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Infrastructure Finance

Uncertainty and Change in Sub-Saharan Africa

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Traditional finance models have faltered in the wake of the global economic crisis

The future of infrastructure finance in Africa is at a crossroads. Traditional finance models have faltered in the wake of the global economic crisis, compounded by significant political and systemic obstacles that could derail a nascent recovery.

The market for infrastructure finance has changed and will continue to evolve. Infrastructure is critical to Africa's future and the potential commercial and developmental advantages to improving African infrastructure are enormous.

The challenge for investors, governments and other stakeholders is to harness this potential in the face of complex risks and uncertainties.

This paper explores the recent gains that Africa has made to bridge the infrastructure gap, the challenges facing stakeholders and the outlook for the future.

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Infrastructure at a crossroads

In Sub-Saharan Africa, private participation in infrastructure (PPI) projects dropped 46% in 2009 compared to 2008, and 65% in the last quarter—significantly worse than the averages for the developing world as a whole

The recent global economic crisis has had a profound impact on infrastructure investment across the developing world, although there are some indications of recovery.

Excluding the five largest developing economies (Brazil, China, India, Turkey and Russia), private investment dropped 32% in 2009 compared to 2008, and 58% in the last quarter of 2009 compared to fourth quarter 2008. In Sub-Saharan Africa, private participation in infrastructure (PPI) projects dropped 46% in 2009 compared to 2008, and 65% in the last quarter—significantly worse than the averages for the developing world as a whole.

The recent global economic crisis has had a profound impact on infrastructure investment across the developing world

Sector Performance

The news is not all bad, however. Many African countries have made significant progress in recent years towards expanding mobile phone coverage.

To date, 50% of Africans live within range of a GSM signal, up from 5% in 1999. The telecoms sector generally is growing rapidly and requires little support from development partners and multilateral institutions.

The sector was responsible for 87% of total investment in African infrastructure in 2008—largely due to faster payback periods and shorter-term debt.

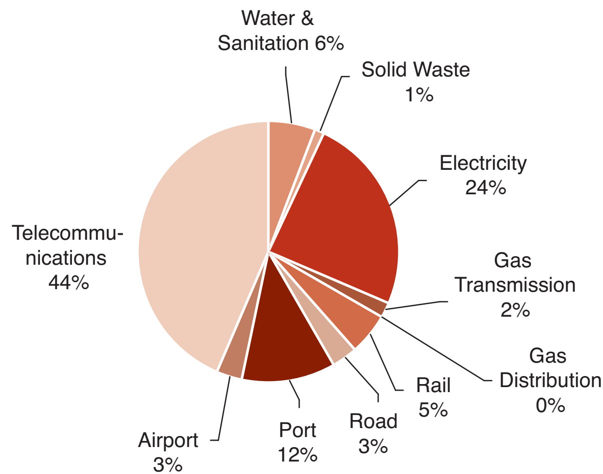
Transport has suffered the most significant decline in demand and investment directly related to the economic crisis, but governments generally remained committed to their

Thirty African countries experience chronic power outages and high transportation costs increase the price of goods on the continent by an average 75%[1]

public-private partnership agreements. Government stimulus packages have in part helped to offset the loss of private financing, as have developed nations and multilateral institutions which continue to honour their development agreements.

In 2009, Sub-Saharan Africa had zero projects delayed, at risk of being delayed or cancelled as a result of the crisis. By comparison, every other region globally suffered some instances of delay, risk of delay or cancellation although these regions also have higher investment and greater numbers of ongoing and completed projects.

