Financing for investment in Africa: a role for the G20
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G20 and Africa: infrastructure for development

In June 2012 at Los Cabos, G20 leaders agreed to ‘strengthen efforts to create a more conducive environment for development, including infrastructure investment.’ In line with this resolve, many Sub-Saharan African (SSA) countries are currently focused on developing their economic potential by attracting institutional investors capable of providing long-term capital for investment with the potential to spur growth and development. The G20 discussions on financing for investment present a unique opportunity in this regard. African countries seeking to raise capital must navigate underdeveloped domestic markets which impact on the channels as well as options through which finance for investment can be accessed. This barrier is compounded when financing is sought for the regional or cross-border projects which are at the heart of achieving the integration agenda of SSA – a particular challenge recognised by the G20 Development Working Group.

Infrastructure investment has been a major focus for the development of Africa, as is elaborated by the African Union (AU) in its Programme for Infrastructure Development in Africa (PIDA). This is a Priority Action Plan highlighting a number of regional infrastructure projects which was endorsed by African heads of state in 2012. Due to SSA’s rapid population growth, finance for investment in infrastructure has mostly been channelled to the electricity sector to date. There are still massive needs on the continent in energy, transport and water, to name just a few sectors. The process of financing infrastructure development presents a wide array of multi-layered challenges for SSA countries which are worth consideration in the G20 context, especially if the forum is to make a contribution to sustainable growth and job creation in Africa.

Challenges for financing African infrastructure

Apart from the current state of the financial markets in most SSA countries (often non-existent domestic capital markets), finance for investment in Africa is hampered by a number
of factors relating to the size, complexity and viability of infrastructure projects. Using energy-related infrastructure projects as a case in point, in order to address the challenge of financing projects of this nature, a host of issues have to be tackled. First, many of these projects are costly to prepare and develop. There are ongoing challenges in project preparation and planning that must be surmounted to ensure that the result is a bankable proposal of interest to investors. Second, the regional aspect of energy development in Africa is difficult to factor into traditional financing arrangements and is often given very little weight in negotiations. Third, there is a need to accompany physical infrastructure development in SSA with the necessary ‘soft’ elements such as upskilling of labour, regulatory adaptation, and streamlining of administrative requirements.

Using Inga III (a proposed hydroelectric project in the Democratic Republic of Congo) as an example, it was estimated that the project would cost US$10 billion, and that the costs of preparing the project would be 9 per cent of the actual project cost. It was expected that these preparation costs would be covered by private investors. However, there was an unwillingness to commit any funds to the preliminary process of project development. The large amount of capital needed meant that financing could only be raised by bringing together a diverse network of investors including multilateral institutions, private investors and governments. The challenge of financing project preparation was compounded by the complexities of a multi-party arrangement.

The AU has identified regional transformational projects such as Inga III as a key factor in increasing the economic competitiveness of SSA. However, a major challenge exists in the lack of leadership or ownership of projects located outside of countries that ought to benefit from the projects. This impacts the pace at which these projects are developed, slowing down the realisation of projected benefits. This, in turn, poses a number of challenges regarding financing for investment, as investors require high levels of certainty (such as sovereign guarantees) before committing funds to project development.

It is necessary for SSA countries to consider alternative methods by which infrastructure projects can be financed. Here, the financing for investment discussions in the G20 could make a real contribution, including through the sharing of experiences of different regions in the world, as well as by encouraging a greater understanding of the particular challenges facing Africa.

**Examples of financing mechanisms**
Focusing particularly on specific attributes of infrastructure projects, a range of alternatives by which governments of SSA countries and projects sponsors can raise finance for investment could be explored in the G20 discussions.

**Bond finance**

Bond issues can be advantageous, based on the size of the bond, which is normally larger than a bank loan and thus provides a substantially larger amount of capital. In the event that governments of SSA countries decide to sell bonds, issues relating to interest rates and maturities should, however, be considered carefully, as bonds are generally considered to be less flexible than bank loans and the creditworthiness of governments is tied to regularly scheduled repayments. Specifically targeted bonds, such as infrastructure or diaspora bonds, are being used by some SSA countries, with potential for broader application.

**PPPs**

Governments of SSA countries are increasingly adopting public–private partnerships (PPPs) as a viable mechanism for funding infrastructure projects. The benefits of PPPs for SSA countries include shorter delivery timeframes for projects for the public sector, and more manageable project risks due to expertise in the private sector. They have the capacity to deliver value for money on projects, if well-structured. However, PPPs are highly complex policy instruments that require advanced capacity within the public sector to both negotiate and manage.

**SWFs**

Currently only a few SSA countries have established sovereign wealth funds (SWFs) aimed at investing revenue raised from natural resources in areas such as infrastructure development. The option of operating an SWF has so far been reserved for the oil-rich SSA nations such as Nigeria, Angola and, in the near future, Tanzania. SWFs can help to boost domestic growth when earnings from the funds are invested in infrastructure development. If properly managed, SWFs can also impact credit ratings of SSA countries positively.

**Pension funds**

For SSA countries, pension funds can serve as a source of revenue for infrastructure projects that require long-term investments. In 2012, the Government Employees Pension Fund (GEPF) in South Africa invested R1 billion in the green bond issued by the Industrial
Development Corporation (IDC) to finance the development of several renewable energy projects across the country. However, in general pension funds are largely conservative and target low-risk investments, in accordance with the mandate to provide security and flexibility to its clients. The G20 could explore ways to mitigate risks around infrastructure projects that would increase the attractiveness to pension funds.

**African initiatives worthy of G20 support**

Along with its partner institutions, the African Development Bank (AfDB) has taken the initiative in developing the Africa50 Fund, in an attempt to fill the infrastructure funding gap—a necessary factor in unlocking the economic potential of African countries and improving the overall economic performance of the continent. The innovative fund focuses on leveraging resources from central bank reserves, SWFs, pension funds, the African diaspora and high net worth individuals to fund infrastructure projects necessary for development in Africa.

Various roles have been taken up by partner organisations to ensure the success of the Africa50 Fund. The AU has been tasked with providing leadership for regional and international advocacy; the New Partnership for Africa’s Development (NEPAD) agency will host a conference on financing for development which would bring together potential investors for the fund; and the United Nations Economic Commission for Africa (UNECA) will engage individual countries to undertake studies to highlight transformational projects as well as monitor and evaluate the implementation processes for the shortlisted projects. This coordinated approach to promote financing for investment in Africa is a practical response to a complex problem.

**Conclusion**

Financing infrastructure projects in Africa would help to unlock the economic potential of the continent and make a contribution to a number of the overarching objectives of the G20. The challenge begins with the structuring and design of projects, as well as in determining viable processes by which funds for project development can be raised. This requires an absolute mastery of the options available for financing, taking into consideration the specific nature of differing infrastructure projects. In addition to promoting new options for financing for investment, the G20 is well placed to encourage greater linkages between the public and private sector in this regard.
Notes

1. Chijioke Oji, and Catherine Grant Makokera, Program Head, Economic Diplomacy, South African Institute of International Affairs.
8. Ibid.