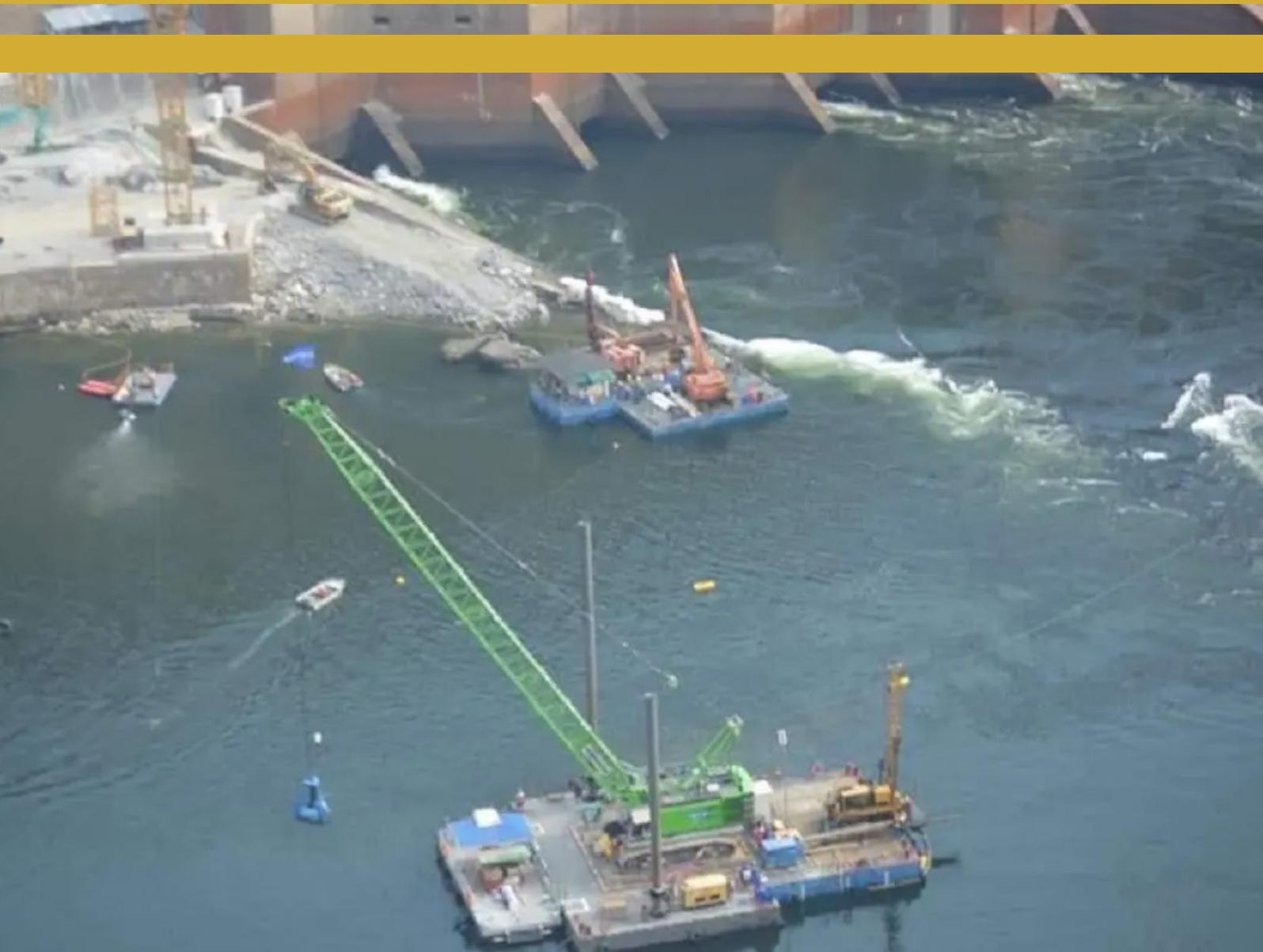


Opportunities for blending Public and Private Sector Resources Towards Infrastructure Funding in Zimbabwe: Policy Option

MAY 2019



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Opportunities for Blending Public and Private Sector Resources towards Infrastructure Funding in Zimbabwe: Policy Options.

Preface

This is a thought-provoking study that was commissioned in July 2018 as part of the Bank's contribution to knowledge generation and sharing.

It followed the realization that Infrastructure funding will benefit from both the public sector, the private sector, donors and philanthropist working together to address the huge infrastructure funding gap estimated at US\$ 27.3 billion. The need to broaden the scope of infrastructure funding to include blended finance beyond PPPs, sets the context for this study.

The overall objective of the study is to contribute towards improving the body of knowledge and provide input into formulation of strategies towards the mobilization of both public and private resources to finance infrastructure development in Zimbabwe.

Successful infrastructure financing, can be enhanced through mobilizing additional funding from institutional investors (pension funds, insurance companies, sovereign wealth funds, etc.). However, as observed by Thorne (2011) there is need for policy makers to put in place comprehensive and effective legal systems; adequate protection of property and creditor rights and a reliable, efficient and independent justice system for effective participation of the private sector in infrastructure development. Public procurement systems should be more effective in facilitating infrastructure development.

Readers of this report will find the recommendations in this report very beneficial towards scaling up infrastructure resource mobilization. The Bank will continue to explore more solutions to the country's developmental challenges especially in the infrastructure sector space. This report is one of the many ways the Bank is trying to cultivate interest in innovative infrastructure financing.



Thomas Zondo Sakala

Chief Executive Officer
Infrastructure Development Bank of Zimbabwe
12 September 2019

Foreword

Blended finance involves financing mechanisms that link a grant element, provided by Official Development Assistance (ODA), with loans from publicly owned institutions or commercial lenders (Romero, 2017). The OECD defines blended finance as the “strategic use of development finance for the mobilisation of additional finance towards sustainable development in developing countries” (Alex Money, 2018).

This study provides information on global and regional experiences in blended infrastructure financing; lessons learnt from past and current experiences in financing infrastructure in Zimbabwe; opportunities for blending public and private sector financing in infrastructure development and policy options for Zimbabwe. Africa Infrastructure Development Association (AfIDA, 2018) observed that there is a steady increase in the rate of blended finance deals in the periods 1980 through 2016.

In 2017, the DFIs financed projects worth more than US\$8.8 billion utilising blended concessional finance (US\$1.1 bn), Private sector finance mobilised for the projects to the tune of US\$3.3 billion and DFIs own account investments amounting to US\$3.9 billion. Generally, blended finance is considered as the second highest potential source of development finance after foreign direct investment (FDI) followed by tax collection, official development assistance (ODA), remittances, trade finance, South-South cooperation and philanthropic activities. It has been observed that blended finance has been successfully executed for projects that required public subsidy or enhancements to be viable.

Development Finance Institutions remain critical in the promotion of blended finance. Sectoral analysis shows that that energy, non-energy infrastructure and housing & real estate constitute 24%, 9% and 1% of the deals with an average deals size of US\$374 million, US\$215 million and US\$290 million, respectively. A breakdown of the energy sector reveals that renewable energy constituted a larger chunk at 62% compared to 16% for non-renewable, off-grid (17%) and other (13%).

The report notes that there is therefore a need to provide technical assistance and training to capacitate both the public and private sector to enhance smooth execution of blended finance. Creating a credible and viable infrastructure bond market is a critical success factor in mobilizing blended infrastructure finance. There is also need for adequate public/concessional funds to facilitate the development of a pipeline of bankable projects for consideration in mobilising blended finance for infrastructure development.

Lessons from Zimbabwe shows that the country has had successful experiences with blended finance which it should build on. Important lessons learnt include that, while ‘sweeteners’ are needed to attract the private sector, it is important to ensure that the tendering process is not defective. Blending for infrastructure financing should also target other local players, such as pension funds, who might be able to invest in long term projects.

This report presents an in-depth analysis of what needs to be done for the country to attract relevant investments through blended finance as well encouraging local players to participate in blended finance.



Phillip Chitsika

Acting Chief Economist

Infrastructure Development Bank of Zimbabwe

12 September 2019

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List of Acronyms

ABS	Asset Backed Security
AFD	French Development Agency
AfDB	African Development Bank
AMT	Alternative Minimum Tax
ANGOs	Australian-accredited NGO
ARA	American Recovery and Reinvestment Act
ARM	Asset and Resource Management Company
BABs	Build America Bonds
BBR	Beit-bridge Bulawayo Railway
BCC	Bulawayo City Council
BLT	Build Lease and Transfer
BMCE	Banque Marocaine du Commerce Extérieur
BOOT	Build Own Operate and Transfer
BORD	Banque Quest Africaine deDeveloppement
BOT	Build Operate and Transfer
BSAC	British South African Company
CAB	Central African Backbone
CAO	Contract Add and Operate
CCC	Chitungwiza City Council
CGF	Credit Guarantee Finance
CJIETCC	China Jiangsu International Economic Technical Cooperation Corporation
CLOs	Collateralised loan obligation
CWE	China Water & Electrical
DAC	Development Assistance Committee
DBM	Design, Build and Maintain
DBMO	Design, Build, Operate and Maintain
DDF	District Development Fund
DFI	Development finance institutions
DOR	Department of Roads
DOT	Develop Operate and Transfer
EIAF	Emerging Africa Infrastructure Fund
EIB	European Investment Bank
EPIRP	Emergency Power Infrastructure Rehabilitation Project
ESA	Southern and East African
ESSAy	Eastern Africa Submarine Cable System
ETFs	Exchange Traded Fund
EWSA	Energy, Water and Sanitation Authority
FDI	Foreign Direct Investment
FTLRP	Fast Track Land Reform Programme
GCR	Global Credit Rating Company
GEPP	Government Employees Pension Fund
GFC	Global Financial Crisis

GFC	Green Climate Fund
GoG	Government of Ghana
GoR	Government of Rwanda
GPs	General Partnerships
ICT	Information and Communications Technology
IDBZ	Infrastructure Development Bank of Zimbabwe
IFC	International Finance Corporation
IITs	Infrastructure investment trust,
IPHC	Insurance and Pension Housing Company
IPP	Independent Power Producers
JVA	Joint Ventures Act
LCC	Lekki Concession Company
MDBs	Multilateral Development Banks
MFIs	Multilateral Financial Institutions
MIGA	Multilateral Investment Guarantee Agency
MLP	Master Limited Partnership
MPNTI	Ministry of Post and New Information Technologies
MPTEN	Ministry of Post and Digital Economy
NBP	Newlands By-Pass
NEPAD-IPPF	New Partnership for Africa's Development-Infrastructure Project Preparation Facility
NGOs	Non-Governmental Organisations
NLB	New Limpopo Bridge
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
PABs	Private Activity Bonds
PDES	Economic and Social Development Plan
PIC	Public Investment Corporation
POTRAZ	Postal and Telecommunications Regulatory Authority of Zimbabwe
PPP	Public Private Partnership
RDC	Rural District Council
REITs	Real Estate Investment Trust
ROO	Rehabilitate Own and Operate
SAICC	South African Infrastructure Investment Company
SDGs	Sustainable Development Goals
SIGIEP	Integrated Management System for the Electronic Identification of People
TAF	Technical Assistance Facility
TIF	Tax Increment Financing
TIFIA	Transportation Infrastructure Finance and Innovation Act
TIGER	Transportation Investment Generating Economic Recovery
TSB	Trans-Sahara Optical Fibre Backbone
TSP	Transitional Stabilization Programme
UCs	Urban Councils
UETCL	Uganda Electricity Transmission Company Limited
UNCTAD	United Nations Conference on Trade and Development
USF	Universal Services Fund
UWSSRP	Urgent Water Supply and Sanitation Rehabilitation Project
WBHO	Wilson Bayly Holmes-Ovcon
WBPGP	World Bank Partial Guarantee Program
ZAPF	Zimbabwe Association of Pension Funds
ZEPARU	Zimbabwe Economic Policy Analysis and Research Unit
ZESA	Zimbabwe Electricity Supply Authority
ZETDC	Zimbabwe Electricity Transmission and Distribution Company
ZIDERA	Zimbabwe Democracy and Economic Recovery Act
ZIMASSET	Zimbabwe Agenda for Sustainable Socio-Economic Transformation
ZimFund	Zimbabwe Multi-Donor Trust Fund
ZIMRA	Zimbabwe Revenue Authority
ZIMREF	Zimbabwe Reconstruction Fund
ZINWA	Zimbabwe National Water Authority
ZPC	Zimbabwe Power Company

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The views expressed here do not in any way represent the views of the client organisation IDBZ and their principal, the Government of Zimbabwe, but those of the researchers. Although all care has been taken to produce an error-free report, the study team takes full responsibility for any inadvertent errors (factual or otherwise) or omissions that may still remain.

Executive Summary

This study was commissioned by Infrastructure Development Bank of Zimbabwe (IDBZ) to explore the opportunities for blending public and private sector resources towards infrastructure funding in Zimbabwe with a focus on the policy options. Blended finance came into mainstream after the Third International Conference on Financing for Development in July 2015 where blended finance and other innovative finance mechanisms were recognized as solutions for addressing the SDGs funding gap in developing countries. The overall objective of the study is to contribute towards improving the body of knowledge and provide input into formulation of strategies to mobilization of both public and private resources towards infrastructure development in Zimbabwe. This overall objective is underpinned by six specific objectives which are detailed in the report.

The research team adopted mixed methods approach that involved a quantitative and qualitative analysis to address the study objectives outlined above. Key methodological steps adopted included an inception meeting with the IDBZ officials, extensive desk review and analysis of literature on global and regional trends in blended financing of infrastructure projects; reviewing of key government policy documents; regulatory frameworks and consultancy reports/studies focusing on infrastructure development in Zimbabwe. The research team also developed research questionnaires that were used to collect primary data from key informants to complement and triangulate with secondary data analysis. The qualitative and quantitative analysis of the primary and secondary data collected including field observations were used as a basis to prepare this report.

A number of lessons drawn from the review of global and regional trends in blended infrastructure financing coupled with the findings from a review of Zimbabwe's experiences with blended finance and input from informant interviews informed the recommendations of this study. The motivation of this study is based on the understanding that inadequate infrastructure funding has resulted in widening infrastructure gap in the country and further jeopardized the functionality of existing infrastructure due to low maintenance budgets. Furthermore, the achievement of targets set out in the Transitional Stabilisation Programme (TSP) and Vision 2030 adopted by Government is premised on building resilient infrastructure, promotion of inclusive and sustainable industrialization and fostering innovation. In this regard IDBZ as a development Finance Institution (DFI) with a mandate to mobilise funding for infrastructure development has a keen interest in understanding the terrain of blended infrastructure finance as an alternative and innovative source of funding infrastructure development.

Thus, the study provides a synopsis of the global trends on the evolution of blending public and private sector resources and infrastructure investment funds/platforms. A common feature emerging from the literature on infrastructure investment funds/platforms is their ability to mobilise additional blending funds mainly from institutional investors (pension funds, insurance companies, sovereign wealth funds, etc.) and other interested investors. The key lesson emerging from this synopsis is that there is scope for IDBZ as an infrastructure investment platform to leverage public funds and its own funds to mobilize private funds from institutional investors. According to the Life Offices Association of Zimbabwe there is a good base of institutional investors in the country whose asset base is in excess of US\$2.7 billion which presents an opportunity for blending finance for infrastructure projects.

The study also reviewed the African experience in blending both public and private interest-bearing instruments to finance infrastructure. It emerged from this review that an increasing number of countries in Africa are exploring opportunities for blending public and private sector funding to address the infrastructure deficits on the continent. The experiences based on the reviewed case studies are varied and are shaped by the different country contexts. Africa Infrastructure Development Association (AfIDA, 2018) observed that there is a steady increase in the rate of blended finance deals in the periods 1980 through 2016.

The African Development Bank (AfDB 2018), also highlighted that one of the key factors retarding industrialization in Africa has been the insufficient stock of productive infrastructure in power, water, and transport services that would allow firms to thrive in industries with strong comparative advantages. Convergence (2018) identified Sub-Saharan Africa as the most popular target region, in terms of mobilization of blended finance, representing 42% of blended finance deals, though the average deal size of US\$125 million for Sub Saharan Africa (SSA) is small when compared to a global average deal of US\$699 million. It also emerged from the same report that middle income countries are most commonly the target recipient of blended finance deal flows, followed by low income countries. The DFI Working Group on Blended Concessional Finance (2018) also observed that concessional finance was generally used to de-risk pioneering projects in high risk countries and/or projects with new technologies or those addressing under-served segments in society.

Highlights emerging from the African experience include the issuance of infrastructure bonds by countries like Kenya, Cameroon, Chad, and South Africa. Creation of a credible and viable infrastructure bond market is a critical success factor in mobilizing blended infrastructure finance. It has also been observed from this review that potential infrastructure projects in Africa have remained on the drawing board for too long due to a variety of reasons including lack funds for the development phase, high risk perceptions, and lack of political support among other factors. In this regard, the need for adequate public/concessional funds to facilitate the development of a pipeline of bankable projects for consideration in mobilising blended finance for infrastructure development has been noted as a key success factor.

The study team also reviewed Zimbabwe's experience in financing infrastructure project with particular focus on identifying the modalities through which they were funded and managed. It was observed for example, that Kariba power station which is a major infrastructure project in the country was financed through external and domestic debt. External debt, which constituted about 59% of the total debt for the project, was in the form of Overseas Development Assistance (ODA) from International Bank for Reconstruction and Development (IBRD), Colonial Development Bank (CDC), and Common Wealth Development Finance Corporation (CDFC)

(International Bank for Reconstruction and Development, 1956). The model used in developing the Triangle Sugar Estate Project also presents some interesting learning points for IDBZ. While this may not be classified technically as a blended financing project, the investment of public funds in a failed private sector project and selling it when it was viable demonstrate the potential for blended financing in the development of irrigation projects in Zimbabwe.

