While Africa faces a huge infrastructure gap, there are measures that Group of 20 (G20) countries and its institutions can take to ensure greater and faster infrastructure investments. G20 institutions, particularly development finance institutions, should undertake enhanced local co-operation with African governments to create more productive infrastructure investment, thereby leading to improvements in connectivity and quality of life for communities across Africa.

Challenge

The infrastructure gap facing Africa is large and growing. It can only be addressed with innovative approaches to attract and leverage private sector investment, while improving the business environment, accelerating build-out processes, and mitigating risks in public-private partnerships, increasing the volume of blended finance, and improving infrastructure investment cycles. Today, private sector investment faces many challenges. These include insufficient and overly risk-averse commitments, low-gross thresholds for “bankability,” and long timelines when international and multilateral financing and guarantees are sought.

Even though infrastructure financing in Africa has reached record highs, the infrastructure gap is growing. According to the Infrastructure Consortium for Africa (ICA), financing for infrastructure reached $100 billion in 2018, significantly higher than African governments’ commitments were 2015–2017 three-year average over the previous three-year average. There have also been continued increases in financing from Arab countries, India, and other non-traditional donors/investors. While the increased financing is welcomed, the ICA estimates for Africa’s financing gap over the next five years. The energy sector remains a key investment target; construction and manufacturing were also top priorities of the G20—have been strongly resilient in attracting investments. For example, FDI volumes to Compact countries have increased by 46% compared to the rest of the continent.

Proposal

Background

Although regional and global efforts address Africa’s infrastructure gap, including those from G20 countries, more is needed to address sustainable, decarbonized/carbon neutral inflows of private capital to finance an investment portfolio.

Development in Africa (PIDA) is a strategic continental initiative that has the buy-in of Africa to mobilize resources and transform Africa through modern infrastructure. Its 51 cross-border infrastructure projects comprise major water, railway, and information and communication technology projects. Likewise, the Africa Investment Forum (AIF) is organized by the African Development Bank (AfDB); it has secured investor interest worth $451 billion and 527 projects. Europe Alliance for Sustainable Investment and Jobs was established to create up to ten million jobs in Africa in the next five years. It is part of the European Union’s (EU) External Investment Plan (EIP), which provides €4.1 billion in grants and exceeding €10 billion for the EIP endgame in 2020.

Among the CwA countries, the countries moving the furthest toward the frontier during this period were Rwanda (+7.53), Togo (+6.96), Côte d’Ivoire (+6.95), and Senegal (+4.11). This reflects a substantial, comprehensive, and continuous commitment to a reform agenda aimed at improving the business environment.

Since the launch of the Compact in 2017, a total of 148 reform commitments have been identified, and all 12 countries have committed to track and report their progress. The World Bank’s DB data suggest that CwA countries—with support from the G20— had better average distance-to-frontier (DTF) scores, and also to a continued increase in financing from Arab countries, India, and other non-traditional donors/investors. While the increased financing is welcomed, the ICA estimates for Africa’s financing gap over the next five years. The energy sector remains a key investment target; construction and manufacturing were also top priorities of the G20—have been strongly resilient in attracting investments. For example, FDI volumes to Compact countries have increased by 46% compared to the rest of the continent.

Ongoing global efforts

While Africa faces a huge infrastructure gap, there are measures that Group of 20 (G20) countries and its institutions can take to ensure greater and faster infrastructure investments. G20 institutions, particularly development finance institutions, should undertake enhanced local co-operation with African governments to create more productive infrastructure investment, thereby leading to improvements in connectivity and quality of life for communities across Africa.

Further analysis shows that compared to the rest of the continent, CwA countries have enacted more reforms to create a more liberal and improved environment for FDI.

The World Bank’s DB data suggest that CwA countries—with support from the G20— had better average distance-to-frontier (DTF) scores, and also to a continued increase in financing from Arab countries, India, and other non-traditional donors/investors. While the increased financing is welcomed, the ICA estimates for Africa’s financing gap over the next five years. The energy sector remains a key investment target; construction and manufacturing were also top priorities of the G20—have been strongly resilient in attracting investments. For example, FDI volumes to Compact countries have increased by 46% compared to the rest of the continent.

Ongoing global efforts

While Africa faces a huge infrastructure gap, there are measures that Group of 20 (G20) countries and its institutions can take to ensure greater and faster infrastructure investments. G20 institutions, particularly development finance institutions, should undertake enhanced local co-operation with African governments to create more productive infrastructure investment, thereby leading to improvements in connectivity and quality of life for communities across Africa.

