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AFRICAN DEVELOPMENT BANK

SEPARATION OF ACCOUNTS - ORDINARY CAPITAL RESOURCES AND SPECIAL RESOURCES

(Note by the Executive Secretary)

63-616

1. The Draft Agreement provides for a strict separation between the Bank's ordinary capital resources and special resources at its disposal. This separation is expressed in provisions for their separate administration (Arts. 8 - 10), the keeping of separate accounts and the preparation of separate balance sheets and their respective liabilities (Arts. 11,13). The purpose of this separation is to ensure the appropriate management and use of both types of resources.

Ordinary Capital Resources

Ordinary capital resources (defined in Art.2) include the Bank's subscribed equity capital, the reserves and surpluses accumulated by the Bank as a result of its ordinary operations, as well as funds secured through borrowing on market terms, whether from private sources or from national or international financial institutions. The Bank will need such funds in order to supplement the always scarce funds that may be available on more favourable terms (grants or "soft" loans). It will have ample use for them in the financing of self-supporting projects (e.g. in the fields of energy, transportation, industry) which produce the revenue with which to repay loans granted on commercial terms.

3. In order to be able to appeal to the capital markets and other institutions operating on market terms, the Bank must ensure that its available guarantees (chiefly its paid-up capital and its callable capital) are reserved for such commitments and will not be drawn down by demands arising from the Bank's special operations, This assurance can be made effective only through a strict separation of the accounts in which the receipt and disbursement of these two types of resources are recorded.

Note Mr. Abdul G. El Emary on leave from the International Finance Corporation, formerly Governor of the Bank of Egypt, served as a Consultant to the Executive Secretary in the preparation of this Note.

4. Reserving the Bank's own ordinary resources (equity capital, reserves and surpluses) for operations on market terms meets also the requirement that the Bank must earn from these operations enough to provide for its heavy administrative expenses (including non-reimbursed technical assistance costs). Use of these resources for low-interest ("soft") loan operations would compel the Bank to draw down its capital in order to meet its current running expenses - a practice which would be as destructive of the Bank's own resources as of its standing for securing additional resources in the capital markets.

Special Resources

5. As stated at the outset, separation is as necessary to protect the Bank's special resources as its ordinary capital resources; the former indeed are normally received by the Bank subject to special provisions regarding their use and/or administration. Thus, in the case of the special loans provided under Art. 24, the proceeds may be used by the Bank only to finance "expenditure in respect of goods or services produced in the territory of (the lending) member for the purpose of a project to be carried out in the territory of another member". Other special funds may be received by the Bank for the financing of particular projects or types of projects or for expenditure on goods or services of a particular (normally the grantor) country, or for investment in accordance with special procedures. The Bank's commitment to abide by the special terms and conditions accompanying such special grants or loans requires their separation from the Bank's ordinary capital resources whose uses are not subject to the same terms.

6. Because these terms may vary as between different special funds, these must be kept as strictly apart from each other, as will all special from all ordinary capital resources. Similarly, separate accounts will

be needed within the ordinary capital resources of the Bank so as to ensure that the Bank will not commit, in its ordinary operations, amounts in a given currency in excess of those which it has secured through its own borrowings (Art. 19(3)).

Common Rules

7. This separation of accounts does not mean, however, that the Bank's projects must also be separated in terms of the funds invested in them. While many projects by their nature are appropriately financed by one type of resource only (e.g. non-income generating infrastructure projects cannot be financed by funds secured on ordinary market terms), some projects may properly justify simultaneous investments on market terms and on preferential terms; thus the Bank may, in helping to finance an important industrial venture, grant a loan on market terms for the purchase of its machinery, and at the same time give the same enterprise a "soft' loan for providing workers' housing - in fact, the Bank may have been given the administration of a Special Fund precisely to finance such low-cost housing construction. The funds thus made available will be separately accounted for and strict banking rules will be applied to the 'hard' loan for machinery, but this should in no way restrict the legitimate flexibility in the Bank's assistance to a wide range of development needs.

8. Whatever may be the types of resources used and the resulting strictness or leniency of the terms to be accorded the recipient by the Bank, there can be no relaxation in the standards which the Bank will apply to the selection, study and examination of the projects before it. Under the best of circumstances, the Bank's resources of all types will be severely limited in relation to the financial needs of development in Africa. No

matter how easy, therefore, the terms on which the Bank may receive - and thus be able to invest - some of its resources, it must make sure that that they are used only for projects which careful analysis indicates are likely to be of substantial benefit to its members.

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