (representing 1.16 per cent of their GDP) in 2020, through the IMF Poverty Reduction and Growth Facility.

22. Two years into the pandemic, the economic outlook is showing signs of improvement. The favourable outlook is threatened, however, by new variants of the COVID-19 virus that continue to slow the recovery, undermine the fiscal position of countries and increase the financing needs of the continent. Africa will have to overcome its financing challenges if it is to mobilize financing at competitive rates and sufficient scale to fund its recovery.

IV. African financing challenges

A. Objective

23. This section examines the key constraints to closing the financing gap in Africa, focusing, among other issues, on the quality and adequacy of domestic and external financing and the impact of such financing.

B. Mobilizing domestic resources

24. Factors underlying the relatively low level of the continent’s domestic resource mobilization outcomes include its large informal sector, weak and inefficient tax administration systems, prevalence of tax incentives, leakages in revenue collection and weak enforcement. Approximately 50 per cent of VAT revenues are not collected, as a consequence of inefficiencies. In addition, despite the prevalence of tax incentives in Africa, their impact on investments is weak; as estimated by ECA, increasing investments by 1 per cent will require a 20 per cent reduction in taxes.

25. Illicit financial flows, a significant source of fiscal leakages, are estimated to siphon at least $83 billion annually out of the economies of Africa, largely through trade misinvoicing. Weak customs administration and limited coordination across tax institutions have created opportunities for tax avoidance and evasion, trade misinvoicing, money laundering and corruption.

1. Domestic capital markets

26. Developed capital markets mobilize domestic equity capital to finance investments while minimizing reliance on external financing and associated foreign currency risks. Domestic capital markets in Africa, however, are not well developed. They have low market capitalization, few listed companies and lower liquidity relative to other developing markets and are costly and heavily geared towards short-term needs, rendering them ineffective in promoting economic growth and achieving the Sustainable Development Goals. As of 2020, there were only 28 stock exchanges in Africa that offered both primary issuance and secondary market trading. The proceeds raised from initial public

offerings in Africa between 2014 and 2019 totalled $27.1 billion, less than 1.4 per cent of global gains from initial public offerings in that period. The market capitalization-to-GDP ratio of most capital markets in Africa is under 30 per cent, well below the expected range of 75–90 per cent. By this metric, the capital markets of Nigeria (10 per cent), Namibia (21 per cent), Kenya (26 per cent) and Rwanda (31 per cent) are underdeveloped. The continent's large informal sector, low ratio of household savings to pension savings and weak regulatory and governance regimes are constraints on its capital market development.

2. Pension funds

27. African public and private pension funds have grown in recent years, providing a diverse variety of long-term funding options. Pension funds in sub-Saharan Africa collectively manage $350 billion in assets, while the Namibian retirement fund is estimated to be larger than the country's annual GDP. Nonetheless, the increase in pension funds has not translated into increased investments in critical areas of development need. The pension funds of Nigeria invested a mere 0.5 per cent of their assets in infrastructure, partly because of negative risk perceptions. In effect, even when capital is available, the financial infrastructure required to unlock these resources for development financing is only nascent. Confronted by low domestic resources, African Governments have turned to external sources of financing.

C. Mobilizing external public financing

28. Multilateral and bilateral financing constitute the main sources of public external financing, in particular for countries with limited or no access to capital markets.

Policy conditionalities, scale of financing, maturity mismatches and eligibility challenges

29. As of 2019, bilateral and multilateral loans to Africa totalled $324.5 billion, representing approximately 60 per cent of the continent's financing. Notwithstanding the concessional nature of such loans, external public financing poses several challenges for African countries. First, some view the associated policy conditionalities as overly restrictive. Second, relative to commercial financing, the tenor of public financing tends to be relatively short and hence inappropriate for long-term infrastructure financing. Deploying external public financing for infrastructure projects can lead to maturity mismatches. Third, the scale of such financing is often inadequate to meet the growing financing needs of eligible countries. For instance, net bilateral official development assistance (ODA) flows from Development Assistance Committee members to sub-Saharan Africa amount only to some $50 billion annually compared to annual infrastructure needs of $130 billion–$170 billion.

30. Furthermore, the balance sheets of multilateral development banks have been stretched by the pandemic, rendering it unlikely that they can adequately respond to the financing needs of developing countries. IMF lending through the Poverty Reduction and Growth Facility, amounting to 6.5 billion in special drawing rights (SDR) in 2020, exceeded the long-term capacity of the Facility, which is estimated at SDR 1.25 billion.

31. In addition, the resources committed to low-income African countries by multilateral development banks represent 26 per cent of their financing needs. Fourth, middle-income countries are generally ineligible for public external financing at concessionary rates, even though virtually all countries have been severely affected by the pandemic.