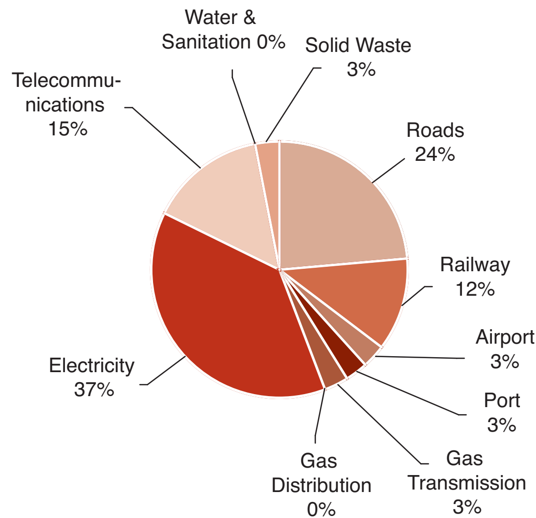
Completed Projects (1990-2008, Africa)



Source: The World Bank, PPI Project Database April 2010

Poor infrastructure reduces Africa's per capita GDP growth by 2% a year and cuts productivity by 40%[2]

Projects in the Pipeline (1990 -2008, Africa)



Source: The World Bank, PPI Project Database April 2010

[1]The World Bank, 'Africa's Infrastructure: A Time for Transformation' Nov 2009
[2]The World Bank, 'Africa's Infrastructure: A Time for Transformation' Nov 2009

The rise and fall of infrastructure finance

The question is whether the global economic crisis will have a longer, systemic impact on infrastructure finance

Growing Demand: 1990–2007

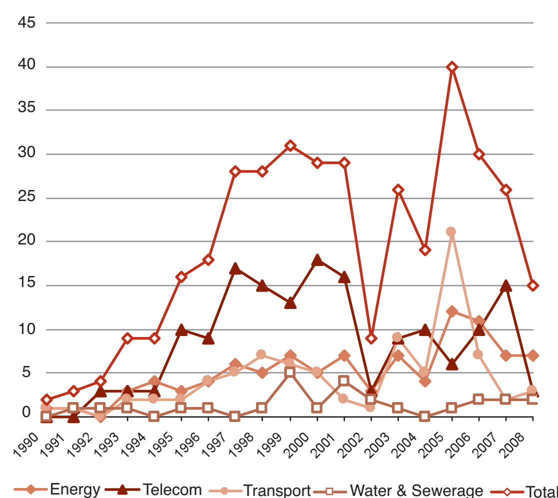
A sea change in African infrastructure finance occurred in the 1990s when governments began turning to the private sector to build, operate, finance, own and transfer assets. Recognising a rapidly growing demand for telecommunications facilities, power plants, ports and airports, these governments hoped that private expertise and finance would help meet this demand.

Massive increases in liquidity from 2002-2007 created a positive investment climate for infrastructure project finance in emerging markets. Some larger African projects benefited directly from financing by international lenders.

In other cases, local or regional African banks borrowed from international banks or capital markets to finance PPP loans or they drew upon credit lines with international banks to secure lending for infrastructure projects.

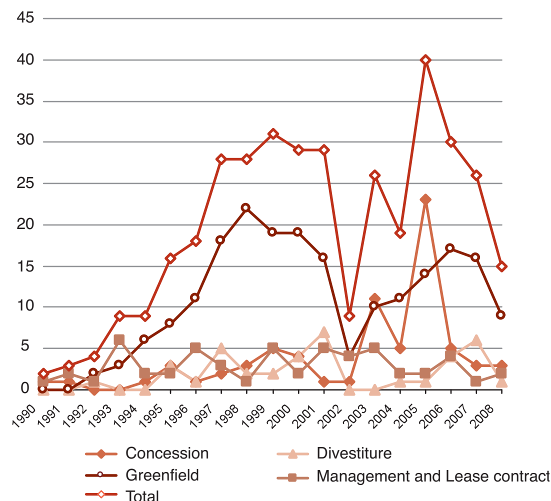
Critics argue that private provision has contributed to adverse environmental impact, and that some services have become less affordable upon the termination of public subsidies. However, the data indicates that private investment in African infrastructure projects has led to a remarkable increase in the number of projects and investment levels since 1990.