Similar opportunities for developing thriving sugarcane plantations are available in Muzarabani and Mbire districts along the Zambezi valley that share the same low veld climatic conditions with Triangle. Other infrastructure projects reviewed are in the dam construction; transport, housing; information and communication technology sectors. While there were indications of willingness by institutional investors to participate in these projects, the most common financing mechanism which they are willing to consider are infrastructure bonds for projects that are assigned prescribed asset status. It was also observed that IDBZ's capacity to mobilise blended infrastructure funding can be enhanced through increasing the level of capitalisation. Increased capitalisation will increase IDBZ's capacity to effectively play a catalytic role in the provision of infrastructure. It was noted that the capacity of IDBZ to co-finance infrastructure projects through own capital contribution is a good de-risking mechanism as it increases infrastructure investors/financiers confidence in the IDBZ promoted projects.

Furthermore, it was observed that enabling regulatory, legal, institutional policy frameworks provide a favourable environment for the mobilization of blended finance infrastructure projects. Institutional capacities with regards to financial, skills and systems; adequacy of legislative and governance frameworks; capacities of infrastructure project promoters and the depth of financial institutions in terms of skills, diversity of financial products/instruments; stability and predictability of the overarching of the macroeconomic environment are all critical elements that create a conducive environment for the growth of a blended infrastructure finance market.

It was also established that although blending reduces risk and helps catalyse concessional funding, there is need for a predictable exchange rate regime. Furthermore, investors need to be assured that they can repatriate proceeds of their investments without cumbersome foreign exchange control regulations. Currency risk was noted as a key consideration in negotiation of blended financing contracts hence the need for improvement in management and predictability of currency regime in any country. Currency risk also occurs when there are unfavourable currency fluctuations for projects financed in foreign currency and returns earned in local currency.

Thorne (2011) observed that a comprehensive and effective legal system; adequate protection of property and creditor rights and a reliable, efficient and independent justice system are essential for the participation of the private sector and ODA in infrastructure development. The Zimbabwean Constitution has very specific provisions that are aimed at protecting economic rights, including property rights, which are fundamental in the attraction of both short term and long term investments. For example, section 71 of the Constitution alludes to the protection of property rights, Subsection (3) state that "subject to this section and to section 72, no person may compulsorily be deprived of their property except where the following conditions are satisfied.....". These notwithstanding, there are some flaws within subsidiary legislation that have been identified by stakeholders as needing reform. While the rules and regulations on public procurement attempt to plug loopholes for corrupt practices there seem to be no enabling legal framework to allow bidder's enforceable right to review when public entities breach the rules. Private investors are also worried about the delays caused by the public procurement processes given that in the private sector decision making is quicker due to limited bureaucratic red tape.

Similarly, strengthening institutional enablers will play a key role in the mobilisation of blended infrastructure finance. For example, creation and adequately capitalised dedicated financial institutions for infrastructure financing is a critical institutional enabler to facilitate blended infrastructure financing. In particular growth in asset base of institutional investors necessitates the channelling of investable funds to long term infrastructure projects. It was also observed that there is lack of confidence among the private sector, with regards to the capacity within government and government related institutions to manage the design and implementation of complex infrastructure projects. In particular institutional investors who are the main source of long-term funds expressed concern that they are not adequately consulted in the design of the instruments used to mobilise funds for infrastructure projects.

It was also observed that laws and regulations are only as good and effective to the extent to which they are reasonably applied. Stakeholders noted a number of flaws in the application of laws and regulation that need redress in order to create an enabling environment for the growth of blended infrastructure finance transactions. Areas of concern raised by stakeholders as impeding the mobilisation of concessional ODA funding include: delays by government to compensate farmers whose land and associated infrastructure was compulsorily acquired by the Government under the fast track land reform programme and violation of the terms of some of the BIPPAs. It also emerged that the limited number of projects with updated feasibility studies or pipeline of bankable projects is also due to lack of capacity among the project promoters/owners to develop the projects from project concept to a bankable project.

The study also observed that there are opportunities for possible collaborative relationships that can be forged between IDBZ and a diverse set of institutions in mobilising resources for blended infrastructure financing. Line Ministries and State Owned Enterprises with mandates to put up infrastructure be it in Energy; Power, ICT; Water etc.; Local Authorities; Universities all have infrastructure gaps and project ideas that have to be developed to bankability and packaged to solicit for funding from prospective financiers. Lack of properly packaged projects hinders the ability to get the concessional funding which can be used to reduce the gap between real and perceived risks, thus making it possible to crowd in commercial investors.

- The study makes a number of recommendations which focus on how to improve the fiscal and monetary policy environment to foster prudent macroeconomic policy management which will anchor: stability in the financial systems; stability and predictability in foreign exchange management and inflation. Building of international reserves; debt and arrears clearance; reducing current account and fiscal deficits were identified as critical pillars of the prudent macroeconomic management framework. This coupled with the strengthening of institutions responsible for Infrastructure development with the requisite

capacity to initiate infrastructure projects would leverage on to mobilize blended infrastructure finance. A number of areas that require institutional strengthening initiatives have been discussed including: diversification and deepening of the financial markets; strengthening the design; implementation and management of complex infrastructure projects within government; consolidation of Treasury Bills and Bonds into few larger bonds; revamping of credit worthiness, governance structures and management of State Enterprises with potential capacity to issue bonds; ring-fencing infrastructure project income streams and the necessary conditions for IDBZ to leverage on the opportunities for possible collaborative relationships among others are detailed in the report.

Chapter 1: Introduction and Contextual Framework

This study which was commissioned by the Infrastructure Development Bank of Zimbabwe (IDBZ) explores the opportunities for blending public and private sector resources towards infrastructure funding in Zimbabwe with a focus on the policy options. The OECD defines blended finance as the “strategic use of development finance for the mobilisation of additional finance towards sustainable development in developing countries” (Alex Money, 2018). This framing distinguishes finance by purpose rather than by source and highlights blending in terms of development and commercial finance rather than public and private. According to the World Water Council Report (2018), between 2000 and 2016, donor governments set up 167 dedicated facilities that pool public financing for blending and the number of new facilities grew every year.

The study also provides information on global and regional experiences in blended infrastructure financing; lessons learnt from past and current experiences in financing infrastructure in Zimbabwe; opportunities for blending public and private sector financing in infrastructure development and policy options for Zimbabwe. Adequate provision of infrastructural services is critical to unlocking the potential productive capacity of the private sector. Investment in development of new infrastructure and maintenance of existing infrastructure was adversely affected by the dwindling public resources allocated to infrastructure development projects particularly during the hyperinflationary period between 2000 and 2008. The level of capital expenditure as a percentage of GDP has remained below the international benchmark of 25% over the period 2009 to 2018.

Studies by World Bank (WB, 2012) and African Development Bank (AfDB, 2011) provide estimates of the infrastructure funding requirements for the country, and these are huge. The AfDB for instance estimated that the country required at least US\$14.2 billion at 2009 constant prices, including US\$4.6 billion of private investment, in upgrading existing infrastructure and new capacity for the period 2011-2020. The World Bank study estimated that Zimbabwe requires at least US\$ 33 billion in infrastructure investment over the next two decades, which translated then to investments of about US\$1.65 billion per year. According to the Transitional Stabilisation Programme (TSP) infrastructure funding requirement for Zimbabwe between the periods 2019 to 2020 is estimated to amount to USD26.97 billion and is disaggregated as summarised in Table 1.

Table 1: Infrastructure funding requirement: Transitional Stabilisation Programme (TSP) (2019-2020)

Sector	Estimated requirements (US\$ Million)
Energy	7,336.0
Transport	6,170.2
Water Sanitation and Hygiene (WASH)	4,239.9
Social Service	5,922.1
ICT	707.0
Institutional housing	1,704.8
Agriculture Infrastructure	816.4
Other Infrastructure	75.0
Total	<u>26,971.4</u>

Source: Ministry of Finance and Economic Development 2018

Inadequate infrastructure funding has not only resulted in widening infrastructure gap but also jeopardized the functionality of existing infrastructure due to low maintenance budgets. A number of infrastructure projects in the energy, housing, transport, water, information communication and technology sectors have stalled due to lack of funding. In this regard, the need for innovative financing arrangements in the country such as blended financing for infrastructure financing or even beyond cannot be overemphasized.

The limited fiscal capacity of the government to provide public funds or to mobilize development capital to finance infrastructure development has motivated Government to solicit for private sector funding of infrastructure under the Public and Private Sector Program (PPP) in line with global developments. In 2004, the Government of Zimbabwe produced the Public Private Partnership in Zimbabwe Policy and Guidelines which concretized government’s policy intentions to adopt the PPP framework in the provision of infrastructure. In 2010 the Government refined the policy framework and published Public Private Partnership Policy and Guidelines which formed the basis upon which PPP transactions would be structured. However, lack of the legislative framework to anchor the policy inhibited full implementation of these policies and guidelines.

The Joint Ventures Act [Chapter 22:22] of 2015 provides the legal framework that can facilitate the structuring of blended financing infrastructure projects. The Act defines the types of Joint Venture Agreements covered by it which include: Build Lease and Transfer (BLT); Build Operate and Transfer (BOT); Build Own and Operate (BOO); Build Own Operate and Transfer (BOOT); Build Transfer and Operate; Contract Add and Operate (CAO); Develop Operate and Transfer (DOT); Rehabilitate Own and Operate (ROO) among other types of contracts. The PPP arrangement is one option of blending Public and Private sector resources in the provision of infrastructure.

The achievement of 2030 Agenda for Sustainable Development, the SDGs, is premised on building resilient infrastructure, promotion of inclusive and sustainable industrialization and fostering innovation. The country's economic policy blue prints i.e. the Medium-Term Plan (2011-2015); ZIMASSET (2013-2018) and the Investment Guidelines and Opportunities in Zimbabwe (2018) and the Transitional Stabilisation Programme (TSP, 2018) have identified the blending finance, in particular the PPPs framework, as an implementation modality for infrastructure provision¹ However, a salient feature of these blue prints is that they are not building on each other. They are on stand-alone basis which is a major weakness especially for promotion of long-term multi-year infrastructure projects.

The other weakness of these policy blue prints and frameworks which has adverse implications on mobilising blended infrastructure finance is a lack of provisions for funding and action plans to facilitate implementation of planned projects. The need to broaden the scope of infrastructure funding to include blended finance² beyond PPPs, sets the context for this study which provides an in-depth review of the opportunities that exist in Zimbabwe for blending public resources including donor funded grants with private sector interest bearing instruments³ to finance infrastructure development in Zimbabwe. The findings of the study are expected to inform IDBZ's resource mobilisation strategies and policy options to be considered by government in support of infrastructure development. The study also draws lessons from other country/project experiences on ways of improving project governance cycles and proffers recommendations of how to close the infrastructure gap in Zimbabwe.

1.1 Overall objective of the study

The overall objective of the study is to contribute towards improving the body of knowledge and provide input into formulation of strategies to mobilization of both public and private resources towards infrastructure development in Zimbabwe. Infrastructure development and provision is a key pillar for sustainable development and transformation of the economy. This overall objective is thus underpinned by some six specific objectives as follows.

1.1.1 Specific objectives of the study

The specific objectives of the study include the following:

- i. Analyzing the global and regional emerging trends on blending public and private sector resources for infrastructure funding;
- ii. Reviewing at least five Zimbabwean and five African projects that were implemented successfully through blending both public and private interest-bearing instruments to finance infrastructure projects and how such cases may be replicated in Zimbabwe. Identification of those blended finance projects whose implementation were not successful (failures) would also provide lessons for future projects. The study also identified some possible projects in Zimbabwe and recommends possible areas where bankable projects can be developed for blended finance infrastructure projects. These projects may need to be followed up with feasibility studies to build a business case.
- iii. Reviewing and recommending the legal, technical and policy environment that will enable effective participation of the private sector in infrastructure development including the PPPs framework.
- iv. Reviewing and recommending the most appropriate legal, policy and institutional framework that facilitate the blending of private and public funding for infrastructure development. The review took cognizance of the legal framework at central Government, local government and other agencies that may hinder or facilitate progress in infrastructure delivery.
- v. Reviewing and recommending the most appropriate fiscal and monetary policy environment that facilitate the blending of private and public funding for infrastructure development and;
- vi. Coming up with possible options/strategies in which international Official Development Assistance (ODA) could be programmed in such a way as to facilitate its blending with private interest-bearing instruments for infrastructure funding in Zimbabwe.

¹ A salient feature of these blue prints is that they are not building on each other. They are on stand-alone basis which is a major weakness especially for promotion of multi-year infrastructure projects.

² According to Convergence while MDBs and DFIs have co-invested with the private sector for decades, blended finance came into mainstream after the Third International Conference on Financing for Development in July 2015 where blended finance and other innovative finance mechanisms were recognized as solutions for addressing the SDGs funding gap in developing countries, page 32

³ Interest bearing instruments refer to paper instruments issued in the capital markets such as bills and bonds for the purpose of financing infrastructure projects.

1.2. Methodology and Approach Used for the Assignment

The research team adopted mixed methods approach that involved a quantitative and qualitative analysis to address the study objectives outlined above. The key methodological steps adopted included an inception meeting with the IDBZ officials. An inception workshop was also held with key stakeholders with interest in blending of public and private sector resources in infrastructure development. The inception workshop assisted the team to establish key stakeholder concerns, source of data and stakeholder mapping as well as selecting stakeholders that were targeted as key informant interviews.

This was followed by extensive desk review and analysis of literature on global and regional trends in blended financing of infrastructure projects; reviewing of key government policy documents; regulatory frameworks and consultancy reports/studies focusing on infrastructure development in Zimbabwe. These reviews enabled the research team to distil the challenges and opportunities available for implementing blended finance infrastructure projects. The reviews and country case studies helped the research team to better understand the operational context of blending of public and private sector funding in financing infrastructural development.

Examples of reviewed policies and legislative frameworks include: ZimAsset; Transitional Stabilization Programme (TSP); Budget Statements; ACTs of Parliament (Joint Ventures Act, Special Economic Zones Act, Zimbabwe Investment Authority Act); Public Sector Investment Guidelines (2010) and Sectorial Policies. The following IDBZ documents were also reviewed: IDBZ Act [Chapter 24:14]; Medium Term Strategy: 2016 – 2020; Results Measurement Framework: 2016 – 2020; Bank's Annual Work Programmes; Budgets; Policies; Operations Guidelines and Manuals; and the Bank's Resource Mobilization and recapitalization strategies to gain a deeper understanding of IDBZ operations.

Survey reports and studies on infrastructural structure financing commissioned by development partners such as World Bank and the AfDB, were also reviewed. The study also relied on online sources for information on global and regional trends in infrastructure financing including relevant case studies on blending public and private sector funding in infrastructure development. The information gleaned from the document reviews assisted in contextualizing this study and development of relevant data collection instruments for the same.

The research team also developed research instruments that were used to collect primary data from key informants to complement and triangulate with secondary data analysis. The data collection instruments captured both qualitative and quantitative information and had sections where stakeholders could comment on their perceptions regarding the impact of policies and practices; legislative and regulatory frameworks in facilitating/inhibiting blending public and private sector resources in infrastructure development in the country. A purposive sampling technique was used to select the participating institutions for the interviews. The selection was also based on geographical location whereby the research team covered the major towns in the country including Bulawayo, Harare, Mutare, Masvingo and Gweru. Key informants who were interviewed were drawn from government; financial institutions; regulatory authorities; local authorities; universities; parastatals and private sector players.

The data collection instruments were administered in pre-arranged face-to-face meetings with the key informants by members of the research team. This was done to ensure that all the relevant sections of the questionnaire were captured and at the same time allowing the research team to probe further on any other leads arising from the responses by the stakeholders in each interview. Notes on major highlights arising from each interview were drafted by the team member leading in each of the interviews and these were shared among the entire research team to facilitate coherence in the analysis and drafting of the study report. Thus, the qualitative and quantitative analysis of the primary and secondary data collected including field observations were used as a basis to prepare this report

1.3. Outline of the rest of the report

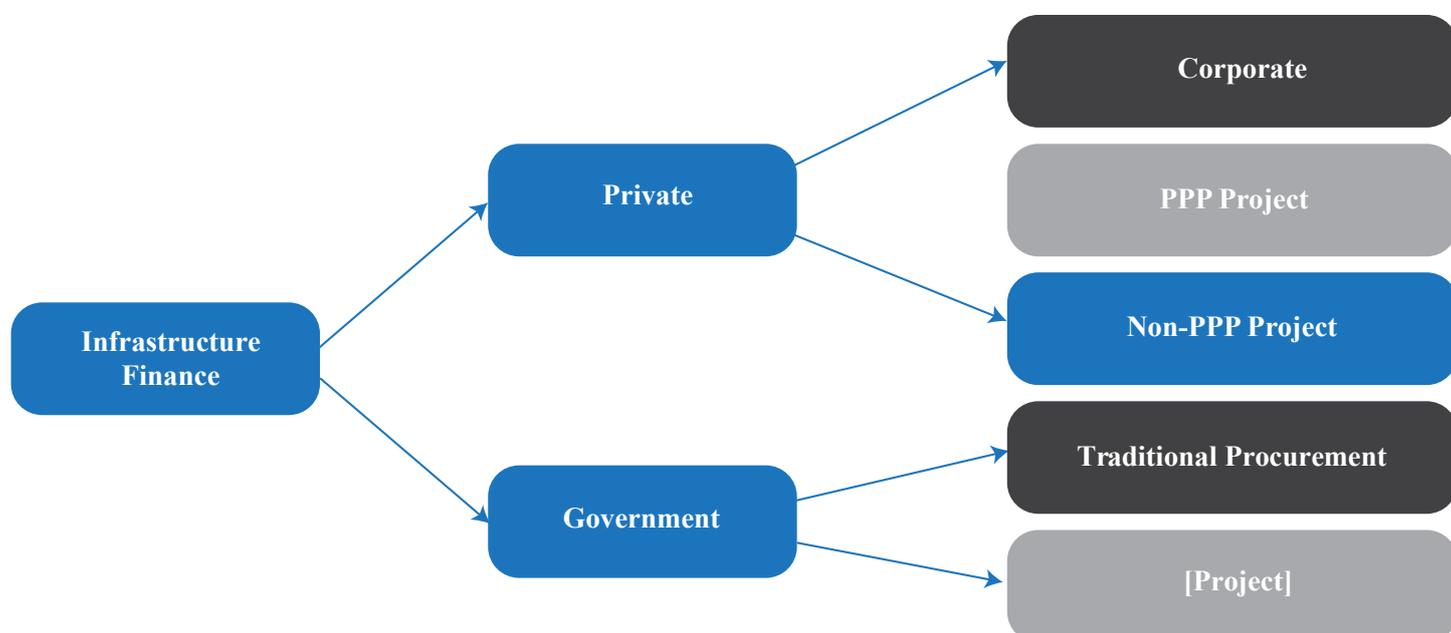
The rest of the report is structured as follows: Chapter 2: Recent Global Trends on blending public and private sector resources for infrastructure funding; Chapter 3: African experience in blending both public and private interest-bearing instruments to finance infrastructure projects; Chapter 4: Zimbabwean Experience in blending both public and private interest-bearing instruments to finance infrastructure projects; Chapter 5: Regulatory, Legal and Institutional and Policy Environment that Facilitates Blended Infrastructure Finance; Chapter 6: Opportunities for Blending in Infrastructure Funding and Chapter 7: Recommendations and Conclusion.