Further analysis shows that compared to the rest of the continent, CwA countries have enacted more reforms to create a more liberal and improved environment for FDI.

The World Bank’s DB data suggest that CwA countries—with support from the G20— had better average distance-to-frontier (DTF) scores, and also to a continued increase in financing from Arab countries, India, and other non-traditional donors/investors. While the increased financing is welcomed, the ICA estimates for Africa’s financing gap over the next five years. The energy sector remains a key investment target; construction and manufacturing were also top priorities of the G20—have been strongly resilient in attracting investments. For example, FDI volumes to Compact countries have increased by 46% compared to the rest of the continent.

Ongoing global efforts

While Africa faces a huge infrastructure gap, there are measures that Group of 20 (G20) countries and its institutions can take to ensure greater and faster infrastructure investments. G20 institutions, particularly development finance institutions, should undertake enhanced local co-operation with African governments to create a more liberal and improved environment for FDI.

Further analysis shows that compared to the rest of the continent, CwA countries have enacted more reforms to create a more liberal and improved environment for FDI.

The World Bank’s DB data suggest that CwA countries—with support from the G20— had better average distance-to-frontier (DTF) scores, and also to a continued increase in financing from Arab countries, India, and other non-traditional donors/investors. While the increased financing is welcomed, the ICA estimates for Africa’s financing gap over the next five years. The energy sector remains a key investment target; construction and manufacturing were also top priorities of the G20—have been strongly resilient in attracting investments. For example, FDI volumes to Compact countries have increased by 46% compared to the rest of the continent.

Ongoing global efforts

While Africa faces a huge infrastructure gap, there are measures that Group of 20 (G20) countries and its institutions can take to ensure greater and faster infrastructure investments. G20 institutions, particularly development finance institutions, should undertake enhanced local co-operation with African governments to create a more liberal and improved environment for FDI.

Further analysis shows that compared to the rest of the continent, CwA countries have enacted more reforms to create a more liberal and improved environment for FDI.

The World Bank’s DB data suggest that CwA countries—with support from the G20— had better average distance-to-frontier (DTF) scores, and also to a continued increase in financing from Arab countries, India, and other non-traditional donors/investors. While the increased financing is welcomed, the ICA estimates for Africa’s financing gap over the next five years. The energy sector remains a key investment target; construction and manufacturing were also top priorities of the G20—have been strongly resilient in attracting investments. For example, FDI volumes to Compact countries have increased by 46% compared to the rest of the continent.

Ongoing global efforts

While Africa faces a huge infrastructure gap, there are measures that Group of 20 (G20) countries and its institutions can take to ensure greater and faster infrastructure investments. G20 institutions, particularly development finance institutions, should undertake enhanced local co-operation with African governments to create a more liberal and improved environment for FDI.

Further analysis shows that compared to the rest of the continent, CwA countries have enacted more reforms to create a more liberal and improved environment for FDI.
sectors in announced investments, illustrating a structural shift in many CwA countries. In addition, chemicals and hotels/tourism attracted a significant share of investments, reflecting strong long-term commitments and a focus on infrasructure region. G20 countries continue to dominate as the main source of FDI to CwA countries. They have accounted for an average annual inflow of $21.3 billion or around 63% of the region's total FDI over the past five years.

The importance of multi-country regional infrastructure projects to buttress integration

As Africa slowly progresses toward an economic union, it will be increasingly important to ensure that infrastructure needs are assessed from the continental and multi-country perspectives. To date, the majority of projects are country-specific markets or pooled resources. Some examples are: (i) The 14 megawatt (MW) run-of-the-river hydro electricity generating station at Kibi in the Upper East Region of Ghana. It is the first of its kind in sub-Saharan Africa and is expected to provide clean and reliable power to the surrounding communities. (ii) The Tanzania pipeline project, a joint venture between the governments of Tanzania and South Africa, is expected to increase the region's energy security and boost economic growth. (iii) The Mozambican gas pipeline project is expected to provide an additional 5.7 billion cubic meters of gas per year to South Africa, contributing to its energy security and economy.

Adaptations for private sector-led infrastructure development in Africa

This brief argues that more needs to be done—particularly by G20 countries—to spur private sector-led infrastructure in Africa. Interventions such as those above are positively impacting the overall investment on the continent. However, for adequate norms and approaches.

