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The Pan-African Infrastructure Development Fund (PAIDF): towards an African agenda

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The purpose of this brief is to assess the viability or otherwise of the Pan-African Infrastructure Development Fund (PAIDF). In doing so, a few definitions and distinctions might be useful. Infrastructure has been defined as 'the structural elements of an economy that facilitate the flow of goods and services between buyers and sellers.'[1] The broader definition includes 'the basic services or social capital of a country, or part of it, which make economic and social activities possible by providing transportation [and other facilities] … in which community activities can take place.'[2] The definitions are alike in identifying infrastructure assets as roads, railways, airports, ports, power systems, telephones, water, and sewerage systems.[3] The broader social-capital definitions also take into account housing, health, and education services, as well as some other social institutions that facilitate economic and social interaction.

Alternatively, distinctions can be drawn among economic infrastructure (the physical assets that provide services used in production and final consumption), social infrastructure (assets that support a healthy workforce with adequate skills), and institutional infrastructure (such as the legal system, culture, and capital markets). Based on these distinctions, this paper will focus primarily on economic infrastructure and certain aspects of institutional infrastructure that are crucial to the operation of infrastructure development, as a platform for economic growth in Africa.

Introduction

Economic development depends in part on the levels of efficient infrastructure services. Infrastructure plays a central role in development, and is viewed as a major contributor to growth, poverty reduction, and, in the African context, the achievement of the Millennium Development Goals (MDGs). In this regard, annexure A illustrates the disparities in expenditure on development of new infrastructure and maintenance as a reflection of the development patterns in various regions of the world. What is noteworthy is the low level of investment in infrastructure in sub-Saharan Africa, North Africa, and the Middle East. This is of particular concern since infrastructure development forms the crucial backbone in maintaining and enhancing regional economic growth, productivity, and quality of life. It must therefore be emphasised that infrastructure development not only focuses on better infrastructure facilities and services, but also on infrastructure that is environmentally sound, socially accepted, and financially sustainable in the long term.[4] In this light, investment in infrastructure should

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be viewed as investment in change towards improving the human condition.[5] In the context of a rapidly globalising world, the requirement to make infrastructure investment and development a priority has become more important in the formulation of developmental policies.

Global trends illustrate the significance of infrastructure development and its benefits for economic development. For example, in countries such as China and India, infrastructure investment and development are a national priority, and serve as a mechanism that fosters growth potential in their burgeoning economies. However, infrastructure investment alone cannot spur economic growth and social development, but can contribute to them where appropriate conditions exist.[6] Therefore, infrastructure development should be regarded as a form of 'complementary capital' that requires the existence of available productive capacity (whether physical or human) for investment and innovation, in order to realise economic growth potential.[7]

In understanding the link between infrastructure and economic growth the following factors should be taken into consideration: the nature and type of infrastructure, the financial partnerships for the investment, and the organisational and institutional arrangements that promote investment initiatives. Existing literature on infrastructure investment and its potential for development and growth asserts that where the macroeconomic policy climate is conducive, growth from infrastructure investment will be stimulated.[8] The requirements include efficient resource allocation by virtue of policies that: provide price stability and inflation control, a favourably structured tax system, and pro-competitive regulations; facilitate international trade and growth, market entry for innovative firms, and skills development and education for the existing and potential workforce; encourage investment in research and development; and remove barriers to network access.

Challenges to infrastructure development

Challenges to infrastructure development in Africa can partly be attributed to the lack of financial resources to fund projects in energy, communications, education, and health. Private investments in infrastructure projects in Africa remain minimal, compared to other developing countries in the world.[9] This is partly due to the failure to manage developmental budgets, which depend heavily on external funding, effectively. This situation is further exacerbated by instability on the continent, especially in strategic countries such as the Democratic Republic of Congo (DRC), which has vast resources, and energy capacity located on the Inga Dam. In addition, the lack of a coherent national policy framework for infrastructure development has also resulted in the financing of socially desirable but non-bankable projects. In this regard, the ability of developing countries to attract infrastructure investment has been hampered by the following challenges:

Political risk: Unforeseen social and political events may change a project's prospects for profitability. This can be attributed to the changing of laws and the introduction of legislation that can adversely affect project economies. This risk is largely under the influence and control of governments. The determination of the credit-risk premium on infrastructure projects within a country's environment is an important matter for consideration.