Chapter 2: Recent Global Trends on blending public and private sector resources for infrastructure funding

2.1. Global Trends on blended finance

As we discuss the evolution of blending public and private sector resources, it is important to understand how infrastructure financing has generally been structured or composed prior to the emergency of blended finance especially given that blended finance entered mainstream themes in conferences only recently (see footnote 3). The diagram below (Figure 1) decomposes infrastructure finance into its various components. The upper branch consists of private finance which is further broken down into corporate finance, private public partnership (PPP) finance and non-PPP projects finance. On the lower branch, the Government budget finance consists of investment through traditional public procurement, and a few projects financed by public sources. A typical mechanism of financing infrastructure projects is through a special purpose vehicle (SPV) funded through government/local authority using public resources. The SPV is typically used in Project finance where there is no recourse to the sponsor of the project.

Figure 1: Composition of Infrastructure Finance



Source: Rein Wagenvoort, Carlo de Nicola, Andreas Kappeler (2010)

It is also important to understand, in a general way, how in the past the various sources of funding infrastructure have responded to booms and busts before we delve into the discussions of recent trends in blended finance. Table 2 below shows how infrastructure funding particularly from the private sector suffered severely from the 2007/2008 global financial crisis (Deloitte, 2013).

Table 2: Annual growth of infrastructure finance, inflation adjusted, – EU average, % GDP

	Government financing as % of GDP	Private financing as a % of GDP
2005	1.7	3.3
2006	4.4	6.3
2007	3.1	5.8
2008	6.1	-4.3
2009	7.8	-13.2
Number of observations	19	19

Source: Eurostat, Projectware, EIB/EPEC

The data shows the sensitivity of Government and private infrastructure finance to crisis in the European Union. Public finance which stood at 3.1% as a percentage of GDP in 2007 rose to 7.8% in 2009. In contrast, private finance fell from 5.8% in 2007 to -13.2% in 2009. This was mainly because infrastructure finance is pro-cyclical. Leading up to the Global Financial Crisis (GFC) in 2008, bank funding was freely available, with significant competition between funders on projects driving pricing to historic lows, and also increasing gearing and hence debt volumes (Deloitte, 2013). However, during and after the financial crisis, the situation changed dramatically as reflected in the Table 2 as funding sources from the private sector became limited due to reduced profitability, illiquid short term wholesale funding markets and as banks were going through a process of repairing balance sheets to reduce debt levels. The development depicted in Table 2 serve as an important lesson to always consider balancing public and private sector project financing to avoid drying up of one source of infrastructure funding during recessions.

Another important factor to consider as countries seek blended finance from sponsors is the preference of the sponsors by sector. In Table 3, the EU experience shows that Government is by far the most important investor in education (87.1% compared to 12.9% by private sector) while private sector dominates in blended finance to the health (67.6%), transport (68.8%) and utilities (78.5), respectively. This preference by the private sector to participate in areas that tend to generate significant cash flows is key for when strategizing and mobilising private blended finance.

Table 3: Composition of infrastructure finance in the EU across sources, by sector of activity (2006-2009)

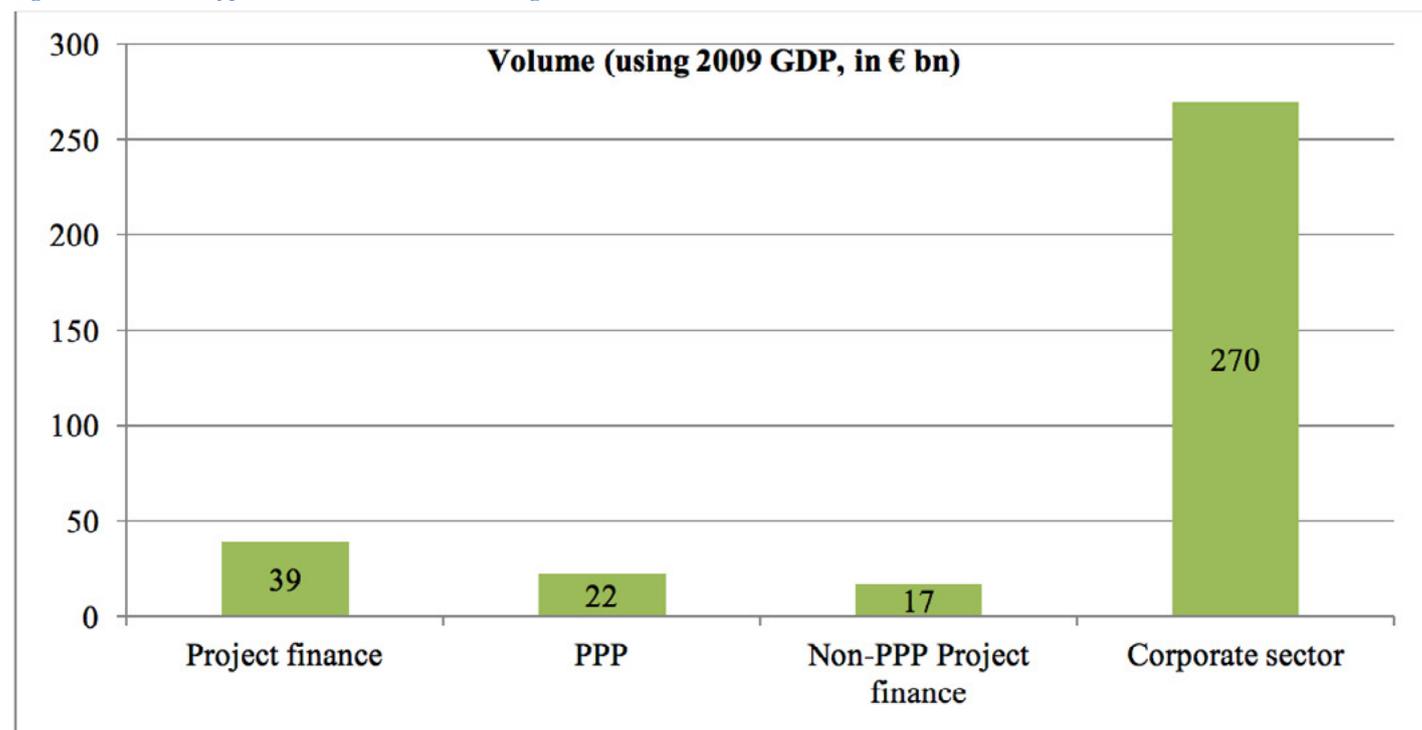
	Education	Health	Transport	Utilities
Government	87.1	32.4	31.2	31.5
Private	12.9	67.6	68.8	78.5
Corporate	5.7	61.6	62.6	60.3
PPP	6.7	5.8	5.1	1.8
Non-PPP	0.5	0.2	1.1	16.4
Number of observations	24	24	20	20

Source: Carlo de Nicola, et al (2010)

Private Infrastructure Spending in Europe⁴

From Figure 2 below, it can be deduced that project finance (financing based on project cash flows) is still a small proportion of total private sector financing. Corporate finance, which is balance sheet based financing i.e. loans and bonds, constitutes a very large proportion of blended private sector infrastructure financing.

Figure 2: Different types of infrastructure financing in the EU, 2013



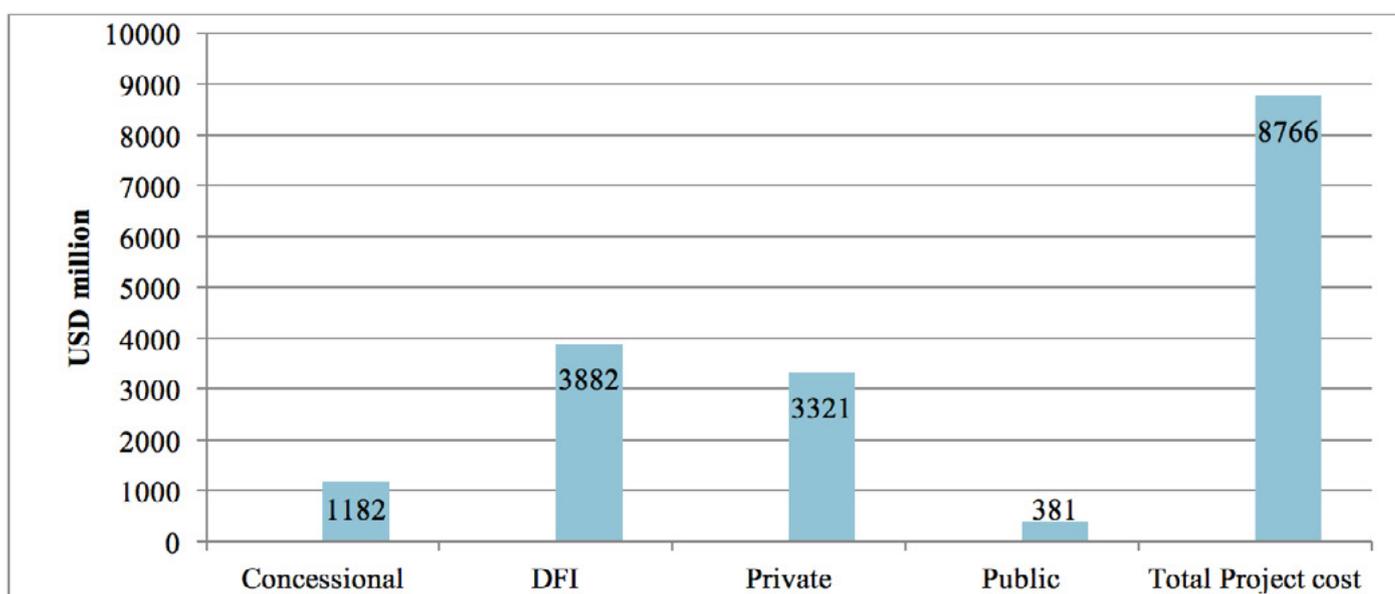
Source: EIB, 2013

⁴ It is important to note that in this analysis, private finance is defined as a residual of total infrastructure investment (minus government investment (Eurostat figures)), corporate finance as a residual within private finance (minus project finance (Dealogic figures)), and, finally, non-PPP as a residual within project finance (minus PPP (EPEC figures)).

Recently, it has emerged that there is a change from funding infrastructure using only government budgets due to a lack of the fiscal space to finance, as well as the required skills needed to design and manage all the infrastructure investments required to meet the sustainable development goals (SDGs). So the focus is now on how to “crowd in” the private sector investment and private management utilizing blended finance (EMCompass, April 2016). This is because government balance sheets are increasingly becoming constrained, making it more difficult to fund infrastructure projects hence the emergence of more blending initiatives globally. The emerging trend on the demand side appears to be emphasizing the blending of concessional finance (Development Finance Institutions (DFI)) with public and private resources and using these resources to catalyse or mobilize additional resources from other actors. It has been observed that blended finance has been successfully executed for projects that required public subsidy or enhancements to be viable. In these cases, government funding was used to ‘write down’ particular project costs (capital and/or operating) or risk elements either up front or over the entire project life cycle.

In line with the foregoing, data released by the DFI Working Group on Blended Concessional Finance for Private sector Projects in October 2018 shows the interesting evolution of blended concessional finance. In 2017, the DFIs financed projects worth more than US\$8.8 billion utilising blended concessional finance (US\$1.1 bn), Private sector finance mobilised for the projects to the tune of US\$3.3 billion and DFIs own account investments amounting to US\$3.9 billion (Figure 3). In fact, this pattern of blended concessional finance was also reflected in the IFC’s Blended Climate Finance (BCF) unit which manages a fund of US\$700 million. Since 2010, the BCF unit committed US\$281 million in donor finance to mobilise US\$1.1 billion in IFC financing and US\$3.7 billion in private sector investment, EMCompass note 3, 2016.

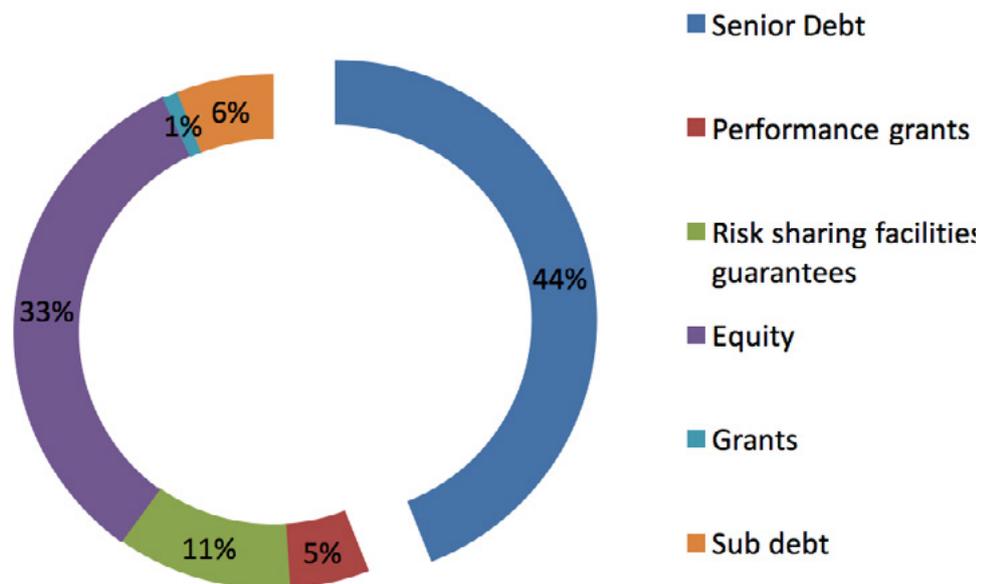
Figure 3: DFI Private Sector Blended Concessional Finance New Projects Commitments, 2017



Source: DFI Working Group on Blended Concessional Finance for Private Sector Projects, 2018

The most common concessional instrument used was senior debt (44%) followed by equity (33%), and then risk sharing facilities or guarantees (11%). Risk sharing facilities or guarantees play a significant role in facilitating and attracting risk capital (Figure 4).

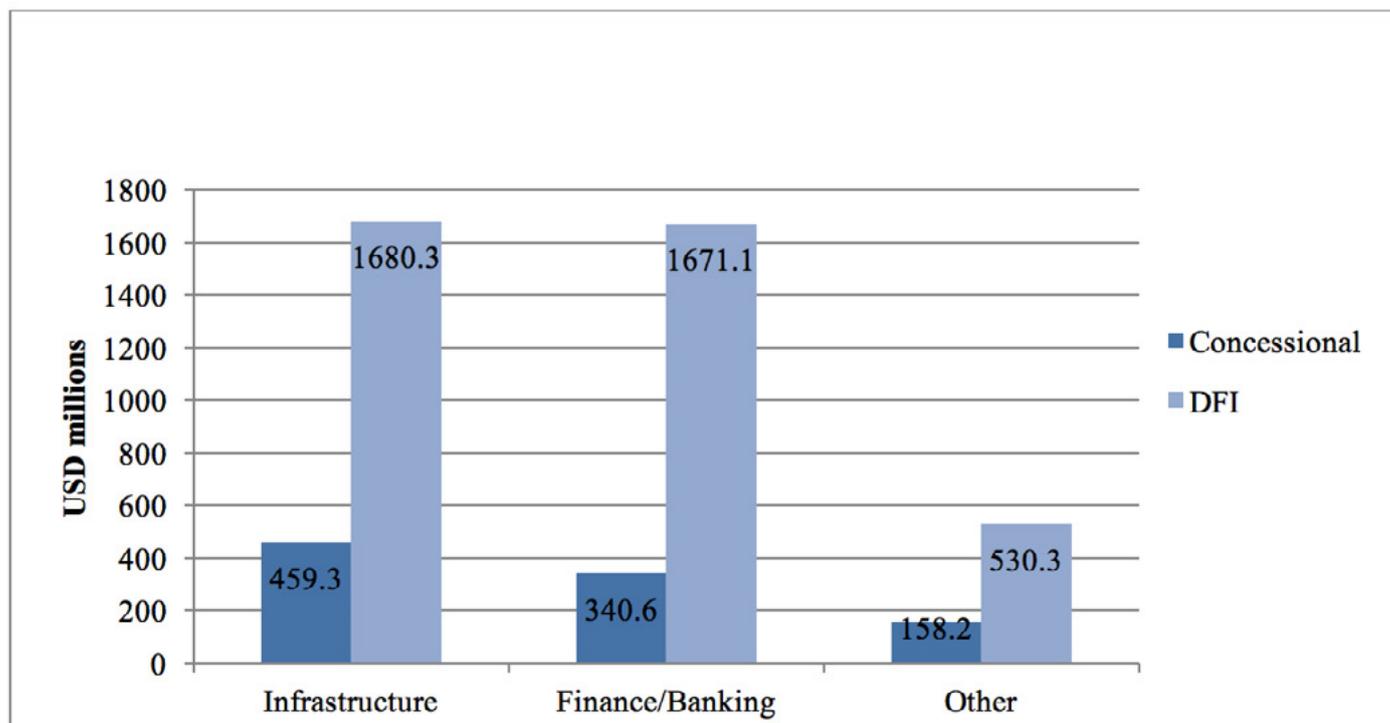
Figure 4: Concessional Commitment Volume by Instrument, 2017



Sector Projects, 2018

Figure 5 below shows the amount of concessional finance and DFI own-account commitments in different sectors in 2017. A broad range of sectors are represented, particularly infrastructure and banking and finance. Many infrastructure projects are associated with climate finance, and many banking projects address Small-Medium Scale Enterprises (SMEs). An example of blended infrastructure in the climate category was by the IFC's BCF unit in South Africa when US\$41.5 million was invested in two concentrated solar power plants that will avoid 442,000MTCO₂ emissions per year, the first of its kind in Sub-Saharan Africa. The "other" sector includes agribusiness, health and other projects.

