THIS IS Africa
A GLOBAL PERSPECTIVE

http://www.thisisafricaonline.com/Business/A-role-for-PPPs-in-African-infrastructure

From **BUSINESS** 11 March 2013

A role for PPPs in African infrastructure

By **RYAN KETCHUM**

Scaling up financing from the traditional sources of taxes, government borrowing, and aid will not be adequate to successfully address Africa's infrastructure gap.

Across Africa, investments in infrastructure have failed to keep pace with growth and demand, creating a tremendous infrastructure deficit. Less than 40 percent of the population across the continent, and only 26 percent of the population of Sub-Saharan Africa, has access to electricity. Approximately 34 percent of the population has access to improved sanitation facilities, and 35 percent lack access to clean drinking water. The infrastructure deficit in Africa is remarkable even when it is compared to the infrastructure of other low income and developing regions.

It has been clear for some time that scaling up financing from the traditional sources of taxes, government borrowing, and aid will not be adequate to successfully address the infrastructure gap. Public-private partnerships (PPPs), which use private expertise and funding to construct, operate, and maintain infrastructure and deliver public services, are one of the solutions African governments are turning towards to solve this deficit. Yet, such projects need to overcome a range of challenges to ensure that they are well structured, deliver value for money, and transfer operational risk to the private sector. In the least developed countries, three of the most significant of these challenges are: (i) political instability, (ii) balancing the interests of investors and consumers (and keeping them balanced), and (iii) a shortage capacity in the public sector.

Political Instability

Many of the least developed countries have suffered political instability and conflict at both the national and the regional levels. It is difficult to attract investors and debt financing for projects that are located in such regions, but it is not impossible – there are tools to address these issues.

Take, for example, the Ruzizi III Regional Hydroelectric Project currently being promoted by Energies des Grand Lacs (EGL), a regional organisation that operates under the auspices of the Economic Community of the Great Lakes Countries with a mission to foster regional cooperation in energy projects. The site of the project is on the border between the Democratic Republic of Congo (DRC) and Rwanda. The offtakers include the parastatal utilities of Burundi, the DRC, and Rwanda – three nations with a long history of conflict. Many projects would simply get derailed in such an environment, but Ruzizi III has benefited tremendously from EGL's cross-border facilitation of the project. The key has been transparency, consultation, and an unwavering focus on the technical, legal, and economic problems that must be overcome.

The project has also benefited tremendously from the support of a broad range of bilateral and multilateral development finance institutions, which financed the initial steps in the project's development, have signaled interest in lending to the project company, and are likely to offer political risk insurance and guarantees that cover the risk of sovereign defaults under the project agreements.

Balancing the Interests of Investors and Consumers

One of the most widespread causes of poor infrastructure is the lack of cost-reflective tariffs. The tariffs paid by consumers for basic services in most African countries are not sufficient to enable the utility or service providers to recover the costs it incurs to provide the service. Across Africa, it is politically difficult for governments to increase tariffs to cost-reflective rates. As a result, many governments have established independent regulatory authorities to de-politicize tariffs. But taking these steps introduces a new problem–the newly established independent regulator has no demonstrated track record of successfully balancing the interests of investors and consumers. This is particularly difficult to achieve with large, complex projects because it may not be feasible for investors to bid a fixed price.

In late 2012, the $900 million, 250 MW Bujagali Hydroelectric Dam – the largest private sector investment ever undertaken in East Africa – achieved commercial operations, signifying a monumental change for Uganda's electricity sector. This large and complex project was possible due to an innovative tariff structure that enabled the project's sponsors to bid a rate of return on their equity investment, then undertake a competitive bid to procure an EPC contract after the Power Purchase Agreement had been executed. This structure enabled geotechnical risks to be allocated primarily to rate-payers, which avoided a risk premium being priced into the EPC contract, and it enabled the sponsors to arrange the financing after the Power Purchase Agreement had been executed. Collectively, these advantages increased private sector interest in undertaking the project. This so-called "regulation by contract" model can be used elsewhere to conquer this challenge.

Public Sector Capacity

Launching a successful

transparently. This challenge is often compounded by a lack of experience and gaps in understanding at the level of the civil servants who are responsible for advising political decision-makers. These problems can be overcome by quality advisors, but the expense of quality advisors is itself a challenge to many governments. Fortunately, bilateral and multilateral development finance institutions, and experienced investors alike understand this problem and often step in to fill the gap.

Ryan Ketchum is a Partner in the Energy and Infrastructure team in the London office of Hunton & Williams

More stories

African businesses should lobby for openness Comment on this article

PPP addresses financing gaps Comment on this article

Africa's infrastructure boom: Will this time be different? Comment on this article

AfDB floats new private sector strategy Comment on this article

Africa's Green Energy Revolution Comment on this article

Mobilising energy access Comment on this article