D. Mobilizing external private financing

1. Interest rate risks

32. Faced with the challenges of securing public financing, countries have increasingly turned to external capital markets to supplement their financing needs. Access to external capital markets, however, is limited and costly. Currently only 21 African countries have a track record of capital market access. Added to which, African countries with market access pay higher interest rates than their peers with similar or worse economic fundamentals, as proxied by their credit risk ratings.

33. Estimates of what may be termed the "African premium" range from 100 to 260 basis points even after accounting for economic fundamentals. For instance, even though Greece has a lower credit rating (BB-) than Morocco (BB+), the country's 10-year sovereign bond, issued in 2020, has a coupon of 1.5 per cent compared to 2 per cent for 10-year bonds offered by Morocco in the same year. Furthermore, the yield spread on Moroccan bonds (235 basis points) was double that of the Greek spread (112 basis points). Low credit ratings increase interest costs for all entities in the financing system, since State-owned companies, banks and corporate bond issuers cannot be rated higher than the sovereign rating. Thus, the African premium is not only a premium on Governments but a premium on the entire domestic value chain.

34. Information asymmetries underpinned by negative risk perceptions and the limited liquidity of African sovereign bonds contribute to the African premium. While advanced countries have a long history of using repurchase agreement markets to enhance the liquidity of financial instruments, such markets in Africa are not well developed.

2. Challenges in mobilizing climate finance

35. Africa will need investments of over $3 trillion in mitigation and adaptation by 2030 in order to implement its nationally determined contributions. This requires significant, accessible and predictable inflows of conditional finance. Despite the vast opportunities for green investments, the continent attracts less than 1 per cent of global green bond issuances, estimated at $600 billion. While, globally, green bonds attract lower interest rates than so-called "vanilla" bonds, the cost of African green bond issuance is more than twice the amount paid by similarly rated peers. The lack of appropriate vehicles to channel climate financing, coupled with weak domestic capacity, has limited the ability of African countries to attract climate financing at scale.

3. Exchange rate and inflationary risk

36. Rising inflationary expectations compounded by a contractionary monetary policy stance in advanced economies are exerting upward pressure on interest rates, with adverse implications for the cost of credit, debt rollovers, portfolio capital flows and exchange rates. The Federal Reserve System expects to raise interest rates three times in 2022 in response to rising inflation expectations. The Bank of England raised interest rates for the first time in more than three years in December 2021, from 0.1 to 0.25 per cent, and the European Central Bank is also scaling down economic support measures, even though it has yet to increase interest rates. Cumulatively, these developments will translate into higher interest rates from public and private financing sources, resulting in capital reversals from developing countries.

37. Increased imports, rising inflationary pressures and sluggish global recovery have contributed to exchange rate depreciations in several countries, which will effectively increase debt servicing and amortization costs. Between the fourth quarter of 2020 and first quarter of 2021, the Ethiopian birr (19.6 per cent), Angolan kwanza (11.6 per cent), Congolese franc (10.7 per cent) and

Algerian dinar (10.2 per cent) experienced substantial depreciations, with adverse consequences for their foreign currency-denominated debt service obligations.

38. Access to scaled-up financing on competitive terms will be critical for recovery in Africa. The scale of financing required to support an enduring recovery is, however, beyond the scope of public financing alone. In this context, efforts by Africa to support the recovery should aim to leverage the estimated $379 trillion in global financial assets held mostly by private sector financial institutions.

V. Leveraging financing opportunities: breaking new ground

39. Closing the Sustainable Development Goal financing gap will require a disruptive approach that promotes innovative finance and long-term investment. There is therefore an urgent need for innovative and sustainable options to scale up public financing, crowd in private sector financing on favourable terms, leverage climate financing and facilitate trade finance.

A. Scaling up public financing

40. Multilateral development banks will require additional concessional resources to effectively support countries' response to the crisis. The recapitalization of multilateral development banks, including through on-lending of special drawing rights, should therefore be a priority. Special drawing rights can be deployed at relatively low cost with little impact on the debt burden. Frontloading International Development Association (IDA) disbursements to eligible countries will also support their recovery without significantly elevating their debt vulnerabilities.

41. Efforts to recapitalize multilateral development banks should be accompanied by measures to ensure that they adopt more flexible financing arrangements, for example to allow crisis lending, and more flexibility in providing concessional assistance to address poverty in middle-income countries. Furthermore, these banks should be encouraged to provide clearer guidelines on when countries should graduate from receiving concessional or non-concessional financial assistance.

42. Bilateral donors should also follow the lead of China by on-lending a portion of their unutilized special drawing rights to low and middle-income countries. An analysis of special drawing rights by ECA and the Economic Commission for Latin America and the Caribbean shows significantly low (5.9 per cent) utilization rates by developed countries compared to developing countries (42.9 per cent), with even higher rates for Africa (52.37 per cent). The on-lending of $100 billion in special drawing rights to Africa would be a cost-effective means of financing the continent's recovery.