Figure 5: Concessional and DFI Commitments by Sector, 2017



DFI Working Group on Blended Concessional Finance for Private Sector Projects, 2018

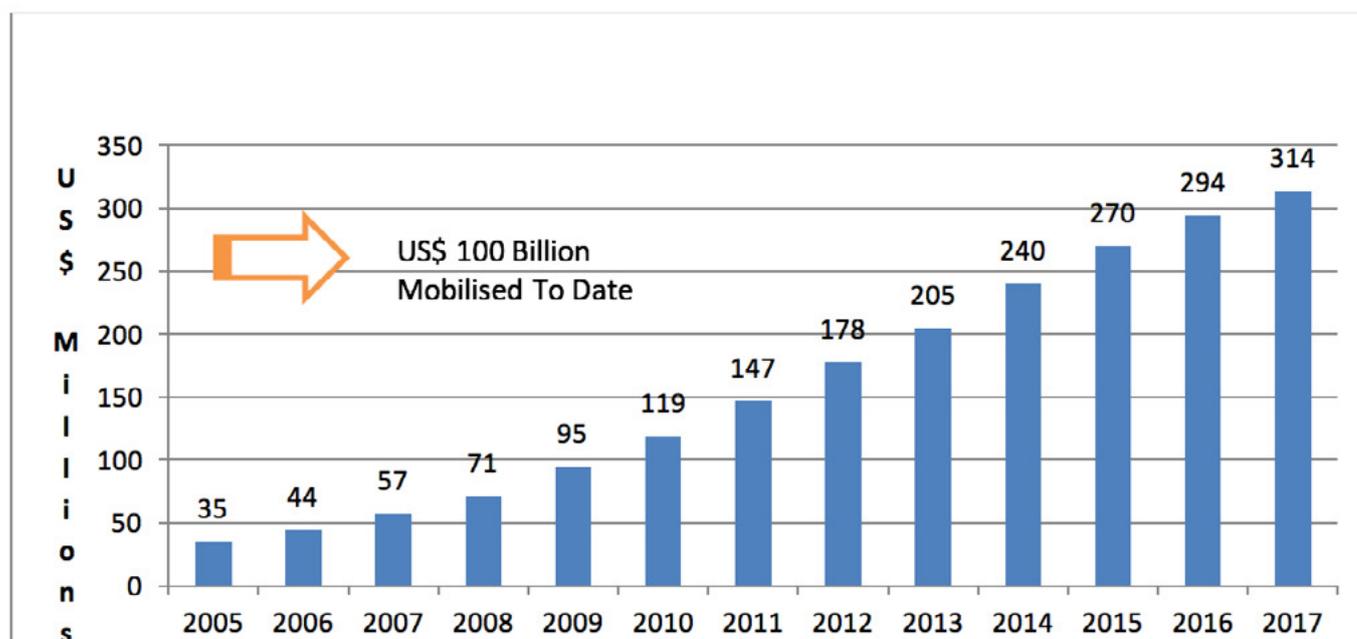
Discussions by the DFI Working Group on blended concessional finance showed that, geographically, the largest share of blended concessional funds went to the lower middle income countries (US\$3,768.9 million) followed by the upper middle income countries (US\$2,450.9 million). However, there was also significant engagement in low income countries (US\$336.2 million). At the regional level, while Sub-Saharan Africa received the largest share of blended finance (US\$326.0 million), the region received only US\$43.0 million infrastructure concessional funding with the bulk going to ‘other’ and finance and banking.

Convergence 2018, in their State of Blended Finance report released significant data on the emerging trends in concessional blended finance globally. The report provided deal trends covering the sizes of the deals and the types of deals. It also provided investor trends by development agencies and multi-donor funds, multilateral development banks and DFIs. The database captures over 2,500 financial commitments to over 300 closed blended finance transactions.

Figure 6 shows the evolution of blended finance mobilised since 2005. It is an interesting upward trend showing the increasing popularity of blended finance. The data is aligned to the SDGs and also reflects on the Addis Ababa Action Agenda⁵ on the “State of Blended Finance” in Africa published in 2017. As shown in the figure, aggregate deal size of blended finance is US\$100 billion with blended finance deal size ranging from US\$5 million to US\$ 1 billion with a median size of US\$50 million.

⁵ At the Third International Conference on Financing for Development in 2015 in Addis Ababa it was agreed that blended finance is one critically important approach to mobilise new sources of capital for the SDGs by deploying public funds to attract private investment.

Figure 6: The Trends in Blended Finance Mobilised To Date, 2018



Source: Convergence, 2018

According to Convergence 2018, Sub-Saharan Africa is the most popular destination with 42% of blended finance deals amounting, on average, to US\$125 million. The main recipients were Microfinance (50%) and renewable energy (60%).

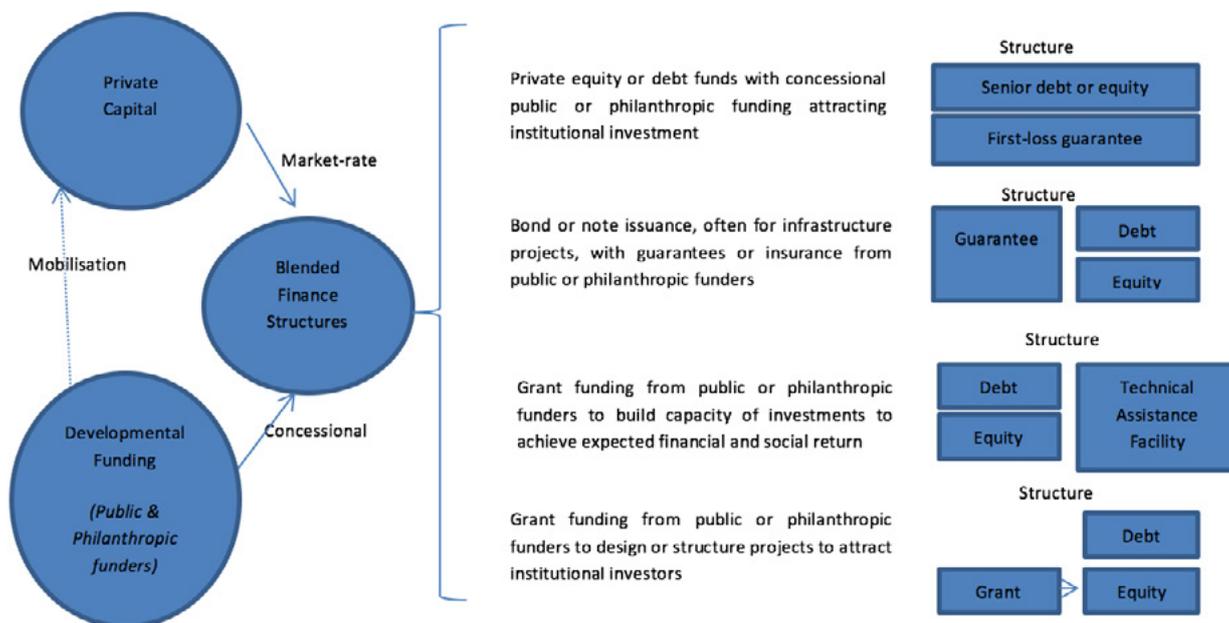
In 2017, there was a significant uptick in interest in blended finance and efforts to mobilise private sector investment more broadly led by the IFC and the Dutch Development Bank (FMO) who continue to refine and grow their blended finance (Convergence, 2018). In the same year, the OECD and the IFC led DFI Working Group agreed on the principles for blended finance as it relates to their development activities⁶. Agreed principles are important as there is still some scepticism from policy makers and traditional grant making agencies on the effectiveness and opportunity costs of blended finance.

Figure 7 below highlights four common blended finance structures in which concessional capital and guarantees/risk insurance are deployed by the public or philanthropic sector to create investment opportunity with acceptable risk-return profiles for the private sector by (i) de-risking the investment or (ii) improving the risk-return profile relative to market norms.

AfIDA Insider, 2018 also sees “the application of blended finance on a strong upwards trajectory as transactors and project developers look for alternative ways of financing projects, and investors look for less risky ways to gain access to new markets with strong returns potential”.

Figure 7: Typical Blended Finance Mechanics and Structures

⁶ The principles sought to improve effectiveness and efficiency of blended finance in contributing towards achieving the SDGs.



Source: *Convergence*, 2018

According to a study by Deloitte (2013), in addition to writing down particular project costs, project sponsors are increasingly looking for innovative ways to make projects viable by involving multiple public sector entities, both within and across jurisdictions. Public-public-private-partnerships, or ‘P4s,’ are starting to emerge as a way to get projects off the ground by combining multiple levels of public support (Deloitte, 2013). For instance, Deloitte study cited a new waste to energy project developed in Staffordshire in the United Kingdom which was a collaborative effort of a number of local governments that banded together to achieve economies of scale that would make the project viable. Meanwhile, the United States has for decades employed public-public partnerships to develop and finance infrastructure through the creation of joint powers agencies, multistate authorities, regional development agencies and other vehicles.

Deloitte (2009) noted that, an American Recovery and Reinvestment Act (ARRA) introduced in 2009 impacted the infrastructure sector in the US in two ways:

- a) The Act increased federal spending on projects;
- b) It expanded the instruments available in the US municipal bond markets to help ease the tight credit conditions.

The ARRA was designed to broaden the base of investors in municipal bonds, hence increasing private investments in infrastructure. A number of instruments were created through this ARRA but the anchor of the policy was the creation of the Build America Bonds (BABs). The introduction of the BABs was a significant shift in structuring municipality debt in that for the first time these were federally taxable bonds. The way it works is that the Federal Government makes an “explicit” subsidy in which it reimburses 35 percent of the bond interest payable, either to the municipal bond issuer (in cash) or to the municipal bond holder (in the form of tax credit). These BABs are taxable instruments saleable to a wider base beyond the traditional confines of the US municipal bond investor base. Historically, interest earned on municipal bonds issued for government purposes was exempt from federal income taxation. Although this implicit subsidy lowered the cost of capital for state and local governments, it limited the investor base to parties for whom exemption from federal taxation has value i.e. US tax payers only. Two important takeaways from this American experience are:

- (i) Broadening the investor base by extending benefits across the border, i.e. tapping into the foreign investors;
- (ii) Being innovative and creating new instruments that widen and deepen the market.

OECD (2015), observed that recent market trends have seen the development of co-investment platforms to leverage institutional investors’ capital in project finance. The report acknowledged that not all investors have the resources and expertise necessary to make direct infrastructure investments, but that some have built significant scale and market presence, along with the expertise to perform due diligence on infrastructure assets. These co-investment platforms pool investor capital to deploy directly in infrastructure projects, by passing intermediaries such as investment managers or banks. This trend is reinforced by large funds looking to reduce the cost of infrastructure investment, and to align internal governance and portfolio management models with direct blended infrastructure investments.

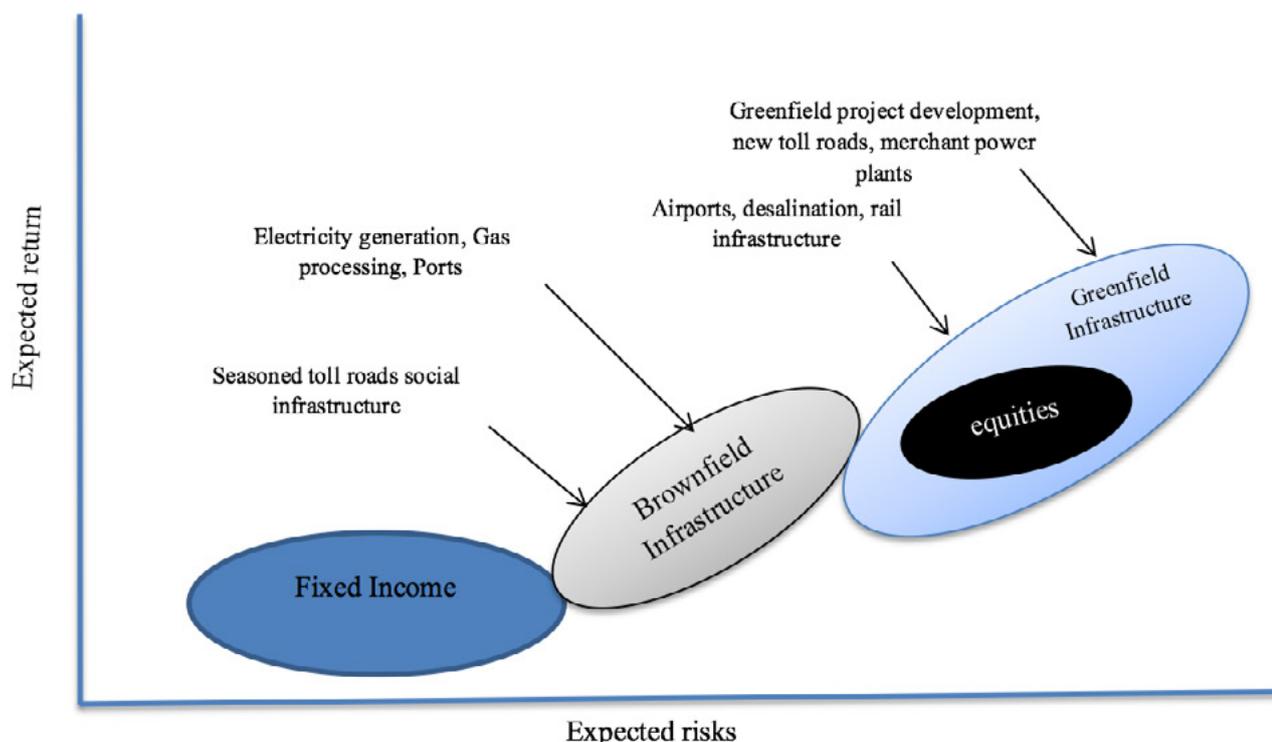
The OECD (2015) report also highlights that corporate finance is the dominant channel in blended private infrastructure finance particularly at the Greenfield and equity levels in figure. For instance, the report observed that private investment in regulated entities such as utilities has a relatively long track record, most often on the balance sheets of these companies. The same is true for developers in other sectors, such as waste, ports, oil and gas, and also traditionally in electricity generation. Companies listed on public exchanges are

sizeable owners of infrastructure assets, providers of infrastructure services and investors in infrastructure projects (ibid). They range from specialist businesses to diversified conglomerates. Examples of such companies include Larsen of India, Adani Ports of India, Siemens global and General Electric global. Further important takeaways from these experiences are:

- (i) Resources can be pooled together from investors and deployed directly into infrastructure projects;
- (ii) Deploying pooled resources directly into projects reduces project costs by not always investing through intermediaries.

Figure 8 shows that concessional blended private finance is mainly attracted at the Greenfield part of the chart where the trade-off between return and risk are high. Projects at that end normally generate sufficient cash flows to be self-financing.

Figure 8: Risk-return profiles of infrastructure investment vary widely in relation to traditional asset classes



Source: Credit Swiss Asset Management by Inderst (2010);

The same OECD (2015) also, observed that as a result of increased budgetary constraints, the financing of infrastructure has increasingly taken the form of project finance. Project finance is not based on the balance sheet of the entity seeking to secure funding but is, instead, based on the project cash flows generated by the project which are usually ring-fenced through an SPV. This technique has, of late, emerged to be the financial solution for infrastructure involving public entities in the role of either regulator or counterparty who do not have strong balance sheets. Project finance has been an increasingly popular technique to attract private capital, most notably investment in projects characterised by high specificity, low re-deployable value and high intensity of capital. The OECD (2015) report therefore mapped out the following:

- i. Investment options available to private investors and which instruments and incentives are available to attract private investors to infrastructure. The coverage of instruments spans all forms of debt and equity and the risk mitigation tools deployed by governments and agents;
- ii. Provides foundation for the identification of effective financing approaches, instruments, and vehicles that could broaden financing options available for infrastructure projects and increase as well as diversify the investor base;
- iii. Focus on identifying new and innovative financing instruments and risk mitigation techniques used to finance infrastructure assets.

A characteristic of project finance is that sponsors provide no guarantees beyond the right to be paid from the project's cash flows. Nevertheless, sponsors need to attract large amounts of resources, which leave them highly leveraged with up to 70%⁷ percent provided by lenders. There is a wide range of financing channels for infrastructure investment, both direct and market-based. Each financing channel has its own set of characteristics and implications for lending or investment portfolios. Capital markets can be an efficient way to allocate risks to those investors that are most willing to bear them at an agreeable rate of compensation. Table 4 complements figure 8 by providing a catalogue of market-based financing instruments that can be used in blending concessional infrastructure finance across the spectrum of investors.

⁷ Investors are now requiring sponsors to share the risks by committing own resources in the project and they are not keen to provide 100% debt.