Financial risk: Currency devaluation remains an obstacle in attracting long-term investment, although recently, local currency bonds and liquidity facilities offer some relief.

Commercial risk: This comprises risks that may affect the industrial operation of the infrastructure project, such as construction delays and cost overruns, operational and maintenance expenses, changes in input and output prices, contractor insolvency, and the availability and quality of supplies.[10]

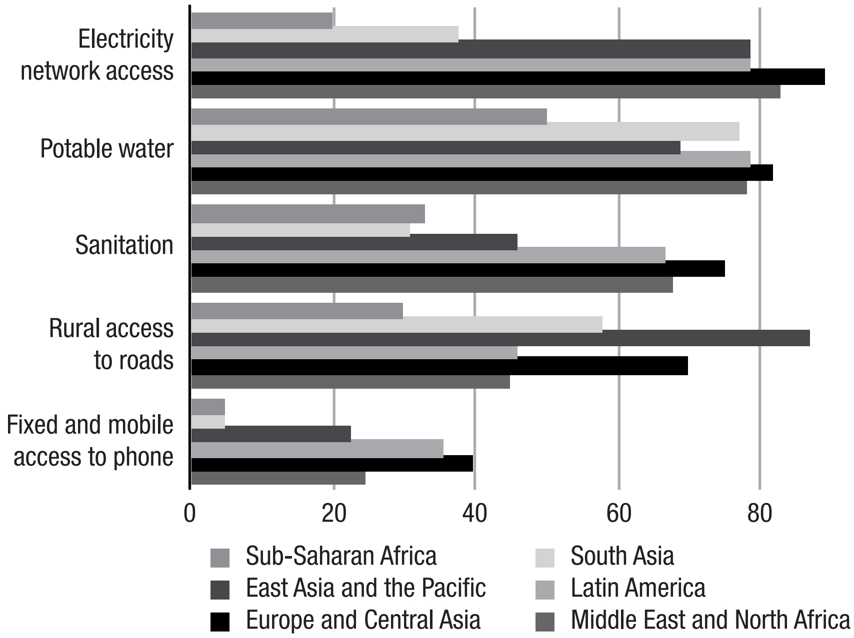
In addition to these challenges, several financial-market imperfections remain stumbling blocks to delivering essential finance for development. These include:

Information asymmetries: In most developing countries, private lenders often experience a shortage of information on monitoring, while borrowers are short on collateral. This may lead to undersupply of capital loans as well as credit rationing.

Externalities: This market imperfection occurs when there is a divergence between individual cost and social gain, resulting in externalities that are not reflected in the profit of the investor. The consequence of this may be a lack of investment in infrastructure projects that are beneficial to society, which are regarded as not profitable in yielding capital returns.

Market failures specifically linked to infrastructure: The length of time it takes for infrastructure projects to generate revenues and profits becomes a factor in increasing risk over time. This is reflected as a disincentive for investment in some infrastructure projects.

Figure 1: Access to infrastructure services



Source: World Bank, Regional comparisons – percentage population with access, Washington DC, 2006.

Africa's infrastructure needs and priorities

Africa's unmet infrastructure needs are estimated at US$22 billion a year, in addition to US$17 billion for operations and maintenance, according to the World Bank's *Africa Development Indicators 2007* report (see also annexure B). Access to infrastructure is viewed as a major bottleneck in Africa's growth. In addition, Africa faces a substantial shortfall in the financing and maintenance of infrastructure projects. Data on access to infrastructure development services demonstrates the extent to which Africa lags behind all other regions globally, as is evident in figure 1 (above). In addition to access, infrastructure maintenance services remain a priority on the continent, as the existence of adequate and efficient infrastructure has a systemic influence on the economy. Sectors to be regarded as Africa's infrastructure priorities are water and sanitation, energy, transport, telecommunications (connectivity), and urban infrastructure.