Number of Projects by Primary Sector, Africa



Source: The World Bank, PPI Project Database April 2010

Number of Projects by Type, Africa



Source: The World Bank, PPI Project Database April 2010

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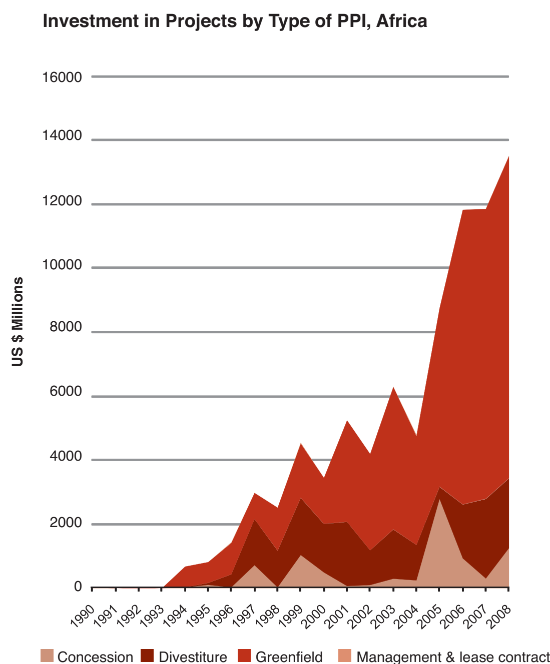

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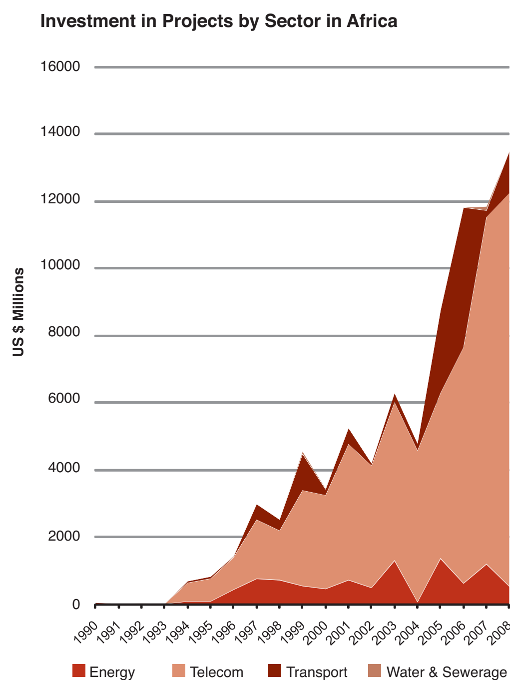


Source: The World Bank, PPI Project Database April 2010

The Crisis Unfolds

That burst of liquidity has dried up in the wake of the global economic crisis. Infrastructure projects now face much more stringent financial conditions, not only through the higher cost of financing but also through lower debt-to-equity ratios, reduced tenor and more conservative risk allocation structures.

Moreover, banks are opting for syndicated lending rather than taking sole-underwriting positions at a fixed price on large infrastructure deals. Banks also now require market flex (the right for lenders to increase interest rates) on pricing and other terms. Borrowers need to work harder to mitigate the risk of changes in terms that may arise from the market flex process.

Some local banks and investment funds in Africa still possess the liquidity necessary to participate in syndicated or club deals. But there are fewer such lenders now, their interest rates are increasing and hold levels decreasing. Even in the best of times, local African financiers could rarely supply all of the financing needed for large international projects without international lenders and regional or international direct foreign investment. Now, the process of raising capital for infrastructure is that much more difficult.

Global infrastructure finance has experienced downturns before, notably and recently during the aftermath of the terrorist attacks of September 11, 2001. Like other financial markets, the market for infrastructure finance is not immune to global shocks. The question is whether the global economic crisis will have a longer, systemic impact on infrastructure finance. The evidence to date appears to indicate that it will, but the crisis converges with other profound changes in the African infrastructure finance sector. The factors currently influencing infrastructure finance in Africa are more complicated than those contributing to the global economic crisis alone. Project closure rates and trends in private sector participation illustrate the complicated effect of the crisis and other factors.