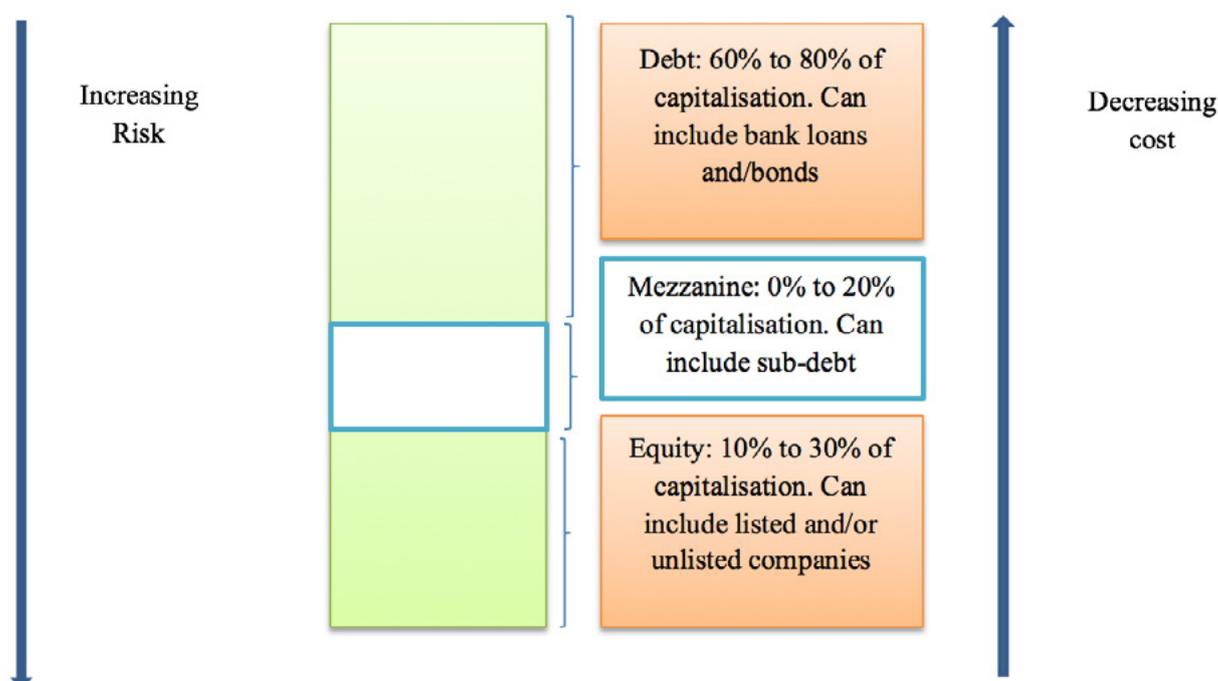
Table 4: Taxonomy of instruments and vehicles for blended infrastructure financing

Modes		Infrastructure Finance Instruments		Market Vehicle
Asset Category	Instrument	Infrastructure Project	Corporate Balance Sheet/ Other entities	Capital Pool
Fixed Income	Bonds	Project bonds	Corporate bonds	Bond Indices, Bond Funds, ETFs
		Municipal sub-sovereign bonds	Green bonds	
		Green bonds	Subordinated bonds	
	Loans	Direct/Co-investment lending to infrastructure project, syndicated project loans	Direct/Co-investment lending to infrastructure corporate	Debt Funds (GPs) ⁹
			Syndicated Loans, Securitized Loans (ABS), CLOs	Loan Indices, Loan Funds
Mixed	Hybrid	Subordinated loans/bonds Mezzanine Finance	Subordinated Bonds, Convertible Bonds, Preferred Stock	Mezzanine Debt Funds (GPs), Hybrid Debt Funds
Equity	Listed	Yield Cos	Listed infrastructure & utilities stocks, Closed-end Funds, REITs, IITs, MLPs	Listed Infrastructure Equity Funds, Indices, trusts, ETFs
	Unlisted	Direct/Co-investment in infrastructure project, equity, PPP	Direct/Co-Investment in infrastructure corporate equity	Unlisted Infrastructure Fund

Source: OECD (2015)⁸

Infrastructure projects often have higher levels of leverage than non-infrastructure investments, given less volatile cash flows and the willingness of sponsors of infrastructure projects to accept higher levels of debt (Beeferman and Wain 2012). Debt instruments have historically comprised 60-80% of the total capitalisation of infrastructure projects (see Figure 9). Infrastructure’s capital intensive nature, generally low-to-manageable operating risk, and the long-term importance of infrastructure services can help to support higher levels of leverage⁹ than similarly rated non-financial corporations (Moody’s, 2018¹⁰).

Figure 9: Blended Financing Instruments



Source: Adapted from Weber and Alfen (2010)

⁸ These are General Partnership Funds which are regarded as pooled funds.

⁹ Financial leverage (gearing) is the use of debt to increase the expected return on equity. Financial leverage is measured by the ratio of debt to debt plus equity (= debt/(debt + equity)).

¹⁰ see http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1110153.

Another emerging trend at the global level is the manner in which risk is allocated among the different parties to blended financing projects as shown in Table 5. One of the key features of blended finance projects is the whole process of allocating risks to the party best able to manage the risk concerned. The table below shows some of the key risks that must be managed in blended financing projects and how they are usually shared.

Table 5: Allocating Key Risks in Blended Financing Projects (i.e. parties responsibilities)

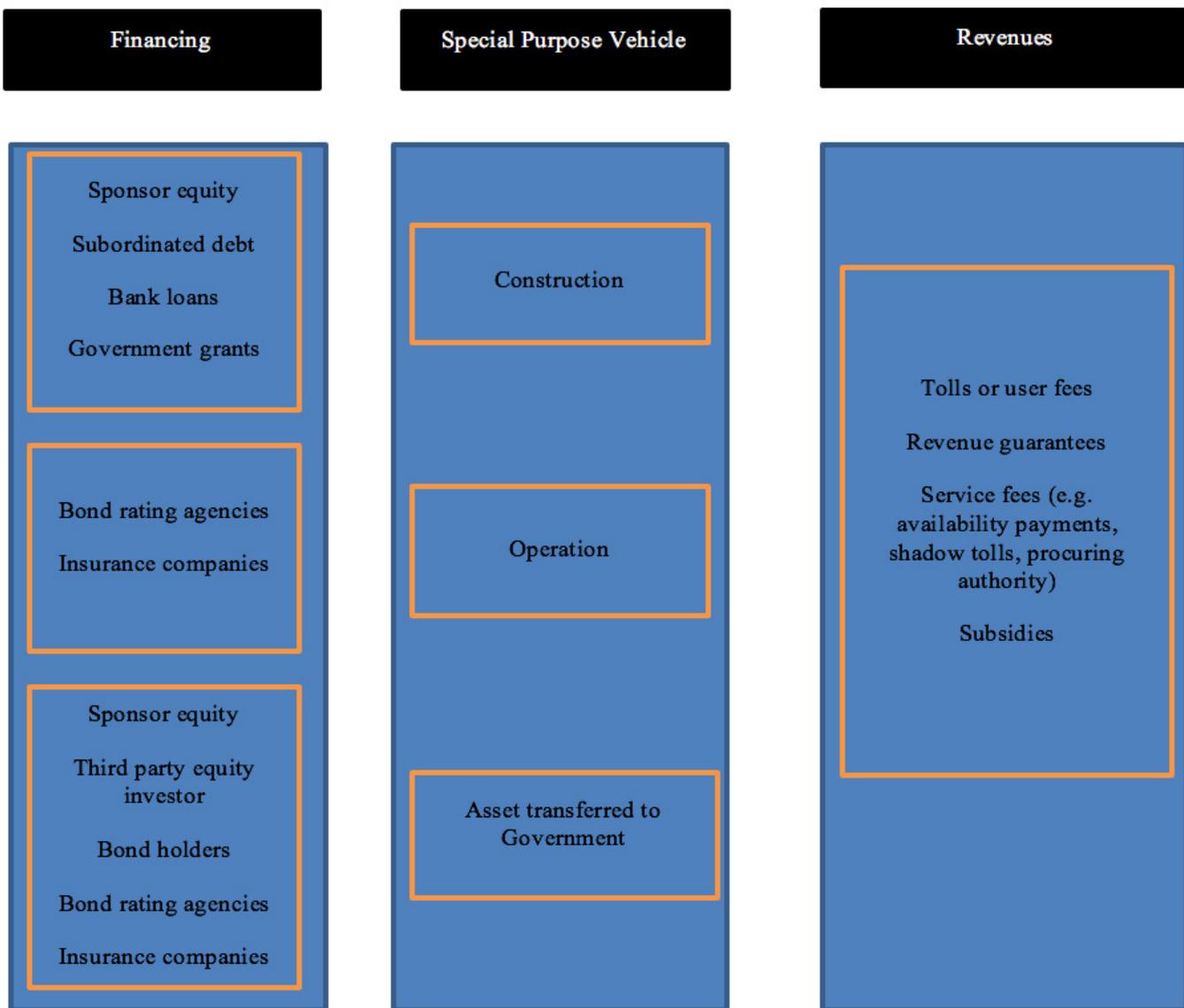
Type of Risk	Description
Completion Risk	Risk that the project is delayed for commissioning within the prescribed timeframes. Typically allocated to the private party. Can be mitigated through the provision of construction bond/guarantees or insurance.
Force Majeure Risk	Occurrence of events beyond control of both parties and prevents either party from performing its duties/obligations. Risk generally shared between the parties.
Market Demand or Volume Risk	Forecast demand for use of a particular facility is not met. Common risk e.g. on toll roads where alternative routes or means of transport are used thereby reducing the traffic. Allocation of the risk often depends on the revenue model – e.g. for user charges it is allocated to the private party; for availability payments it is allocated to government as long as facility is operational.
Design/Output Risk	Capacity/output or performance of the project facility may not meet the agreed design criteria or project specifications. Typically allocated to the private party. Mitigated through clear regime in the concession/offtake agreement setting out the required technical parameters.
Finance Risk	Availability of financing to develop a project, interest rates, inflation and foreign currency risks. Usually allocated to the concessionaire. In markets where there is non-transferable currency, the foreign exchange risk is assumed by the government.
Cost overrun Risk	Cost of project overrunning projected amounts – allocated to the concessionaire. Usually mitigated by arranging a fixed lump sum construction contract.
Political Risk	Generally covers acts of war, imposition of sanctions, blockades or embargoes, and failure to issue or renew consents required for a project. Risk lies with government

Source: Self and Dentons, 2018

Transfer of some project risks to the private sector, which brings with it private sector expertise, financial discipline and timely delivery of projects is an evolving aspect in the management of risk in blended finance. Considerable transfer of construction, operation and maintenance, financing, technology and more risk tends to be transferred to the private partners who are more innovative in how to manage and mitigate such risks. Usually, the private sector achieves this by apportioning key risks to the suppliers and contractors in the project’s value chain. Growth and spread of blended finance is closely linked to the development of project finance, a technique based on lending against the cash flow of a project that is legally and economically self-contained (Yescombe, 2007). The diagram below depicts a typical life cycle of blended finance SPV.

Figure 10: The Financial Lifecycle of blended finance SPV¹¹

¹¹ Typically project cash flows are ring-fenced.



Source: Eduardo Engel et al (2010) and own adjustments

From the above discussion, the trends in infrastructure funding with regards to blending in the global market can be summarised as follows:

- 1) It has been demonstrated that the corporate sector has always been a significant player in infrastructure financing even before the emergency of blended finance.
- 2) Data released by DFI Working Group in October 2018 shows tremendous uptake in private sector blended concessional finance new projects to the tune of US\$8.8 billion in 2017.
- 3) Blended private finance mobilized has been growing in leaps and bounds since 2005 (US\$35 billion) to 2017 (US\$314 billion; showing an average annual growth of 7.7 percent’.
- 4) The DFI Working Group data also shows that the most preferred instrument in blended concessional finance is senior debt (44%) followed by equity (33%) and risk sharing facilities or guarantees (11%).
- 5) With respect to which private sector attracts the most blended concessional financing, infrastructure led the pack and was closely followed by finance/banking (specifically destined for SMEs).
- 6) Balancing of the partnership in financing infrastructure by the public and private sector is critical especially during periods of financial crisis as reflected in Table 2 which shows flight to safety by the private sector in times of financial crisis.
- 7) Introduction of innovative new financial instruments such as the ARRA and BABs in America, which expanded the instruments available in municipal bonds markets and introduced an explicit subsidy in which the government reimburses 35% of the bond interest payable either to the bond issuer (in cash) or to the bond holder in the form of a tax credit is a good innovative lesson. The initiative expanded the instruments available in the local market and also widened or broadened the investor base to outside the country borders;
- 8) Recent market trends have seen the emergence of co-investment platforms which pool investor capital to deploy directly into infrastructure projects hence by-passing intermediaries such as investment managers and/or banks thereby saving some significant amounts reducing the project costs;
- 9) Trends have seen Project finance which is an off balance sheet instrument and is based on the strength of cash flows generated by the project emerging as an alternative blended concessional infrastructure funding mechanism mainly via the creation of

special purpose vehicles.

2.2 Examples of Global Infrastructure Investment Funds and Platforms

IDBZ itself is an infrastructure investment platform and therefore should benefit from the experiences of other global infrastructure investment platforms and infrastructure investment trusts. This section is included to demonstrate some of the global structures involved in blended concessional infrastructure financing and also to broaden the innovative/alternative funding approaches that help in creating infrastructure as an asset class. In fact, some of the leading drivers of concessional blended finance such as the DFIs Working Group belong to these platforms.

2.2.1 Infrastructure Debt Funds

Infrastructure debt is the fixed income component of infrastructure assets. Infrastructure debt can take the form of corporate debt (balance sheet lending) or project finance debt (cashflow lending), and expose investors to different credit and risk/return profiles. It provides yield enhancements, especially those dealing with capital preservation. Preqin¹² currently holds information on 26 infrastructure fund managers managing a total of 38 unlisted infrastructure debt funds.

Key Infrastructure fund managers currently raising debt funds include Aviva Investors, which is seeking £1 billion in commitments for Aviva Investors Hadrian Capital Fund I, Hastings Funds Management and Sequoia Investment Management Company, both raising debt vehicles targeting €1 billion. infrastructure debt¹³ is also an expanding asset class for Australian pension fund investors. Fund managers that operate in this space include AMP Capital (www.ampcapital.com), Infradebt (www.infradebt.com.au), IFM Investors (www.ifminvestors.com) and Westbourne Capital (www.westbournecapital.com.au).

2.2. Infrastructure Investment Platforms¹⁴

The Infrastructure Investment Funds invest in infrastructure platforms and infrastructure services companies with high growth potential that derive their revenues principally from infrastructure projects. The targeted investments cover a number of sectors, including the following examples and related sectors:

- Energy and utilities (e.g. renewable energy, electric transmission and distribution networks, water and wastewater systems, smart cities, etc.);
- Transportation and logistics (e.g. roads, airports, bridges, tunnels, ports, railways, waterways, intermodal systems linking various transport modes, urban transport, logistics and logistics related infrastructure, etc.);
- Other sectors including telecommunications, broadband, urban PPP projects, healthcare and education.

There are several important global infrastructure investment initiatives that are at various early stages of development. These include: the Juncker Plan, November 2014, the G20 Global Infrastructure Initiative, November, 2014, the establishment by the European Commission of infrastructure investments as a new asset class, October 2015, and the launch by the International Finance Corporation (IFC) of a new accounting platform earmarked for infrastructure projects in emerging markets, November, 2015 (Winrow, 2015). The following are examples of major investment platforms:

1. **The European Investment Bank Model (Investment Platform)** - with total assets just exceeding half a trillion Euros in 2014 and funded projects in over 160 countries (Arezki et al, 2016).
2. **The World Bank's Global Infrastructure Facility (GIF)** - officially established at its October 2014 Annual Meeting (Arezki et al, 2016). The World Bank's involvement in infrastructure investment is of course not new. It has been engaged in infrastructure financing ever since its creation in 1945, and has thus accumulated a deep expertise in this area.
3. **The European Bank for Reconstruction and Development (EBRD) Equity Participation Fund** - the EBRD Equity Participation is another infrastructure investment platform (EUR 750 million to EUR 1 billion). The platform is structured as a General Partnership (GP) into which investors are admitted as Limited Partners and adhere to the terms of the Fund. The General Partner (GP) is an English limited liability company, owned 100% by a third party administrator (Arezki et al, 2016).
4. **The Asia Infrastructure Investment Bank** – created in 2016, it is entirely dedicated to infrastructure investment, as its name indicates. It has a start-up committed capital of US\$50 billion with another US\$50 billion in future capital

¹² Preqin is a data solutions company and also involved in compiling fund managers and funds <https://www.preqin.com/>

¹³ See https://byai.de/fileadmin/PDFs/DE/Themenschwerpunkte/Infrastruktur_11_18/BLK_-_Deconstructing_Infrastructure_Debt_-_EMEA_002_.pdf for some discussion on the performance of infrastructure debt.

¹⁴ See <https://www.imf.org/external/pubs/ft/wp/2016/wp1618.pdf>, for details.

commitments. While the total committed capital of the AIIB is lower than the EIB's, analysts say its maximum leverage ratio is much higher (borrowing may be as high as 20 times capital) so that total assets of the AIIB could be double those of the EIB when it reaches full capacity.

2.3 Infrastructure Investments Funds¹⁵

Infrastructure Investment Funds are like mutual funds which enable direct investment of small amounts of money from possible institutional investors or individuals to invest in blended concessional financing for infrastructure to earn a small portion of income as returns. Investments Trusts work like mutual funds or real estate investment trusts (REITs).