B. Blending public and private resources

43. In accordance with the Addis Ababa Action Agenda, blended financing approaches are potentially catalytic: they could ensure that public resources leverage and de-risk private financing to support the development of Africa. Private finance mobilization has not increased significantly beyond 2015 levels, however, and continues to face multiple challenges. Public finance mobilizes around $30 billion of private finance annually, with most of the resources going to middle-income countries where projects are easier to realize. Through the

provision of credit guarantees, such as policy-based guarantees, and enhancements needed to lower perceived default risks, blended public and private financing can improve credit ratings. As a result of a partial guarantee by IDA, Fitch Ratings and Moody's upgraded the credit rating of Ghana from B/B3 to BB-/B1, enabling the country to borrow at a lower rate than its previous bond issuances and resulting in a 14.25 percentage point savings in interest payments.

C. Lowering the cost of commercial credit: Liquidity and Sustainability Facility

44. Reducing the cost of commercial borrowing will strengthen the development impact of private credit and minimize the debt vulnerabilities of borrowers. To compress yields on African sovereign bonds, the Pacific Investment Management Company and ECA launched the Liquidity and Sustainability Facility, a repurchase agreement facility that aims to compress the yields on African sovereign bonds by enhancing the liquidity and attractiveness of such instruments. The financing opportunities provided by the Facility are expected to expand the pool of institutional investors in African sovereign bonds, improve market access opportunities and expedite the graduation of market-access countries from the IMF Poverty Reduction and Growth Facility. This will help free up much-needed resources for the poorer countries with limited opportunities for market access. Currently, four relatively strong economies with market access (namely, Cameroon, Côte d'Ivoire, Ghana and Kenya) rank among the top five debtors under the Poverty Reduction and Growth Facility and account for SDR 3.7 billion or 29 per cent of all Facility loans outstanding.

D. Crowding in private financing at affordable rates

45. The experiences of African countries that have recently returned to capital markets point to strategies that can lead to lower borrowing costs and improved debt management. Rwanda was able to lower its Eurobond coupon rate by 1 per cent through an intensive effort of engaging and communicating with investors in more than 100 roadshows, aimed at minimizing risk perceptions and information asymmetries. Some African countries have been successful in using liability management strategies to extend the maturity of their outstanding bonds, in some cases by as much as 30 years. Out of the eight African countries that issued Eurobonds in 2021, five included a liability management component that extended the maturity of 65 per cent to 85 per cent of their outstanding bonds, higher than the norm of 40–60 per cent.

E. Boosting the issuance of sustainability linked bonds

46. Private sector demand for investment products that promote sustainable development has been rising steeply in recent years. These so-called "sustainability-themed products" were worth $3.2 trillion in 2020. Despite the vast green resources of Africa and increased investor demand for sustainability-themed products, the continent accounts for less than 1 per cent of global green bond issuances. The Liquidity and Sustainability Facility can incentivize green bond issuances by offering preferred repurchase agreement rates to institutional investors that refinance their positions using African green bonds as collateral.

47. Advocacy to factor the state of a country's natural capital into sovereign credit rating considerations could contribute to better ratings and lower borrowing costs. Nature performance bonds are a sovereign debt instrument that link the cost of sovereign debt to success in protecting or enhancing a

country's valued and productive natural capital. Successfully deployed, such bonds can improve African credit ratings and incentivize initiatives that improve nature and climate outcomes.

F. Leveraging the vast pension fund resources of Africa

48. Assets managed by African institutional investors are expected to reach $1.8 trillion by 2020, with the expansion of pension funds in Africa as the primary driver. To incentivize pension fund managers to invest more actively in the continent, countries are designing innovative mechanisms. In Kenya, more than 20 pension funds have formed a consortium to invest in infrastructure, pooling their capacity to mitigate risks and identify opportunities. Governments and foreign donors can mitigate the risk perceptions of fund managers by issuing guarantees and creating regulatory reforms that enhance transparency, reduce information asymmetries and promote informed investment decisions.

G. Strengthening the pipeline of bankable projects

49. Strengthening the pipeline of bankable projects will be essential to attract global institutional investors. This can be achieved by encouraging African regional development banks to invest in strengthening capacities for the design of investment-ready bankable projects that can speed up the recovery path from COVID-19. Typically, the bankability of projects should be determined at the project development stage and the integrity of the bankable projects should be enhanced through policy coordination and the provision of institutional support.

H. Deepening domestic capital markets

50. Deepening domestic financial markets is critical for increasing resource availability, and also reducing exposure to possible foreign exchange risks. African stock exchanges must modernize their trading systems, minimize settlement lag times and transaction costs, and improve quotation methods. Stable political and macroeconomic environments, credible legal frameworks capable of enforcing financial contracts and independent regulators that ensure fairness and transparency are all prerequisites for capital market development. Accelerating progress on the African Continental Free Trade Area could boost the development of African financial markets. The enlargement of markets under the Area would enable cross-listing, efficient pricing, increased competitiveness in regional and global value chains, and more opportunities for innovative business financing.