A continental response

The ability to finance, develop, and maintain infrastructure has historically been a major challenge to African developmental initiatives. With a decline in public funding for infrastructure development, the private sector has emerged as the primary agent as the source of investment capital. The World Bank study on infrastructure investment has concluded that developing countries today spend an average of 3–4 per cent of GDP on infrastructure annually, whereas they should spend an estimated 7 per cent of GDP for new investments, operations, and maintenance of existing infrastructure to meet the access challenges.[11] Against this background, the PAIDF was officially launched in July 2007 at the AU Heads of States Summit, convened in Ghana. The establishment of the PAIDF (otherwise known as 'the Fund') was partly informed by the recognition that mobilising private capital and creating public–private partnerships (PPPs) is crucial and complementary in responding to Africa's infrastructure development backlog.

Operational mandate and financial partners

The operational mandate of the PAIDF primarily focuses on regional funding of infrastructure on the continent, the vision being to create a sustainable infrastructure platform. The operational mandate illustrates investment opportunities as indicated below:

- a range of investment instruments to help diversify African pension fund portfolios;
- competitive instruments based on public–private infrastructure investments to increase total portfolio risk-adjusted returns;
- the mitigation of risk at key levels;

- a long-term investment horizon with the flexibility to match pension fund abilities; and
- an opportunity to participate in an initiative for Africa's reconstruction that supports its growth.[12]

The Fund seeks to enhance economic growth on the continent, as well as the continent's ability to respond to its own infrastructure requirements. This can be facilitated by the promotion of socio-economic development in African countries, thus boosting the continent's ability to be competitive in the global environment. In this regard, boosting intra-African trade is an imperative that can best be attained by the implementation of an infrastructure investment and development model, which supports economic growth and competitiveness by achieving economies of scale and reducing costs in trade. Within the spectrum of infrastructure development, the Fund's sector targets include: energy and power, telecommunications, transport, and water and sanitation. Moreover, the Fund has been structured to provide long-term equity financing over 15 years for commercially viable regional infrastructure.

The Fund aims to take responsibility in driving continental developmental trajectories by developing partnerships with the private sector and other key African developmental institutions. These partners include: the Development Bank of Southern Africa (DBSA), the African Development Bank (ADB), African Pension Funds (APF), the commercial bank ABSA, the Public Investment Company (PIC), and other South African banks and institutional investors. In the next 12 months, the PAIDF seeks to expand its investor list to include international investors in the United States, Europe, and the Far East. So far, the PAIDF has mobilised close to US$625 million which will be used to finance continental projects under the AU development flagship programme, the New Partnership for Africa's Development (NEPAD). Further efforts by South Africa and Ghana, on behalf of Africa, to mobilise financial support for the Fund are ongoing. This is largely because the success of the Fund will be determined by African commitment and the continent's ability to mobilise resources for the Fund.

Linkages with existing initiatives

The Fund is also faced with a number of challenges, especially regarding existing infrastructure development initiatives, and whether linkages with these existing initiatives can enhance its presence and impact on the continent. Infrastructure development initiatives in progress on the continent include: the Economic Commission for Africa Infrastructure Development Activities (ECAIDA); the Sub-Saharan African Transport Policy Programme (SSATP); the Infrastructure Consortium for Africa (ICA);[13] the NEPAD Infrastructure Programme (NIP); and the EU–Africa Infrastructure Partnership, and trust fund and steering committee, to support the AU/NEPAD Infrastructure Short-term Action Plan (i-STAP) and the Medium- to Long-term Strategic Framework (MLTSF) programmes in the sectors of transport, energy, water and sanitation, and Information and Communication Technologies (ICTs).

Challenges encountered in strengthening and harmonising African infrastructure development initiatives include the absence of a continental body that progressively monitors infrastructure projects on a country-to-country basis, which means that some projects could be replicated. Infrastructure development initiatives on the continent have similar but competing priorities, considering various stategic sectors where development gaps have to be met. The lack of synergies among the various initiatives has created the tendency to concentrate capital in specific sectors, such as economic-infrastructure investment and financial-market development, seemingly undermining the developmental imperatives of equally important sectors, such as social-development infrastructure.