Table 6: Infrastructure investment funds

Why Investment Infrastructure Trusts		Investment Infrastructure Trusts
Aiding in financing/refinancing of infrastructure projects	Sponsor	Set up Infrastructure Investment Trust
		Hold minimum required percentage of total units of the Investment Infrastructure Trust
Unlocking tied up capital of developers	Trustee	Hold Infrastructure Investment Trusts assets in the name of the Infrastructure Investment Trust for the benefit of unit holders
		Ensure investment manager makes timely payment of dividend to unit holders
Lowering domestic financial institutions' loan exposure	Investment manager	Make investment decisions in relation to underlying assets
		Ensure assets have proper legal title and contracts entered are legal, valid and binding
Attracting foreign capital	Project Manager	Undertake operations and management of Infrastructure Investment Trusts
		For under construction projects, ensure progress of developments, approval status and such other aspects

2.4. Lessons Learnt

- 1) A first lesson is the ability of the platforms to leverage concessional public money – committed capital from government contributions and their own resources - by attracting private investors as co-investors in infrastructure projects thereby increasing the efficiency and effectiveness of blended infrastructure development finance;
- 2) The private investors together with the platforms can achieve more efficient blending concessional resources with private resources;
- 3) Investment Platforms and other infrastructure funds are not just lead investors providing some loss absorbing capital to private investors, they also give access to their expertise and unique human capital to private investors, who would otherwise not have the capabilities to do the highly technical, time-consuming, due diligence to identify and prepare infrastructure projects.
- 4) Platforms issue highly rated bonds to long term investors which also match the maturity profiles of the institutional investors and they tend to fund larger projects;
- 5) They coordinate investment for entire infrastructure and networking thereby increasing the bankability of individual projects.
- 6) A common thread running through all these funds is the ability to mobilise additional blending funds mainly from institutional investors (pension funds, insurance companies, sovereign wealth funds, etc.) and other interested investors.
- 7) In the case of Zimbabwe, the platform (IDBZ) can employ the same strategies to use public funds and its own funds to mobilize private funds from institutional investors. According to the Life Offices Association of Zimbabwe there is a good base of institutional investors (pension funds and life policy) in the country whose asset base is in excess of US\$2.7 billion which presents an opportunity for blending finance for infrastructure projects.

¹⁵ See (<https://www.asx.com.au/products/managed-funds/infrastructure-funds.htm>) for details.

Chapter 3: African experience in blending both public and private interest-bearing instruments to finance infrastructure projects

Facing the dearth of infrastructure funding, an increasing number of countries in Africa are exploring opportunities for blending public and private sector funding to address the infrastructure deficits on the continent. A lack of modern infrastructure is a major challenge to Africa's economic development and constitutes a significant impediment to the achievement of the Sustainable Development Goals (SDGs). According to World Bank (2017), there are varying trends in Africa's infrastructure performance across key sectors and regions. In telecommunications, Sub-Saharan Africa has seen a dramatic improvement in the quantity and quality of infrastructure, and the gains are broad-based. Access to safe water has also risen, with 77% of the population having access to water in 2015, from 51% in 1990. In the power sector, by contrast, the region's electricity-generating capacity has changed little in more than 20 years. At about 0.04 megawatts per 1,000 people, capacity is less than one-third of that of South Asia, and less than one-tenth of that of Latin America and the Caribbean (Fida Rana et.al. 2018)¹⁶.

The African Development Bank (AfDB), 2018 Economic Outlook¹⁷ also highlights that one of the key factors retarding industrialization in Africa has been the insufficient stock of productive infrastructure in power, water, and transport services that would allow firms to thrive in industries with strong comparative advantages. New estimates by the AfDB suggest that the continent's infrastructure needs amount to US\$130–170 billion a year, with a financing gap in the range US\$68–US\$108 billion. The report further notes that institutional investors such as insurance companies, pension funds, and sovereign wealth funds have more than US\$100 trillion in assets under management globally. A small fraction of the excess global savings and low-yield resources would be enough to plug Africa's financing gap and finance productive and profitable infrastructure. Initiatives to explore blended financing models are premised on the need to tap into the excess global savings to finance infrastructure and address the glaring infrastructure deficits on the continent.

In terms of mobilization of blended finance, Sub-Saharan Africa is the most popular target region, representing 42% of blended finance deals. However, the average deal size of US\$125 million for SSA is small when compared with a global average deal of US\$699 million (Convergence, 2018). Latin America and the Caribbean is the second most frequent region, followed by the Middle East and North Africa and then South Asia. Sub-Saharan Africa has the second smallest deal size after South Asia which registered US\$108 million during the same period (Ibid). Despite Middle East & North Africa garnering only 18% of blended finance deals, their average deal size of US\$229 million is almost double that of Sub-Saharan Africa. Within Sub-Saharan Africa, 73% of blended finance deals target countries in East Africa, which produced the continent's best economic performance in 2017 (Ibid). West Africa and Southern Africa are second and third most common target sub-regions in Sub-Saharan Africa, and Central Africa receives the least blended finance, which likely reflects underdeveloped local capital markets as well as political instability.

Africa Infrastructure Development Association (AfIDA, 2018) argues that there is a steady increase in the rate of blended finance deals in the periods 1980 through 2016. It also argues that Sub-Saharan Africa and North Africa mobilized blended finance which constituted 26.3% and 2.8% of global blended financing respectively between 2012 and 2014, respectively. This was followed by Europe (15.1%), South America (12.2%), South and Central Asia (11.7%) and North and Central America (8.9%) among other regions. DFI Working Group on Blended Concessional Finance Projects (2018) also argues that several blended concessional finance projects committed in 2017 by Development Finance Institutions (DFIs) include innovative renewable energy projects in frontier countries in Africa, supporting the financing of new technologies in North Africa. This view is also supported by AfIDA (2018) which argues that significant private capital mobilized through Blended Finance between 2012 and 2014 was directed towards the energy, industry, mining, construction and banking sectors. Other sectors prioritized by the Sustainable Development Goals (SDG's) like water and sanitation continue to experience funding deficits which corroborates the view of private investor preference in blended finance infrastructure projects.

When considering how sub-regions in Africa are faring compared to other regions in the world, East Africa remains at the top¹⁸ with 16% of blended capital mobilized followed by West Africa (13%), Southern Africa (10%), Central Africa (8%) and North Africa (7%) which cumulatively constitute about 54% of the global blended capital (Figure 11). Other sub-regions outside Africa are trailing behind East Africa, West Africa and Southern African regions with blended capital mobilized at less than 10% per sub-region.

¹⁶ <http://blogs.worldbank.org/ppps/infrastructure-africa-s-development-ppp-imperative>

¹⁷ file:///C:/Users/admin/Documents/IDBZ/IDBZ%20Study/Drafts/African_Economic_Outlook_2018_-_EN_Chapter3.pdf

¹⁸ Efforts within this region to drive intra and inter regional trade through the development of regional transportation projects to create sustainable economic have resulted in bankable projects that are attracting institutional investors looking for infrastructure assets. Countries within the region are also embarking on innovative infrastructure projects. For example Proparco arranged a €40 million financing to SCOUT, Uganda's third largest sugar manufacturing company, to finance a new 26MW cogeneration power plant (see AfIDA Newsletter June-August 2018).

AfDB (2018) figures agree with Convergences 2018 that 42% of global blended finance went to Sub-Saharan Africa. This is because of the appetite for infrastructure financing in the region. In this regard AfDB sees the need to negotiate bigger deal sizes since most deals negotiated for Sub-Saharan Africa are relatively small compared to other regions. The same view was expressed by the United Nations Capital Development Fund (UNCDF) (2016) which argued that 77% of private finance mobilized for Less Developed Countries went to Sub-Saharan Africa, 22% to Asia (mostly South and Central), and 1% to Central America (Haiti). Top three countries that benefited in 2012–2015 are Angola which benefited with over US\$1 billion followed by Senegal and Zambia which benefited with over US\$500 million each. In addition, Liberia, Djibouti, São Tomé and Príncipe, Guinea-Bissau, and The Gambia are other African countries that mobilized less than US\$10 million. Angola was mainly supported by guarantees from both multilateral and bilateral organizations since it managed to mobilise large per-deal amounts of over US\$100 million on average in sectors such as water management, metal industries, information and communication technology and telecommunications, trade and financial services. Mauritania, Malawi, Zambia and Mozambique mobilized more than US\$10 million per operation. Guinea-Bissau and Gambia, on the other hand, registered the lowest mobilization per transaction, at less than US\$1 million. Generally, the lower mobilization of blended finance in Africa may reflect the smaller size of private-sector transactions in Africa and/or the higher use of concessional finance per transaction. The enormous focus on Sub-Saharan Africa reflects the significant infrastructure needs of the continent and reflects the limitations of African markets to attract and support large-scale blended finance deals.

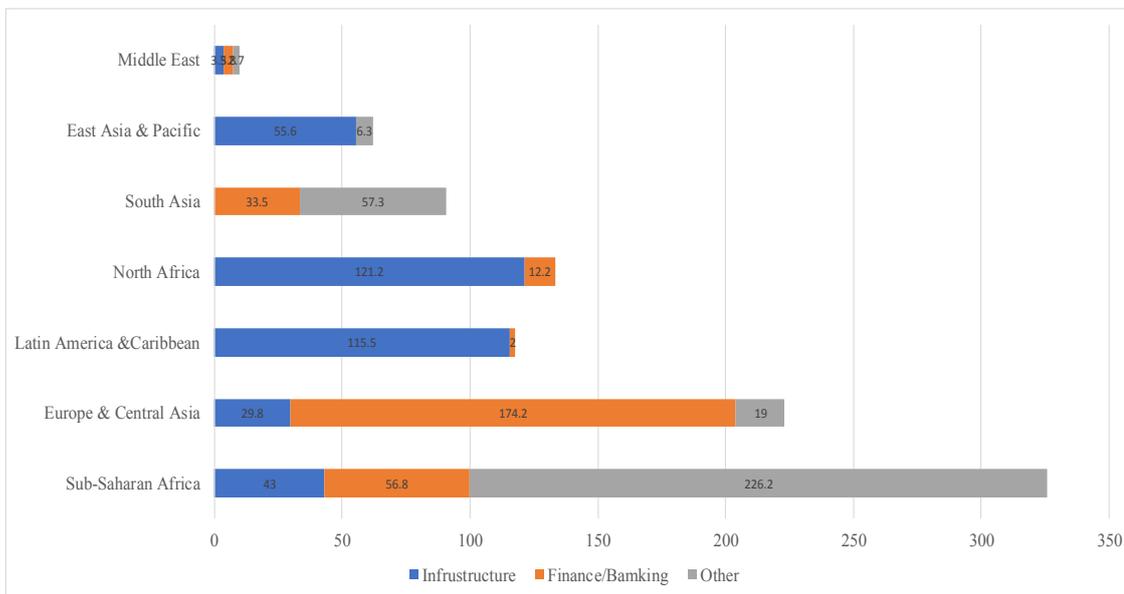
Blue Orchard (2018) reports a much lower figure compared to AfDB and UNCDF of 16% of total capital mobilized by blended finance by Sub-Saharan Africa compared to 62% for projects that have a global focus, 7% for Middle East and North Africa, 5% for Latin America, 4% each for Europe & Central Asia and East Asia & Pacific and 3% for South Asia.

The differing statistics by source notwithstanding, it has generally, been noted that middle income countries are most commonly the target recipient of blended finance deal flows, followed by low income countries (Convergence, 2018). Upper middle-income countries constitute 24% of total deals with a higher average deal size of US\$262 million. Lower middle-income countries and low-income countries constitute 48% and 26% against the deal size of US\$145 million and US\$123 million, respectively. A look at the top beneficiaries of blended finance globally reveals that the top countries for blended finance deals are Kenya (14%), India (13%), Tanzania (11%), Uganda (11%), Nigeria (8%), Ghana (8%), Rwanda (8%), Mexico (8%) and South Africa (6%). Of these nine countries seven are Sub-Saharan African countries. Tanzania, Uganda and Rwanda are the low-income countries whereas Kenya, Nigeria and Ghana are lower middle-income countries together with South Africa as the only upper middle-income country receiving blended finance deals in Sub-Saharan Africa.

A focus on the sectors that are related to IDBZ's focus areas reveals that energy, non-energy infrastructure and housing & real estate constitute 24%, 9% and 1% of the deals with an average deals size of US\$374 million, US\$215 million and US\$290 million, respectively. A breakdown of the energy sector reveals that renewable energy constituted a larger chunk at 62% compared to 16% for non-renewable, off-grid (17%) and other (13%). Among the non-energy infrastructure, telecommunication constituted a larger chunk at 41%, followed by water (31%), transport (28%), and other (10%). The median deal size for non-energy infrastructure deals (US\$52 million) is considerably smaller compared to the energy sector at US\$90 million. Other sectors such as financial services, agriculture and health garnered 29%, 10% and 5% of the deals with the average deal size of US\$399 million, US\$105 million and US\$1.015 billion, respectively. This may imply that as Zimbabwe targets to become an upper middle-income country by 2030, it can be a good indicator to help lure investors in infrastructure through blending since this is more prominent in middle income countries in Sub-Saharan Africa

Concessional financing which goes towards infrastructure as a proportion of total concessional financing in each region reveals that Sub-Saharan Africa received only 13.2% as compared to 98.3% for Latin America and Caribbean, 91% for North Africa and 89.8% for East Asia and Pacific. Sub-Saharan Africa's share of concessional financing for infrastructure is behind that of finance and banking (17.4%) by about 4.2 percentage points, at a time when the region has infrastructure deficits.

Figure 11: A comparison of Sub-Sharan Africa's Concessional Financing and Other regions by Target Sectors



Source: DFI Working Group on Blended Concessional Finance Projects, 2018

The DFI Working Group on Blended Concessional Finance (2018) observed that concessional finance was generally used to de-risk pioneering projects in high risk countries and/or projects with new technologies or those addressing under-served segments in society. For instance, reference was made to the solar projects in Mozambique and Egypt and housing finance development in West Africa. Some of the DFIs which have implemented blended projects in Africa include the African Development Bank, Islamic Corporation for the Development of Private Sector (ICD) and the International Finance Corporation. The African Development Bank financed Egypt’s Solar Photovoltaic Power Project under the Egyptian Feed-in-Tariff Program.

Egypt has developed an overarching regulatory framework for the development of renewable energy capacity with the aim of securing 20% of its energy generation from renewable sources by 2022. The Government of Egypt (GoE), in September 2014, launched a Feed-in-Tariff (FiT) Program to implement 2,300 MW of Solar PV projects. The Shapoorji Pallonji Project involves the design, construction and operation of a 50 MW solar PV power project to be implemented under the FiT Program Round-2. The AfDB is providing a senior loan of USD 12 million. It has also arranged an additional concessional loan of USD 7 million from the Global Environment Facility (GEF). The motive is to promote the scaling up of renewable energy technologies and contribute to the delivery of universal power supply in Africa.

Another project in Egypt, the Scatec Solar Project was financed by Islamic Corporation for the Development of The Private Sector (ICD). The main objective of ICD in providing blended concessional finance was to help de-risk the project, to provide a contribution to the renewable energy development and carbon reduction agenda of the Government of Egypt. The ICD provided long term concessional debt to the project at an amount of US\$30 million. This was meant to diversify Egypt’s energy mix and support for expanding Egypt’s renewable energy generating capacity in light of heavy reliance on imported fossil fuel-generated energy.

The International Finance Corporation (IFC) also provided financing to CRRH, a mortgage financing company serving eight countries in the West African Economic and Monetary Union on housing finance in West Africa. It utilized concessional funds from the IDA Private Sector Window to reduce project risks associated with providing local currency financing. Another project funded by IFC in Africa is the Mocuba Solar project in Mozambique. IFC provided a debt financing package of US\$55 million to build Mozambique’s first utility-scale solar photovoltaic plant. The package included US\$19 million of concessional financing from the Climate Investment Fund and a syndicated loan of up to US\$17 million from the Emerging Africa Infrastructure Fund. Equity of US\$14 million was provided by Scatec Solar, Norfund, and Mozambique’s electricity utility Electricidade de Moçambique (EDM). The project expected to receive a US\$7 million Viability Gap Funding grant from the Technical Assistance Fund of the Private Infrastructure Development Group (PIDG), a multi-donor funded institution that encourages private investment in infrastructure in emerging markets.

However, AfIDA (2018) observed that lack of execution on deals and absence of sufficient early stage capital are some of the hurdles in implementing blended finance.¹⁹ It further noted that there is need to provide technical assistance and training to capacitate both the public and private sector to enhance smooth execution of blended finance. Given that most infrastructure projects in Zimbabwe are not developed to bankability, blended finance can be used to develop the projects especially at the pre-design stage where most projects

¹⁹ The lack of access to third-party financing causes an ‘Early-Stage Financing Gap’ which has become a critical market failure in most developing economies – one that the private sector has been unable to resolve on its own. Thus, improving access to ODA and philanthropic sources of funding can assist in closing the early stage financing gap (see United Nations Environment Programme. 2011 study on catalyzing early stage investment on mobilizing early stage capital to crowd in private sector funding, available at: https://www.scaf-energy.org/sites/default/files/public/downloads/files/Catalysing_Early_Stage_Investment.pdf)

fail to attract financing due to the high-risk nature of the project at the early stages of the project. The focus of blended finance can be on renewable energy. IDBZ can take a cue from these projects which used blended finance to crowd in private sector funding even in difficult setting like Zimbabwe. Housing projects and renewable energy like solar projects can be used as target areas since they have already attracted financiers in Africa.

Generally, blended finance is considered as the second highest potential source of development finance after foreign direct investment (FDI) followed by tax collection, official development assistance (ODA), remittances, trade finance, South-South cooperation and philanthropic activities (Convergence, 2017). Thus, Sub-Saharan African countries including Zimbabwe need to focus more on mobilizing blended finance which include concessional financing for infrastructure development. This should be preceded by or accompanied by initiatives to reduce debt exposure; improving the doing business environment and the regulatory framework.

3.1. Trends in Issuance of Infrastructure Bonds in Africa

In recent years, some African countries such as Kenya, Cameroon, Chad, and South Africa have issued infrastructure bonds. However, strictly speaking, if we consider the definition of an infrastructure bond *per se*, most of those bonds except for some South African ones were not infrastructure bonds but general government bonds with some promise to spend the money in infrastructure investment (Mezui, 2013). There was also no guarantee that the money raised went into the infrastructure projects as promised, and neither was there a dedicated Fund Manager. Lack of dedicated Fund Manager, have raised concerns about the ability of central government to channel the funds to actual development of infrastructure projects and have dampened investor confidence as well as lowering the credibility of government. Creating a credible and viable infrastructure bond market will assist in mobilizing blended infrastructure finance.