Signs of Recovery

Project closure rates were 26% lower in the initial months of the crisis (August to November 2008) compared to the same period the previous year. Project closure rates improved somewhat to 15% lower than 2007 levels during the last quarter of 2008, and there were no projects delayed, at risk of delay or cancelled during the last quarter of 2009. The delay or cancellation of infrastructure projects in sub-Saharan Africa has tended to be the result of local factors, such as regulatory constraints and the absence of reliable information.

Until recently, privatisation had been the dominant form of private sector participation but an examination of deals currently in the pipeline (many of them stalled by the effects of the global economic crisis and local factors) shows that there is a move from privatisation to new assets.

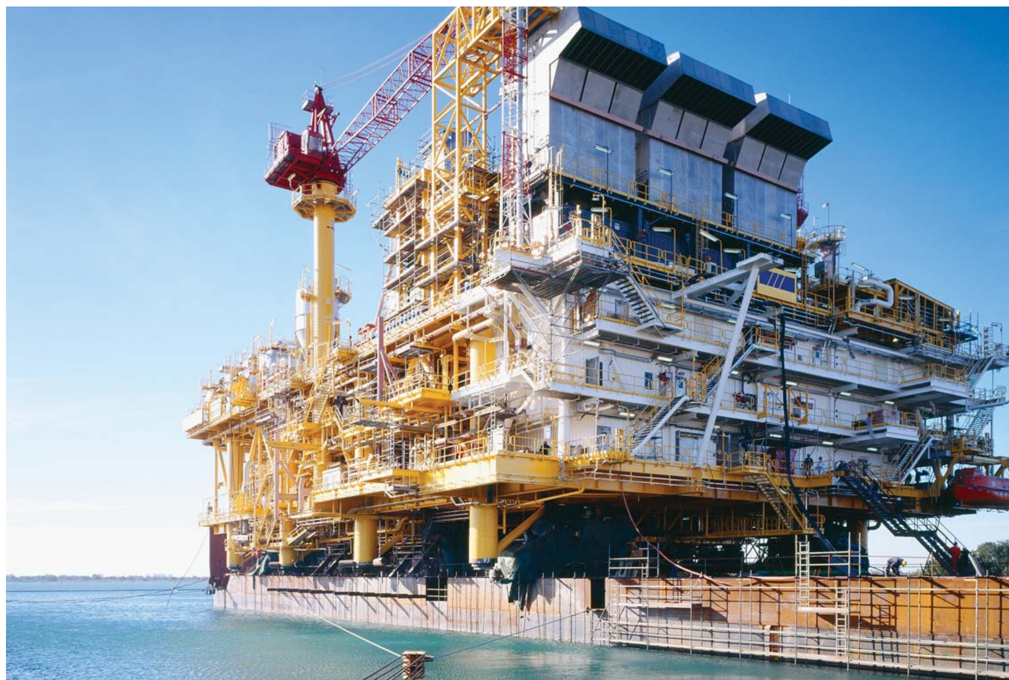
Greenfield ventures made up 67% of total investments in 2008, while the relative and total value of investments in concessions and divestitures has fallen. Governments are using contract forms of privatisation rather than asset sale and embracing concession-type structures.

Comparing historic deals to deals in the pipeline, the trend indicates that there is a move towards concessions/BOTs versus management and lease contracts. This could indicate a worrying 'herd mentality' among governments who may perceive less risk but attempts to create a 'one-size-fits-all' approach could be contributing to bottlenecks in the deals pipeline.

The future of infrastructure finance

To address the shortfall in private infrastructure finance, African governments must control monetary and fiscal policies carefully to avoid falling back into the slow-growth gap. Development agencies can support this process through higher, more responsive and better-targeted assistance.