It must be taken into consideration that in order to create sustainable infrastructure platforms on the continent, infrastructure investment and development mechanisms should be 'people centred', and should include human-development initiatives. In this context, the PAIDF aims to facilitate synergies and interconnectivities among existing infrastructure investment and development initiatives, in order to strengthen trade and integration at continental, regional, and national levels. It is important that synergies among the PAIDF, regional economic communities (RECs), and developmental financial institutions (DFIs) be harmonised to avoid and reduce duplication of projects, as well as transaction costs. To this end, NEPAD's Spatial Development Programme (SDP) is an important platform for the Fund in configuring, prioritising, and promoting interrelated infrastructure development and large-scale economic sectoral investment in defined geographic areas along transport corridors. This SDP strategy seeks to: promote private-sector participation in infrastructure development; promote trade- and investment-led economic growth; optimise the utilisation of infrastructure; encourage value-added processing; and enhance the competetiveness of African economies.[14]

The NEPAD SDP also provides the means to promote integrated economic development platforms based on promotion of key large-scale anchor investments and related upstream and downstream investments. Given NEPAD's continental legitimacy as the AU's economic programme, the SDP will provide the PAIDF with the much-needed continental buy-in, and also enhance its ability to raise funds and ensure infrastructure viability through sustainable revenue streams. Moreover, the SDP methodology is largely informed by the completion of existing infrastructure development corridors, such as the Maputo Development Corridor, which includes the Joburg–Maputo Highway; the Pande-Secunda gas line, coal-based power station, and Joburg–Maputo railway line upgrade; and the Zambezi Valley Development, which is in the process of implementation. This methodology has been applied in identifying other projects on the continent, based on the development-corridor model. As such, NEPAD has also identified a series of potential infrastructure development projects in the four geographical regions, namely: the Maghreb Coastal SDP; the Niger SDP and Gulf of Guinea Coastal SDP in West Africa; the Douala-N'djamena and Libreville-Lome SDP, and Bas Congo, Mombasa, and Central SDPs (Dar to Kisangani), all in East and Central Africa; and the Tazara and Madagascar SDPs in Southern Africa.[15] To avoid duplication and competition for infrastructure development funding, the PAIDF should seek to harmonise its agenda with the existing SDP projects, and to support other NEPAD and REC initiatives on infrastructure development.

Conclusion

The establishment of the PAIDF has demonstrated renewed commitment towards infrastructure development on the continent. Moreover, the political commitment expressed by African leaders at the launch of the Fund is an indication of their readiness to address challenges to infrastructure investment and development on the continent. However, given the vast number of infrastructure development initiatives on the continent, the Fund is faced with the difficult task of resources mobilisation, and identifying viable resource-investment projects without duplicating existing projects. Moreover, for PPPs to be effective in infrastructure development, there is a need to identify sectors in which the return of capital, whether public or private, is greatest from a perspective that emphasises long-term returns. This should be in terms of human welfare, productivity, and economic growth. Understanding the likely sectors that serve as drivers of economic growth, country by country, as well as prioritising them project by project, are necessary first steps in this regard. To this end, the Fund should consider harmonising its infrastructure projects with the existing NEPAD SDP, as well as supporting REC projects that fall within the scope of the broader continental economic and developmental agenda.

Policy considerations

The Fund must further stimulate private infrastructure investment by addressing the basic requirements for sustainable private-capital flows. It is recommended that the Fund take into consideration the following key prerequisites for attracting private financing: (i) efficient financial markets, which can provide funding at suitable terms and conditions; (ii) transparent and reliable investment and regulatory frameworks; and (iii) project revenues that are predictable and ensure a reasonable rate of return on equity.

The success of infrastructure investment projects will depend on the Fund's ability to secure political commitment. This will be crucial in ensuring rapid planning and delivery of infrastructure projects and programmes.