South Africa has a large and sophisticated investor base totalling US\$600 bn (more than the other countries combined), and stands out on the continent in terms of local market liquidity, capital market development and experience with project finance (Ibid). For example, Eskom, an integrated power utility wholly owned by the government has a track record of issuing bonds locally in Rand as well as internationally in Euro and Dollars. In 2016 South Africa had ZAR 105 bn outstanding in the market, with 2033 as the longest maturity date. Similarly, the South African National Roads Agency (SANRAL) has a domestic capital markets program totalling ZAR 44 bn. In 2008 it issued four bonds totalling ZAR 2 bn to fund new tolled highways in Gauteng as well as other road upgrades. This included inflation-linked floating-rate bonds and three fixed rate bonds with maturities up to 20 years. It was the first time SANRAL issued bonds without a guarantee from the National Treasury. Also, the Airport Company of South Africa (ACSA) rolled out a ZAR 1bn three month commercial paper program in 2008-09, which it subsequently refinanced using long-term bonds.

Beyond Africa, other emerging economies such as Chile, Brazil and Malaysia are using project finance bonds as a way to catalyze investor interest in infrastructure project. Such examples can serve as a template for African countries including Zimbabwe on how to develop their own bond markets. Pension funds can play a significant role in financing infrastructure directly and via the capital markets. In this regard there is need to create a conducive environment firstly to grow the asset base of pension funds and insurance companies (life offices) which will then be leveraged on when mobilizing blended infrastructure finance. Institutional investors can use their asset base to participate in infrastructure projects through subscribing to issued infrastructure bonds or take-up equity in infrastructure projects.

In South Africa the Government Employees Pension Fund (GEPF) is valued at \$133.4 billion) has the largest funds in Africa. Furthermore, the Public Investment Corporation (PIC), which is the investment wing of the GEPF is valued at Rand 2.083 trillion and invests in bonds across the continent. Thus, African Pension Funds can be leveraged on to mobilize blended infrastructure finance.

3.2. Development of Pipeline of Bankable Projects

In the African context, another area where more progress is required in all markets is the provision of adequate public funds to facilitate the development of a pipeline of bankable projects for consideration in mobilising blended finance for infrastructure development. South Africa is one country in the region that has a consistent deal-flow of blended infrastructure projects. However, capacity to develop bankable infrastructure projects; evaluate, approve and regulate blended finance infrastructure projects in most countries in the Africa is still weak. The Global Infrastructure Facility (GIF), the IFC and World Bank are providing assistance to countries in pipeline project development. The GIF is committed to a market-changing scope of 200 projects over the next five years (Jordan Schwartz, 2018)²⁰

Potential infrastructure projects in Africa have remained on the drawing board for too long due to a variety of reasons including lack of funds for the development phase, high risk perceptions²¹, and lack of political support among other factors. For example, development of a hydropower scheme on the Zambezi River downstream of Victoria Falls has been investigated in various degrees of detail since 1904, when geological investigations for potential sites commenced. Since 1972, three more phases of site/geological investigations have been undertaken at the preferred Batoka Gorge site (12 km upstream of that defined in 1972). These investigations were conducted in 1981/82, 1983 and 1989 respectively, in order to supplement information acquired during previous studies. Following these studies, in 1992 the Zambezi River Authority (ZRA) commissioned the Batoka Gorge Joint Venture Consultants (BJVC) to carry out a feasibility study for the proposed Batoka Gorge Hydropower scheme. An Environmental and Social Impact Assessment (ESIA) for this proposed scheme was also undertaken as part of this feasibility study, and to address gaps identified in this 1993 ESIA, further environmental

²⁰ <http://blogs.worldbank.org/ppps/subtle-significant-changes-private-infrastructure-investment-first-half-2018>

²¹ Blending is one strategy meant to de-risk the infrastructure projects.

and social studies were undertaken in 1998. In 2014, the ZRA initiated some further studies on the proposed Batoka Gorge Hydro Electric Scheme (BGHES) to update the Engineering Feasibility Studies, to update and carry out an Environmental and Social Impact Assessment (ESIA), and engaged Transaction Advisors to advise on the financial and commercial aspects of the project²²

The long gestation period in project development is not consistent with the urgent need to address infrastructure deficits on the continent. This may reflect the inhibiting financial constraints faced by African Governments to mobilise public resources to meet project development cost including feasibility studies. In this regard attention should be focused on mobilising blended infrastructure finance. Furthermore, policy, legislative and regulatory reforms are needed to facilitate increased participation of the private sector particularly institutional investors in financing infrastructure development in Africa.

3.3. Lessons Learnt

Key lessons emerging from the analysis in this section include the following:

1. African countries are exploring opportunities for blending public and private sector funding to address the infrastructure deficits given that one of the key factors retarding industrialization in Africa has been identified as insufficient stock of productive infrastructure in power, water, and transport services.
2. There are distinct sectorial preferences by private investors in blended finance infrastructure projects.
3. It has emerged that middle income countries are the target recipient of blended finance deal flows;
4. Creating a credible and viable infrastructure bond market is a critical success factor in mobilizing blended infrastructure finance.
5. Need to leverage on resources under management of African Pension Funds in mobilizing blended infrastructure finance.
6. Concessional finance was generally used to de-risk pioneering projects in high risk countries and/or projects with new technologies or those addressing under-served segments in society.
7. Need for adequate public/concessional funds to facilitate the development of a pipeline of bankable projects for consideration in mobilising blended finance for infrastructure development.
8. Potential infrastructure projects in Africa have remained on the drawing board for too long due to a variety of reasons including lack funds for the development phase, high risk perceptions, and lack of political support among other factors.

²² file:///C:/Users/admin/Documents/IDBZ/IDBZ%20Study/Drafts/BGHES_Project%20Overview%20Document.pdf

Chapter 4: Zimbabwean Experience in blending both public and private interest-bearing instruments to finance infrastructure projects

This chapter provides a brief review of blended financing experiences in infrastructure in selected sectors in Zimbabwe. It highlights some major projects undertaken in the country and the modalities through which they were funded and managed. Some of the challenges arising are also discussed.

4.1. Power Projects

Hwange, Bulawayo, Munyati, Harare and Kariba power stations²³ are the major power infrastructure in the country. The financing of Kariba and Hwange power stations are examples of blending in Zimbabwe. Kariba power station was financed through external and domestic debt (see Figure 24 in Annex L3). External debt, which contributed about 59% of the total debt for the project, was in the form of ODA from International Bank for Reconstruction and Development (IBRD), Colonial Development Bank (CDC), and Commonwealth Development Finance Corporation (CDFC) (International Bank for Reconstruction and Development, 1956). Internal debt contributed about 41% of the total debt for the project, and was raised from copper mining companies²⁴, banks, the British South African Company and Federal Government of Rhodesia and Nyasaland. Of the total project debt, 35.4% came from the private sector as loans. Copper mining companies made a significant contribution (25.3%) to the total project debt because they were the biggest consumers of electricity (International Bank for Reconstruction and Development, 1956) and hence they benefited most from the project. This implies that the private sector companies that stand to benefit a lot from a project may be more willing to contribute towards the development of the project using their own balance sheets (corporate finance).

The structure of the financing arrangement of the Kariba Hydro Electric Project catalysed the participation of the private sector in a number of ways. First, the Federal Government borrowed internal loans on behalf of the Federal Power Board which was the owner of the project. This enabled the project to access loans from the market at favourable rates that the Federal Power Board would otherwise not have accessed on its own. Second, the Federal Government agreed that its loan to the Federal Power Board may not be serviced if the latter is unable to service loans from other lenders. Therefore the Federal Government's loan to the Power Board was subordinated to all the other loans, implying that it was the first to absorb any loss from the project. Third, by borrowing internally on behalf of the Federal Power Board, the Federal Government implicitly guaranteed the internal loans, hence assuring the private lenders of getting back their money. Fourth, the Federal Government bridged the gap between the project requirements and the resources of the copper mining companies which partly financed the Kariba Hydroelectric Project. The Federal Government borrowed from the copper mining companies the loans which were supposed to begin servicing within a year, and then on-lent them to the Federal Power Board on the same terms but deferring the inception of loan servicing by 5 years.

However, the Kariba Hydroelectric Project had weak blending in the sense that private sector debt was subordinated to the ODA finance.

²³ Details of this project will be provided under the case studies.

²⁴ This remains another important source of infrastructure funding. For example, heavy users of infrastructure (road, energy and water), the Bank can consider projects structured around these.

This implies that ODA did not play a key role in catalysing private investment. Only the Federal Government played a significant role in crowding in private investment into the project.

The Hwange Power I Project was financed through ODA, private sector funding and internal revenue generation (see Figure 25, Annex L4). ODA which constituted 31.7% of project cost was raised from IBRD, CDC, EIB and UK Government (World Bank, 1982). The private sector contributed at least 39.9% to total project cost through credit finance from manufacturers/suppliers and loans from a syndicate of banks, while internal borrowing and cash generation contributed 28.4%. In the Hwange Power I Project, ODA played a critical role in blending. It financed the cost of training and technical assistance for the project in order to avert the risk of delayed project completion due to shortage of the necessary skills locally. It also financed the electricity tariff and energy pricing studies which were intended to encourage the use of least cost energy. ODA also covered the cost of interest during construction (IDC) because of the time lag in building up revenues from the project and the impossibility of raising electricity tariffs to meet the required IDC expenses which amounted to US\$188 million. Thus, the providers of ODA agreed to include IDC in the loan amount. On the other hand, the Government of Zimbabwe provided guarantees for all the loans extended to the Electricity Sector Commission for the project. The government also exempted the project from paying duty on all the imported materials and equipment for the project.

Generally, there has not been much blending of private and public interest bearing instruments in the energy sector. Most of the projects have been financed through official development assistance (ODA) funds and/or private sector funds without necessarily blending the two. For example, IDBZ raised from the local private market US\$38.8 million as a condition precedent to the unlocking of a US\$535 million loan from China Exim Bank for the refurbishment of the 300-megawatt (MW) Kariba South hydroelectric power station units 7 and 8. Whereas blending requires that public funds (in this case the China Exim Bank loan) catalyse the crowding in of private funds, this example was actually the opposite whereby private funds were needed to unlock public funding. In a number of cases the IDBZ has also raised private funds through bond issuance to finance energy projects (see Table 7). Apart from IDBZ bonds that have been used to finance energy infrastructure projects, the government has also been licensing independent power producers (IPPs) as a way of crowding in private investments into the energy sector.

Table 7: Bonds issued by IDBZ to support energy sector, 2012 to 2018

Name of Bond/Bills	Date issued	Tenor	Coupon (per annum)	Size of issue (millions)	Amount Raised (millions)
Infrastructure Bond - Financing Pre-paid metering project	2012-2013	3 years	10%	US\$30	US\$17.8 (public issue) US\$12.2 (private placements) - investors were fully paid
Infrastructure Development Bond Issue – 20 November 2014- Financing Pre-paid metering project	20 November 2014	5 years- Semi- annually	8%	US\$15	US\$15
Infrastructure Development Bond Issue – 20 November 2014- Financing Kariba South – US\$38.8 Million and Harare Power Station – US\$11.2 million	20 November 2014	5 years- Semi- annually	8%	US\$50	US\$50

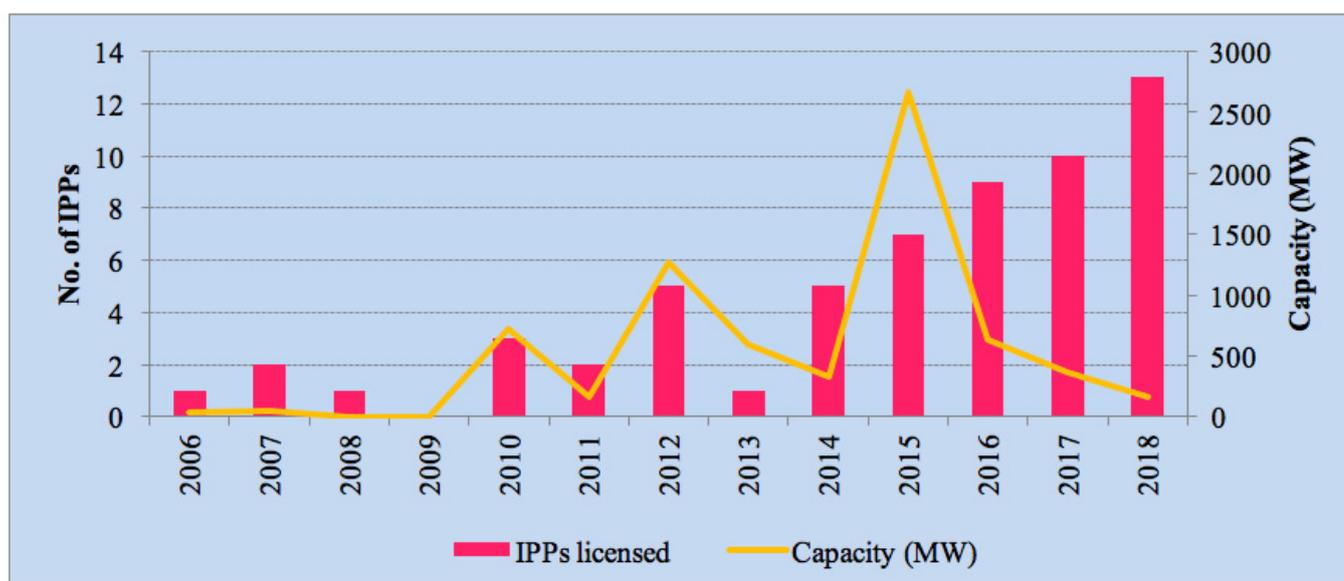
Source: IDBZ website

The energy deficit in the country and the limited blending in the energy sector indicate that there is potential for increased blending. About 1200MW of electricity is produced in the country against a demand of 2029MW (Mzezewa and Murove, 2017). The shortfall is partially offset by imports from Hydro Cabora Basa (about 50MW) and Eskom which provides between 50MW and 320MW (Mudzingwa, 2016). The lower national electrification rate of 40% (Ministry of Energy and Power Development, 2017) implies that the potential demand for electricity is way above the estimated 2029MW.

The high interest shown by the private sector through IPPs in the energy sector is a testimony to the interest and potential of private sector funding that can be leveraged for blending. The annual number of IPPs that have been licensed by ZERA has been growing, from 1 in 2006 to 13 in 2018, making a cumulative total of 59 IPPs that have been licensed over the period (Figure 12). The cumulative total of planned electricity generation capacity over the same period is around 6983.35MW, which is way above local demand and can be exported. The spike in planned generation capacity in 2015 resulted from several individual projects that had relatively large generation capacity compared to the other projects which were licensed in other years.

However, there is need to institute mechanisms to ensure that those granted IPP licences expedite implementation and ensure the planned electricity generation is realised. Zimbabwe is strategically located at the heart of the Southern African Power Pool such that increased electricity generating capacity will make the country a power hub that can competitively export power into the entire Southern Africa region.

Figure 12: IPPs that have been licensed and their electricity generation capacity, 2006 to 2018



Source: ZERA Database, 31 December 2018

However, there are several issues that adversely affect the viability of power projects, and hence the interest of private sector funding of energy projects in Zimbabwe. For hydro and thermal electricity projects, the tariffs for non-consumptive water use are relatively high in Zimbabwe. For instance, for a hydroelectricity project on infrastructure developed by the power producer, ZINWA gets a royalty which is 14 times greater than a tariff charged by the Department of Water Affairs and Forestry in South Africa (Chikwanda, 2015). This increases project costs, reduces returns and impacts negatively on the attractiveness of Zimbabwean energy projects. Thus, the tariffs need to be reviewed to ensure that they are competitive and encourage investment.

The costs for environmental impact assessment (EIA) are prohibitive (Nyangani Renewable Energy, 2015). In addition, they are paid upfront for the issue of an EIA certificate. This increases project development costs and reduces potential returns for investors. In this case, ODA may come in to issue grants for EIAs to lower project costs and improve the risk-return profile for private commercial investors and lenders.

The off-taker credit risk is high in Zimbabwe (Nyangani Renewable Energy, 2015). The lenders of power projects require that the electricity generated by the project should be paid for on time so that the project can be able to make timely loan repayments. However, ZETDC which is the only off-taker for electricity projects is not perceived as credit worthy by potential investors. This increases the premium on equity and debt financing, thereby reducing the overall attractiveness of power projects in the country. Nevertheless, this risk can be dealt with sustainably by improving the credit worthiness of ZETDC, for example, through credit enhancements and also being rated by credit rating agencies.

Medium to long term bank finance is either internally unobtainable or excessively costly. This necessitates private sector players to borrow offshore where rates are generally competitive. However, these competitive rates tend to exceed the rates stipulated by the Reserve Bank of Zimbabwe External Loans Coordinating Committee (ELCC) guidelines (Nyangani Renewable Energy, 2015).

The tariffs at which ZETDC sells electricity to the end users are not fully cost reflective as indicated by very high subsidies. In 2015, the post-tax subsidy for electricity was 20.5% of GDP in Zimbabwe (against 2.6% Sub Saharan Africa average), implying a per capita post-tax subsidy of US\$219.65 against an average of US\$41.91 in sub Saharan Africa (IMF, 2015).²⁵ Therefore electricity projects, due to their high capital nature and perceived high country risk, they face a huge challenge in agreeing with ZETDC on applicable tariffs that IPPs can sell their electricity to ZETDC and get good returns. This challenge has resulted in some private power generation projects stalling, failing to reach financial closure and eventually losing power generation licenses.

VAT registration is very difficult to obtain from ZIMRA. As a result power projects end up being burdened by VAT payments for the period prior registration leading to higher tariffs to electricity customers. VAT refunds take longer whereas VAT collection is done immediately (Nyangani Renewable Energy, 2015). This adversely affects the cash flows of power projects.

Despite these challenges, there are a number of specific opportunities for blending public including ODA funds and the private sector funds in the energy sector to facilitate the construction of new power generation plants and rehabilitating the existing ones (see Table 8).

²⁵ A post-tax subsidy arise when consumer prices are below supply cost plus a tax to reflect environmental damage and an additional tax applied to all consumption goods to raise government revenues.