The time is right for innovations and adaptations that have been informed by recent analytical work and private sector consultations. This brief outlines three policy actions whereby G20 countries as well as African governments and other stakeholders can contribute to accelerating project cycles while ensuring quality infrastructure.

At the 18th OECD International Economic Forum on Africa, President Akufo-Addo of Ghana challenged OECD nations to focus on Africa particularly infrastructure. He noted the large infrastructure financing gap and indicated that OECD country processes for infrastructure projects have become ever more cumbersome. These have forced rapidly transforming African countries to look elsewhere for financing. In response, the OECD Development Center and the African Center for Economic Transformation are working with other international and regional development organizations, DFIs, and the private sector. It has a formalized governance structure (G20 Africa Advisory Group) and a network of support.

In 2019, the African Center for Economic Transformation (ACET), the OECD, Indiana University, and the European Center for Policy and Management (IECUP) analyzed how development finance organizations adapt to local country conditions. Many blended finance projects have strong local ownership, repurpose consultations, and entail explicit positive local spill-overs. However, the analysis also shows that investment decisions may at times derive from the priorities of external institutions or follow a standardized approach, without sufficient context and may be driven by local stakeholders. The analysis included assessments of the Agence Française de Développement (AFD) and its subsidiary dedicated to private sector Promparco; IFW Development Bank (IFB); European Bank for Reconstruction and Development (EBRD); European Investment Bank (EIB); Islamic Corporation for the Development of the Private Sector (ICD); International Finance Corporation (IFC); CDIC Gn (OPIC); European Union (EU); and the External Investment Plan (EIP).

The research produced a series of recommendations that were validated at a peer-to-peer learning event in September 2019 in Abidjan, Côte d'Ivoire. Ten African countries (all members of the CwA), DFIs, G20 representatives, and international development finance institutions (DFIs) were represented. The findings do not apply uniformly to all DFIs or all country conditions, but are transaction-specific in ensuring that blended finance is adequately accounting for the local context. These include, for example:

Organizational insights

1. DFIs should ensure their investment policies explicitly consider the local context, following good global practice.
2. If not already the norm, DFIs should develop country or sub-regional strategies that are aligned with national development strategies and avoid ad-hoc investment choices.
3. DFIs should ensure systematic consultations with local actors such as civil society, beneficiaries, local commercial investors, and the domestic private sector. This follows for both sovereign and private clients.

Partnering with local actors

1. DFIs should strengthen partnering arrangements with local DFIs, national development banks, Sovereign Investment Funds (SIFs), and local pension funds to better scale-up activities and tailor them to the local context. Additional credit lines, institutional investors, and financial institutions are attracted to blended finance operations.
2. Local DFIs or development banks do not exist, DFIs should explore options for providing technical know-how and financial support to create new local institutions.
3. Where appropriate, DFIs should provide support to and work with sub-sovereign entities such as local DFIs. They are under-resourced and, in many cases, have the potential to provide a more robust local solution to development challenges.

Local currency and local finance

1. There is a clear need to increase the gross and proportional amount of finance in local currency. Efforts to increase the capacity of issuing local currency securities have shown results, yet the demand for cost-effective foreign exchange international investors far exceeds the supply. More research is needed on the instruments best suited to local approaches or instruments that are most effective at attracting capital in local currency. This includes research on the role of managing financial tools/instruments for specific projects.
2. More needs to be done to increase the proportion of local finance in blended finance. There is engagement with local investors such as banks, investment funds, pension funds, and individual investors, but there is very limited crowding-in (LCs).
3. DFIs must do more to extend greater blended finance to LCs. They may be required to accept more risk and align with development priorities in the poorest countries and in fragile states.

Proposal 2: Improving infrastructure investment project cycles

Africa needs faster progress in implementing infrastructure development. The United Nations (UN) projects the continent’s population to double from 2.2 billion in 2020 to 4.5 billion in 2050. This will significantly stress the existing infrastructure. The African Continental Free Trade Area (AfCFTA) has now been ratified and provides increased opportunities for scaling up the provision of quality infrastructure, both sub-regionally and across the continent. Africa has the potential to be a leading player in the world of regional economic development. To do so, it must rapidly accelerate infrastructure investment. This requires significantly shorter project cycles, particularly for projects sponsored or financed by OECD counties or development agencies.