Unless African governments invest in project preparation, the private sector will not respond effectively



Development partner countries must honour their commitments to Africa's development goals. Fluctuations in global development funds—driven by the uncertainty created by the global economic crisis—are not helpful to the infrastructure finance sector, which requires steady and reliable sources of investment over the medium- and long-term to complete critical, large-scale projects on time.

Multilateral organisations have created vehicles to supplement development partner and IFI funding for commercial finance in order to jumpstart and revive new and existing infrastructure PPPs. These multilaterally-anchored vehicles must focus on project preparation, difficult projects with the highest impact and value and development as projects move towards completion. Primarily, the focus should be on maintaining concessions rather than new investments.

Some African governments are crafting interim emergency measures to keep PPP project development pipelines alive. These measures include accelerating and simplifying the PPP project approval process and providing direct financial support to projects via loans, equity, grants or guarantees.

Investment in African infrastructure is laden with challenges. Issues around transparency, unclear policies and weak project preparation obstruct the flow of capital to African infrastructure projects. Low per capita income, poor cross-border coordination, absent or malfunctioning regulatory structures, high political risk, poor sovereign credit ratings and heavily degraded infrastructure are just a few of many challenges facing investors.

The Way Forward

In the short term, African economies must develop domestic drivers of growth. The continent needs to boost domestic resource mobilization to support growth and investment in the infrastructure sector. Several initiatives are already underway; in Cape Verde, the Central Bank introduced Treasury

How can donors and governments avoid taking on so much project risk that private partners no longer have incentives to meet performance expectations?

bills to encourage private domestic saving. In February 2009, the Kenyan government issued an infrastructure bond of 18.5 billion shillings (USD 232.6 million) with 12-year maturity. The bond was oversubscribed, a testimony to the existence of a substantial untapped domestic saving capacity.

In the long run, Africa must sustain and intensify investment in infrastructure through a variety of means. Development partners should be encouraged to increase financial support; flexible domestic policy frameworks will facilitate increased budgetary allocations to public infrastructure; the private sector can lead infrastructure investment and management of infrastructure services and governments must explore and encourage management arrangements that accelerate cost recovery.

Infrastructure investment in developing countries will eventually recover because infrastructure is critical to development and progress. But the recovery is likely to be driven by governments and development partners, at least in the short term. Sources of private equity for project finance will be scarce for the foreseeable future.

The global economic crisis has exacerbated existing weaknesses and vulnerabilities among African governments. Bridging the 'infrastructure gap' will demand innovative approaches to both raising additional finance and using infrastructure more efficiently and more intelligently, through new technologies, demand management strategies, regulatory changes and improved planning.

Development partners, governments and non-government entities with a vested interest in PPI projects in Sub-Saharan Africa can support the sector by unlocking deals in the pipeline for the electricity and rail sectors, overcoming policy hurdles on airports and focusing on transaction structuring. There is also a compelling need to encourage the use of lease and management contracts, particularly for privatisations. Governments and non-governmental organisations can improve their involvement in transactions.

Risky measures to keep PPP project development pipelines moving must be abandoned in favour of efforts to keep existing PPPs afloat. Business risk in the infrastructure sector will remain relatively low despite changes in the macroeconomic environment.

Regardless of the financial crisis, the infrastructure sector will continue to attract investors and lenders because the sector fundamentally offers core services that customers cannot do without. Public and private investors from China, India, various Arab countries and African developers are currently showing significant interest. There are tremendous, untapped opportunities in the infrastructure finance sector.

Africa's infrastructure development depends upon the realisation of these opportunities and an ongoing, unwavering commitment to reform and long-term project support.

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Vishal is a career Investment Banker who specializes in project and infrastructure financings in developing markets. He has served in leadership positions in global advisory – where he has worked with governments, institutions and infrastructure developers in Asia, Eastern Europe, the Americas and the Caribbean. Mr. Agarwal now heads the PPP and Infrastructure Finance Group for PricewaterhouseCoopers. Based in Nairobi, he covers the sub-Saharan Africa region.