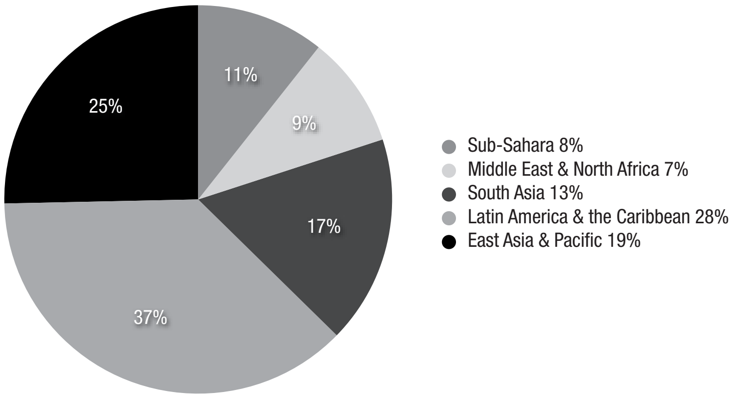
The Fund should put in place monitoring bodies that address obstacles regarding infrastructure investment. These include the lack of transparency and corporate governance in some African countries, as well as the legal, liquidity, and regulatory risks of financial markets. Technical strategic partners at national level could play a key role in the management and monitoring of private investment in infrastructure, as well as strengthen relationships between pan-African funds and private investors.

Challenges in harmonising the PAIDF initiatives with RECs should be addressed by initiating a programme of action that focuses on capacity-building of the REC secretariats. In this regard, synergies should be forged among the African Capacity-Building Foundation, the PAIDF, and respective RECs on the continent.

In order to reduce the growing need for new investments in infrastructure, the Fund should (in addition to stimulating investment) focus on optimising the capabilities of existing infrastructure.

Annexure A

Investment commitment to public–private infrastructure (PPI) projects in developing countries, by region – 2001–2006



Source: World Bank and Public–Private Infrastructure Advisory Facility (PPIAF) PPI project database.

Annexure B

Expected annual infrastructure investment needs (2005–2010)

	New		Maintenance		Total	
	US$m	**%GDP**	**US$m**	**%GDP**	**US$m**	**%GDP**
Developing countries by region						
East Asia & Pacific	99 906	3,67%	78 986	2,90%	178 892	6,57%
South Asia	28 069	3,06%	35 033	3,82%	63 101	6,37%
Europe & Central Asia	39 069	2,76%	58 849	4,16%	97 918	6,92%
Middle East & North Africa	14 884	2,37%	13 264	2,11%	28 148	4,48%
Sub-Saharan Africa	13 268	2,84%	12 644	2,71%	25 912	5,55%
Latin America & Caribbean	37 944	1,62%	32 878	1,40%	70 822	3,02%
All developing countries	**233 139**	**2,74%**	**231 654**	**2,73%**	**464 793**	**5,47%**

GDP deflator used is an average of 2005–2010 projections
Source: Mariann Fay and Tito Yepes, Investing in Infrastructure: what is needed from 2000 to 2010?, World Bank policy research working paper 3102, 2003.

Endnotes

1 New Zealand Ministry of Economic Development, Linkages between infrastructure and economic growth, December 2003, Executive summary. At http://www.med.govt.nz/templates/MultipageDocumentPage9188.aspx.

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5 Trevor A Manuel, Ministerial roundtable discussions on infrastructure development and regional integration: issues, opportunities and challenges, Republic of South Africa National Treasury, 16 May 2006. At http://www.treasury.gov.za/comm_media/speeches/2006/2006051601.pdf.

6 In this case, especially important are macroeconomic policies that ensure efficient resource allocation, and allow the competent use of capital to improve existing infrastructure and develop new projects.

7 New Zealand Ministry of Economic Development, Linkages, Executive summary.

8 New Zealand Ministry of Economic Development, Linkages. At http://www.med.govt.nz/templates/MultipageDocumentPage9189.aspx#P69_24141.

9 See annexure A.

10 Stephany Griffith- Jones and Teresa Fuzzo de Lima, Alternative loan guarantee mechanisms and project finance for infrastructure in developing countries, Institute for Development Studies, University of Sussex, February 2004.

11 See annexure B.

12 Aziz Pahad, NEPAD and African business opportunities – what are the challenges, Ministerial address to the Association of SADC Chambers of Commerce and Industry. At http://www.dfa.gov.za/docs/speeches/2007/paha0826.htm.

13 The ICA secretariat is located in the ADB, and collaborates closely with the AU, NEPAD and the RECs.

14 See Africa Resource-Based Sustainable Development: the NEPAD Spatial Development Programme (SDP), Sector stakeholder workshops of the NEPAD MLTSF infrastructure study, Addis Ababa, July 2007.

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