At the 28th OECD International Economic Forum on Africa, President Aliibu-Abi of Ghana challenged OECD nations to focus their support on growth-enhancing interventions, particularly infrastructure. He noted the large infrastructure investment in Africa has been more evident and ambitious. These have forced rapidly transforming African countries to resort to less traditional sources of investment. In response, the OECD Development Center and the African Center for Economic Transformation are working with other stakeholders. They have identified ways to speed up project cycles while ensuring quality infrastructure.

The research produced a series of recommendations that were validated at a peer-to-peer learning event in September 2019 in Abidjan, Côte d’Ivoire. Ten African countries (all members of the CwA), DFIs, G20 representatives, and international development finance institutions (DFIs) were represented. The findings do not apply uniformly to all DFIs or all country conditions, but are transaction-specific in ensuring that blended finance is adequately accounting for the local context. These include, for example:

1. Better planning and coordination among all stakeholders, particularly between Ministries, between municipal and federal governments, and between the private sector and other financiers and guarantors, such as multilateral organizational
If these proposals are effectively implemented, accepting PPP fiscal risks would be consistent with good risk allocation ... and contingent liabilities, which are widely used to shield the private sector from risk and are a common feature of PPPs.

For example, in many countries, investment projects have been procured as PPPs via special purpose vehicles (SPVs) to circumvent budget constraints and postpone recording the fiscal costs of providing infrastructure services (IMF 2006). The debt off the government balance sheet, but may still result in contingent liabilities for the government. Naturally, contingent liabilities require expenditure only if an unlikely future event occurs, such as a default. Furthermore, PPPs create co-finance for Ministries of Finance when balance sheets are hidden or not properly captured. As contingent liabilities often materialize in times of economic distress, they may exacerbate or even trigger fiscal crises. These crises have been shown to affect economically vulnerable countries significantly. Alternatively, PPPs sometimes require governments to assume contingent liabilities related to, for example, early contract termination or revenue guarantees. These guarantees and contingent liabilities, which are widely used to shield the private sector from risk, have severe implications for government budgets and may result in underestimation of fiscal risks and contingent liabilities.

The G20 has an important role to play in helping African countries to mitigate fiscal risks in PPPs. For example, G20 countries and associated institutions can support African governments and other stakeholders (Irwin and Mokdad 2010) to:

1. Improve the cost-benefit analyses used to select projects and improve value-for-money analyses to choose between PPPs and public finance.
2. Require, whenever appropriate, that PPPs be approved by the Cabinet as they have implications for sectoral Ministries, the Ministry of Finance, and often Ministries of other sectors, such as trade or tourism. Such approvals will also help ensure transparency in the costs and risks of the financial obligations they impose on the government.
3. Support, where appropriate, modern accrual-accounting standards for financial reporting to avoid using PPPs to disguise fiscal obligations.
4. Support managing and controlling liabilities in all phases of PPP project development processes by embedding appropriate control processes within National PPP policies and PPP Guidelines.

If these proposals are effectively implemented, accepting PPP fiscal risks would be consistent with good risk allocation (IMF Knowledge Lab 2020b). These proposals will nevertheless create contingent liabilities for governments, the cost of which can be harder to assess than the direct liabilities and initial costs of providing infrastructure services (IMF 2006). The risk to governments is that the SPV will be used to shield a budget deficit or the government will have to provide currency convertibility/hard currency support. Concessional stabilization provisions that shield the PPP from changes in regulatory frameworks or tax rates. The largest impact of PPPs on the government balance sheet comes from these support mechanisms and government guarantees of government Economic Transformation and the United Nations Economic Commission for Africa (UNECA) are undertaking a research project (UNECA 2020 forthcoming) to further inform good practices to avoid PPP fiscal risks. This work will serve as input for future discussions involving participating countries and other stakeholders.

The multiple sources of fiscal risk include but are not restricted to the following:

1. Risks that are the government’s direct responsibility, such as policy instability, changes in relevant laws and regulations, future spending commitments, and financing risks.
2. Project risks allocated to the government, such as government intervention and default, extended government approval, project bidding, feasibility demonstration, residual asset value, renegotiation, and force majeure.
3. Government guarantee risks, including credit guarantees, material supply and price guarantees, minimum income guarantees, and exchange rate, interest rate, and inflation guarantees.
4. Contingent liabilities risk, such as environmental or private sector bankruptcy risks.

Disclaimer
This policy brief was developed and written by the authors and has undergone a peer review process. The views and opinions expressed in this policy brief are those of the authors and do not necessarily reflect the official policy or position of the authors’ organizations or the T20 Secretariat.

References


---

Existing Initiatives & Analysis

---