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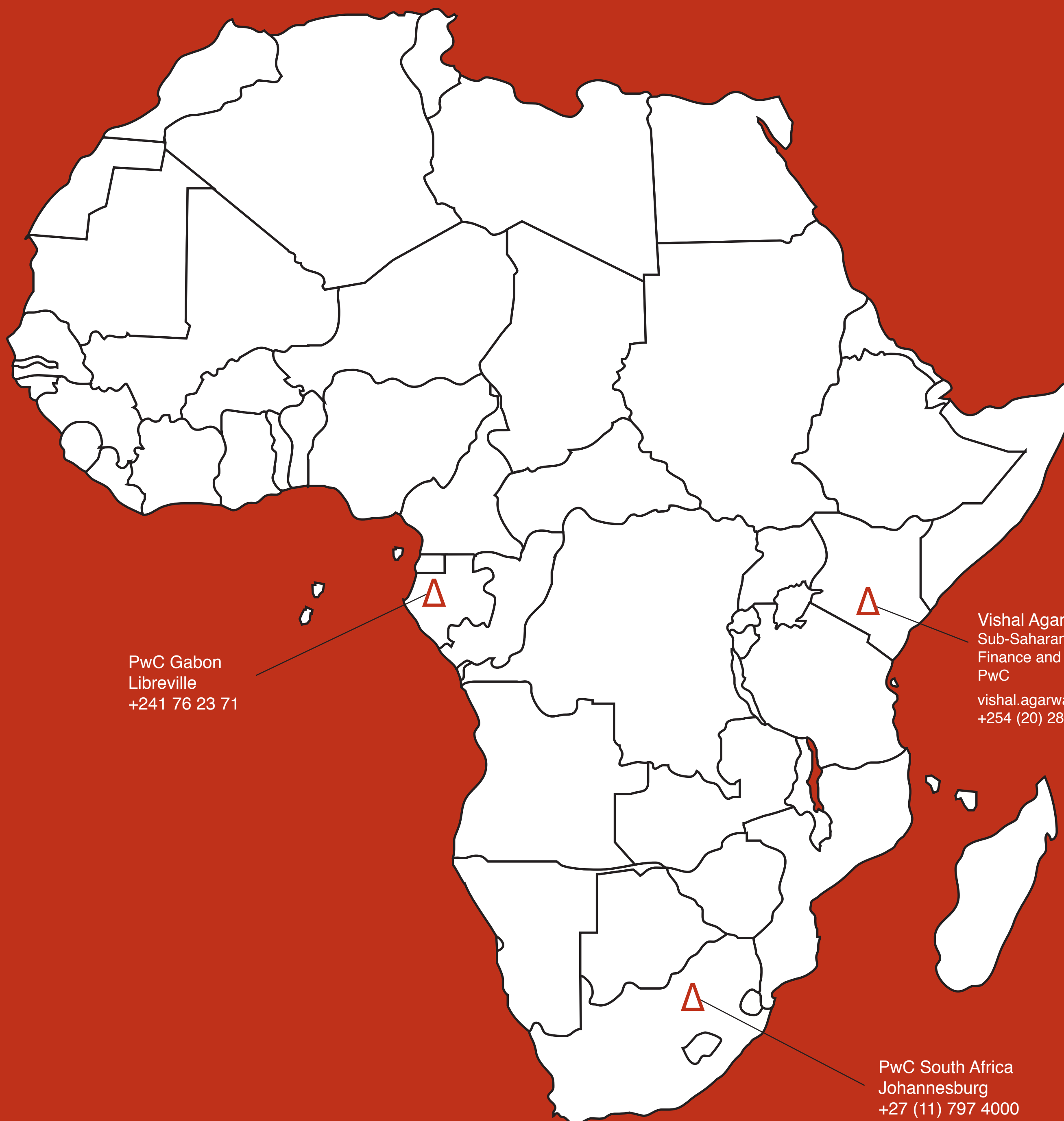

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