I. Scaling impact investments

51. Impact investments leverage new sources of capital in sectors such as environment that lack sufficient development financing. Impact investments are projected to represent a global market of $500 billion in the next five to ten years and the prospects of impact investments look promising for Africa. In all, 43 per cent of impact investors have allocated funds to Africa, more than any other emerging market region. Furthermore, 52 per cent of surveyed investors plan to increase their investments in Africa over the next five years. Nonetheless, impact investing is not at a sufficient scale to meet the continent's financing needs, owing in part to negative risk perceptions. As a result, only a handful of private equity funds have raised more than $1 billion. Creating a stable macro-environment and creating platforms that enhance information

flows between investors and Governments is key to building trust and minimizing unfounded perceptions.

J. Leveraging the African Institutional Infrastructure Co-Investment Platform initiative

52. Well-designed investment platforms can effectively facilitate development financing by convening investors and Governments in one space. The 5% Agenda is a joint initiative of the African Union Development Agency and the New Partnership for Africa's Development, under which African Governments agree to collaborate on project design and the alignment of infrastructure investment policy regimes with the investment mandates of African asset owners. In exchange, African institutional investors agree to increase their allocations to African infrastructure investment to 5 per cent of assets under management and to support the African Institutional Infrastructure Co-Investment Platform initiative, which brings together African sovereign investors and international pension and sovereign fund peers to co-invest in one another's markets across the continent.

K. Boosting intra-African trade through improved payment systems

53. Reducing the currently high transaction costs associated with multiple currency regimes can maximize revenues from intra-African trade. The Pan-African Payments and Settlement System enables instant, cross-border payments in local currencies between African markets by simplifying cross-border transactions and reducing the dependence on hard currencies for these transactions.

54. The African Trade Exchange, an initiative of ECA, the African Export-Import Bank and the secretariat of the African Continental Free Trade Area, is a business-to-business platform which serves as a virtual marketplace for buyers and suppliers, based on the African Continental Free Trade Area rules. It can foster the economic growth and recovery of Africa by strengthening regional supply chains and promoting business linkages. For micro, small and medium-scale enterprises, the platform can significantly facilitate their integration into regional value chains and can help them to withstand shocks in their domestic markets.

VI. Conclusions

55. The financing needs of the continent have been exacerbated by the pandemic, resulting in a widening of the financing gap and increased debt vulnerabilities underpinned by a growing reliance on private financing. Reducing the cost of commercial credit will be vital to mitigate debt vulnerabilities. Nevertheless, scaling up financing will require measures that build synergies between domestic and external financing from both public and private sources.

56. At the domestic level, strengthening tax administration capacities and promoting value addition will be vital to stemming illicit financial flows and widening the tax base. Furthermore, enhancing trust and transparency of the regulatory environment, including through the creation of credit risk agencies, will be critical to crowding in pension funds, deepening domestic capital markets and improving credit risk perceptions.

57. At the external level, improving access to concessional financing, including through the recapitalization of multilateral development banks, and designing a global financial architecture that is agile and responsive to the financing needs of low-income and vulnerable middle-income countries are imperative. That said, the bulk of global financial assets reside with the private sector. Blended financing approaches that de-risk and leverage private financing coupled with the deepening of secondary markets for African sovereign bonds will be critical in compressing Eurobond yields and mitigating debt vulnerabilities.

58. Ultimately, the risk appetite of investors will be influenced by the decisions of domestic investors, including pension funds. Hence, mobilizing the continent's own resources for development is key to closing its financing gap.

59. Based on these observations the following recommendations are put forward. Policymakers should:

(a) Improve transparency in their legal and regulatory regimes to reduce information asymmetries and enhance informed decision making by investors;

(b) Support the operationalization of the Liquidity and Sustainability Facility, including efforts to on-lend special drawing rights to the Facility;

(c) Support efforts to recapitalize multilateral development banks;

(d) Invest in strengthening capacities to develop bankable projects aimed at attracting potential investors;

(e) Create an enabling regulatory environment to deepen domestic capital markets and incentivize the local investments of pension fund resources.

60. In addition, the following policy issues and key questions may be raised for discussion:

(a) What measures should African countries put in place to crowd in private sector financing? What type of technical support do Governments need?

(b) How can African countries utilize their special drawing rights more effectively?

(c) What measures are African countries putting in place to mobilize climate financing?

(d) What type of technical support do Governments need?

(e) Which of the proposed financing measures resonate well with African countries? What are the experiences and lessons learned regarding the financing measures?

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