Table 8: Opportunities in new generation power plants and rehabilitation of existing ones

OTHER ZPC PROJECTS (NEW GENERATION PLANTS)				
Project	Start Date	End Date	Milestones Reached	Challenges
Munyati Solar Project (100MW)	2021	2022	<ul style="list-style-type: none"> EPC Contract in place and feasibility report finalised. EIA studies were done and draft is available. 	Sourcing of funding.
Insukamini Solar Project (100MW)	2021	2022	<ul style="list-style-type: none"> EPC Contract in place and feasibility studies were completed. Engagements with ZIMTA, owners of the prospective land, are ongoing. 	Sourcing of funding.
Peaking/ Emergency Power Plant (120MW)	2018	2019	<ul style="list-style-type: none"> EPC Contract is in place. Initial activities and ESIA studies were done. Planning permission was granted. 	Sourcing of funding.
Coal Bed Methane (300MW)	TBA	TBA	<ul style="list-style-type: none"> ZPC awaits the gas suppliers to do comprehensive exploration studies for power feasibility studies to proceed. 	Exploration studies are yet to take place.
Tokwe Mukosi (15MW)	TBA	TBA	<ul style="list-style-type: none"> Project was being developed as part of the dam construction process by ZINWA. Ministry of Energy and Power Development requested ZPC to take over the power plant project from ZINWA. 	Engagements are still underway to facilitate project takeover by ZPC and subsequent developmental steps.
Munyati Repowering (100MW)	2019	2020	<ul style="list-style-type: none"> EPC Contract negotiations were completed and the draft contract initialled. 	<ul style="list-style-type: none"> Sourcing of funding.
Bulawayo Repowering (100MW)	2017	2019	<ul style="list-style-type: none"> Loan agreement for senior debt was signed. Bids were submitted to pre-qualified bidders and site visit was done. Environmental clearance was secured from EMA. Secured water supply agreement. 	<ul style="list-style-type: none"> The USD87 million secured for the project may be inadequate to cover the EPC cost.

Source: Zimbabwe Power Company, 2018

4.2. Water

4.2.1 Dam and Irrigation Projects

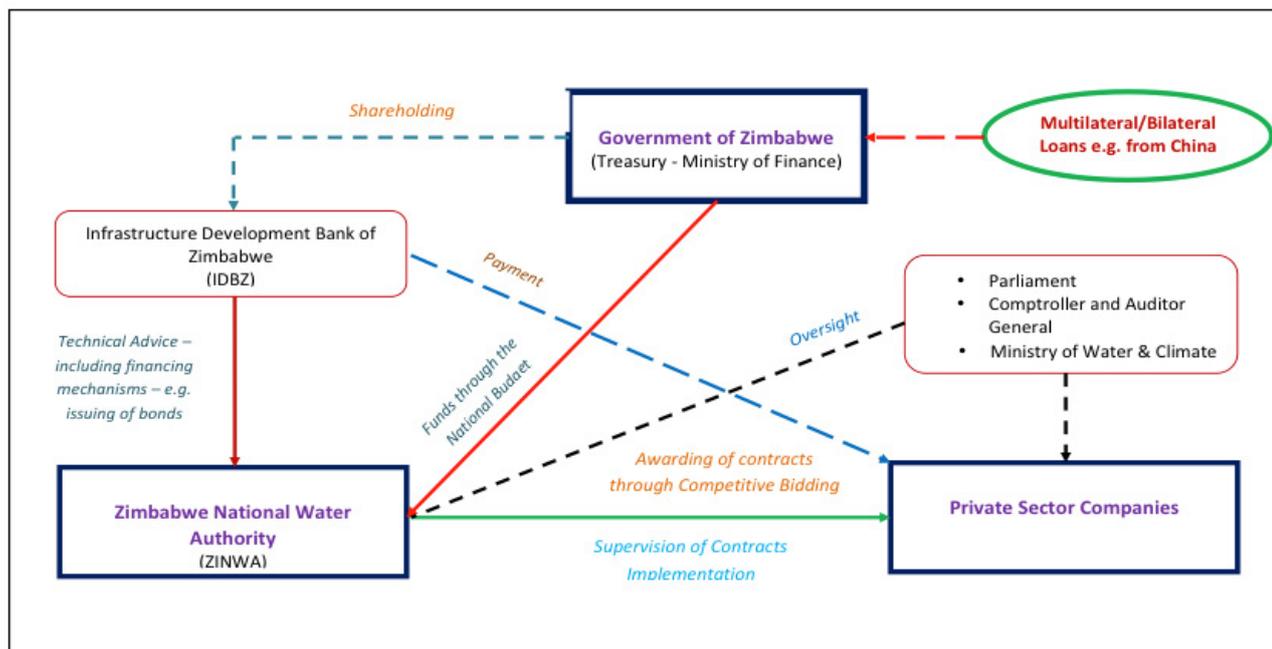
There are several irrigation projects in Zimbabwe but the irrigation of sugar in the low veld stand out as a success story. In the 1940s Mr. McDougall started the Triangle Sugar Estate Company which focused on sugar cane production under irrigation as a private player. The project was taken over by government (after failing to make profit) through the Sugar Industry Act of 22nd December 1944. Government which was convinced of the viability of the project invested public funds into the project which soon made profits in 1954. As the company began making profits it became attractive to private investors and subsequently Triangle was purchased by a syndicate of Natal farmers and has since operated as a private sector initiative. The construction of dams and irrigation canals by government improved the viability of producing sugar cane in the arid low veld.

While the implementation of this Triangle Sugar Estate Project may not be classified as a blended financing project, the investment of public funds in a failed private sector project and selling it when it was viable demonstrate the potential for blended financing in the development of irrigation projects. Similar opportunities for developing thriving sugarcane plantations are available in Muzarabani and Mbire districts along the Zambezi valley that share the same climatic conditions of the low veld. IDBZ may want to look closely at these proposed projects which have capacity to generate revenue streams to repay loans. Figure 3 below shows a funding structure for dam construction and water supply projects that can be adopted in the mobilisation of blended financing.

Under this funding structure Government has delegated the supervision and awarding of contracts as well as making of payments to Zimbabwe National Water Authority (ZINWA). ZINWA supervises the competitive bidding process by private sector service providers who then are contracted to provide the construction services and materials. The Government provides the funding for the water projects

through the national budget allocations as specified under the Public Sector Investment Programme (PSIP). Funds can also be raised on the open market through the issuance of bonds by the IDBZ or a designated institution which acts as a technical and financial advisor to both ZINWA and the Government on water infrastructure development and financing. Some of the funds also come through the treasury as part of loans negotiated by the Government from multilateral and bilateral arrangements. The Comptroller and Auditor General, Ministry of Water and Climate and Parliament provide oversight in the implementation of the water projects.

Figure 13: Funding Structure for Dam Construction and Water Supply Projects in Zimbabwe



Source: ZEPARU

Dam construction has been predominantly funded through the PSIP with funds raised locally or through government loans. In the construction of these dams ZINWA is the contracting, management and supervisory authority. Prior to 2000 dams in commercial farming areas were funded through private funding raised by individual or a consortium of farmers in the farming areas. The loans were repaid from general farming proceeds. However, unresolved issues of land title militate against private sector participation in the construction of dams and ancillary irrigation infrastructure. Increasing agricultural productivity requires increased investments in water harvesting and irrigation infrastructure.

Interviews with players also revealed that the development of dams and irrigation facilities has also benefited from a number of development partner support, including the World Bank, UNICEF, AfDB and GIZ. The support provided by donors includes technical assistance in the form of feasibility studies and contracting. There is scope for IDBZ to work with the local authorities with bankable project proposals to mobilise funds from the private sector. These opportunities are likely to increase with the implementation of Devolution that is being prioritised by Government.

Furthermore, IDBZ can also leverage on the PSIP resources that they disbursed to specific water projects by mobilising addition resources for the same cause. IDBZ has been mandated to fundraise for the Victoria Falls municipality water augmentation project under Victoria Falls municipality which involves rehabilitation of water facilities estimated at US\$12 million. Such cases also create opportunities for IDBZ to explore options for blended financing. To facilitate completion of ongoing dam projects, IDBZ issued a water bond to fund commercially viable water sector projects and rehabilitation of the pumping and distribution infrastructure on behalf of ZINWA. The capacity of IDBZ to mobilise similar funds and effectively use the issuing of bonds to tap into private sector financing requires government to put in place measures to deepen the Bond market. This will further enhance IDBZ's initiatives to develop models for the financing of 10 water sector national priority projects through private sector participation. The projects include the following:

- Epping Forest (Nyamandlovu Aquifer) - Bulawayo;
- Chivu Water Supply Project - Chivhu and Mashonaland East;
- Muda Nyatsime Dam - Chitungwiza and Harare;
- National Matabeleland Zambezi Water Project - Matabeleland and Bulawayo;
- Kunzvi- Musami Dam - Harare;
- Kondo Dam- Save River - Odzi;
- Kudu Dam - Kadoma, Sanyati;
- Nyatana Dam - Mutoko;
- Lubongo Dam - Gweru- Shurugwi; and
- Bindura Dam - Bindura and Mashonaland Central.

Another area where there are considerations for private sector participation in joint venture arrangements with the local authorities is in the provision of water meters. According to key informants, there are proposals in the Gweru City Council (GCC) and Bulawayo City Council (BCC) to bring in the private sector to invest in the supply and installation of the water meters and recoup their investments from revenue streams over time through joint venture arrangements with the local authorities.

4.2.2 Water and Sanitation Infrastructure

Water and sanitation infrastructure projects have been established and funded by Government, local authorities, the private sector and donors. The thrust and nature of the intervention including funding structures have largely been dictated by the immediate objectives in the provision of the water and sanitation infrastructure. In circumstances where the immediate objective has been developmental, government sometimes in partnership with the private sector has largely been at the forefront. In cases where the overriding need has been humanitarian, for example, to deal with specific health issues like dealing with disease outbreaks, government in partnership with development partners/donors has been on the forefront. Support provided by UNICEF to the 12 Small Towns²⁶ in response to the 2008/2009s cholera outbreak is a good example of this type of intervention. This programme included repair, rehabilitation and upgrading of water supply and similar infrastructure. There were opportunities in these donor funded programmes which the IDBZ could have leveraged on as blended concessional finance to mobilise private sector financing.

Donors have also pooled funds to establish Multi-Donor Trust Funds to support provision of infrastructure in response to the economic crisis in Zimbabwe which was characterised by hyperinflation, underperformance of the economy and constrained fiscal space. Multi Donor Trust Funds which focused on infrastructure rehabilitation and development include the Zimbabwe Multi Donor Trust Fund (ZimFund)²⁷ established in 2010 and managed by the African Development Bank and the Zimbabwe Reconstruction Fund (ZIMREF)²⁸ established in 2014 and managed by the World Bank.

The formation of these Multi-Donor Trust Funds demonstrates a source of concessional funding that can be leveraged on to mobilise blended finance for infrastructure projects in Zimbabwe. The model of pooling donor funds within the context of ZIMFUND and ZIMREF can be replicated to create a fund to crowd in funds from the DFIs, Private Sector, Public Sector to mobilise more funds for infrastructure development. Furthermore, infrastructure components funded through donor funds can be leveraged upon in future expansion of water and sanitation infrastructure in the assisted local authorities as well as the expansion power production at Hwange. These projects highlight potential of structuring blended financing projects where donor funding can be used in the project development phase to reduce project risks, improve project viability and make infrastructure projects attractive for private capital. Similar projects in future could be developed by blending donor funding with private capital.

Access to long term infrastructure loans by the local authorities to develop water and sanitation infrastructure has been severely restricted due to their inability to get borrowing powers from the Government. This has been necessitated by the constrained fiscal space at central government level, mismanagement, poor governance, lack of transparency and accountability by local authorities. Some local authorities have been failing to produce audited financial statements and account for money provided by government or other agencies like ZINARA. This could be a reflection of both human skills and systems capacity challenges within the local authorities. Consequently, the local authorities have not been able to obtain Government guarantees to access foreign loans and domestic loans (e.g. through issuance of infrastructure bonds). The inability of government to give guarantees to local authorities undermines their capacity to mobilise blended finance where the private partners require such guarantees.

4.3. Transport Infrastructure

The transport sector in Zimbabwe comprises five modes, namely, road, rail, aviation, inland water and pipeline transport. The road network excluding urban roads totals 76, 241km of which 9, 256km or 12.1% are bitumen surfaced (AfDB, 2013)²⁹. The Zimbabwe National Roads Administration (ZINARA), is responsible for managing the Road Fund and disbursing to the following road authorities: Department of Roads in the Ministry of Transport and Infrastructure Development, responsible for trunk roads; Rural District Councils (RDCs) and Urban Councils (UCs), and District Development Fund, responsible for urban and rural roads respectively. Historically, financing of road infrastructure, has mostly been through fiscal budgetary allocations to the different road authorities. There are immense demands from residents for maintenance, rehabilitation and expansion of road infrastructure in the 33 UCs and the 60 RDCs to address infrastructure deficits within these local authorities.

Transport infrastructure is a critical enabler for economic growth and transformation, hence the need by government to facilitate construction and/or rehabilitation of roads, airports, rail, inland waterways and pipeline transport systems. As the country opens up for business, it requires adequate and viable transport infrastructure stock that seamlessly links cities and towns, connecting people with economic opportunities and tourist attractions; connecting businesses with markets both local and regional markets. Modernising the country's infrastructure and leveraging on the country's geographical location within the region will further facilitate regional integration and improve the country's competitiveness as an investment destination.

²⁶ See <https://www.youtube.com/watch?feature=youtu.be&v=nVvcKXmwACQ> and <https://www.unicef.org/zimbabwe/stories> for details.

²⁷ See <https://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/zimbabwe-multi-donor-trust-fund/> for details.

²⁸ See <http://www.worldbank.org/en/programs/zimbabwe-reconstruction-fund> for details.

²⁹ https://www.afdb.org/fileadmin/uploads/afdb/Documents/Project-and-Operations/Zimbabwe_-_National_Transport_Sector_Master_Plan_Study_-_Appraisal_Report.pdf

Opportunities for blending in the transport sector exist although a look at the key projects in the sector reflects dominance of the use of the PSIP budget in financing infrastructure projects. However, fiscal budgetary allocations are not enough given the total resource requirements, which call for involvement of other partners, including the private sector and development partners. The Transitional Stabilisation Programme (TSP) estimates that rehabilitating Zimbabwe's entire road network would require about US\$5.5 billion. It is also estimated that the National Railways of Zimbabwe (NRZ) requires in excess of US\$2 billion worth of investment for its rolling stock and to rehabilitate its entire network³⁰. This funding requirement is way beyond the government ability to provide through the PSIP given the binding fiscal constraint facing government. It is in this regard that government is keen to engage the private sector, with the PPP framework having already been identified.

The other area of transport infrastructure that is under the government spotlight is the maintenance, rehabilitation and expansion in the aviation sub-sector. This sector comprises ten airports, three of which are international airports, namely at Harare, Bulawayo and Victoria Falls. The other airports are located at Kariba, Masvingo, Buffalo Range, Mutare, Gweru, Beitbridge and Charles Prince. The ten airports are managed by the Civil Aviation Authority of Zimbabwe (CAAZ). With respect to pipeline transport, Zimbabwe through the National Oil Infrastructure Company (NOIC) manages the movement of fuel through the pipeline, including the 287km oil pipeline running from the Beira port in Mozambique to the Feruka Oil Refinery in Zimbabwe and the 208km long pipeline from Feruka to Mabvuku (Harare). Water transport is dominated by waterborne tourism, leisure activities, commercial and small-scale fishing and sports on the Kariba Dam and the Zambezi River. There is however potential for water transport (AfDB 2013).

The huge demands in rehabilitation, maintenance, and expansion of transport infrastructure offers immense opportunities for blended financing as these projects have potential to generate income streams. In this regard there is scope for developing innovative blended funding models which take into account the dynamics and risk profiles in each transport infrastructure subsector³¹. IDBZ, given its mandate, can structure these innovative blended financing models; offer training and financial advisory work to project promoters and mobilize blended financing to implement infrastructure rehabilitation, maintenance, and expansion projects in all the nodes of the transport sector.

Although there are a number of infrastructure projects that have been implemented in Zimbabwe in the transport sector, most of them did not involve any blending of public and private interest-bearing instruments, including blending with ODA. There is one example of a transport infrastructure project that can be showcased as having successfully incorporated elements of blending in Zimbabwe, even though the blending aspect is not largely pronounced. In addition, there are two examples of projects that had elements of blending but failed due to different reasons. These can be briefly discussed as follows:

Successful blending example

An example that can be given as a successful story involving blending is the Beitbridge Bulawayo Railway Project. It involved government using some incentives to attract the private sector, which was mainly in the form of a government guarantee, exemption of duty on imported rail equipment and spares, tariffs which are discounted and tax holidays (African Development Bank, 2011). Through the offering of these incentives, government was able to attract private capital (mainly from South Africa) to undertake a 30 year build-operate and transfer (BOT) PPP project worth about US\$85 million³². A special purpose vehicle, Beitbridge Bulawayo Railway (PVT) Limited (BBR) was established in which government, through the NRZ had a 15% shareholding while the other four investors had a combined shareholding of 85% (see project details in Annexure L.1.).

Thus, through a minimal contribution mainly in the form of foregone tax revenues and a debt guarantee, government was able to successfully mobilise four private investors into the project to broaden risk sharing. This example, though with only some limited use of blending tools and strategies, can be leveraged upon in drawing lessons on how similar projects can be designed.

Unsuccessful blending

Despite efforts to devise strategies that are able to incentivise private sector finance, some transport sector projects which were successfully negotiated failed at the implementation stage. In 2011, a road transport project which was aimed at refurbishing the Beitbridge Border Post through a build-rehabilitate-operate-transfer PPP concession worth about US\$90 million was concluded³³. The project involved the upgrading of the border post, construction of the main access road to the border, and provision of a weighbridge facility and accommodation for government staff at the post. It was designed to be completed over 18 months, from which the financing firms would recover their costs through user fees over a 15 year period. By providing a government debt guarantee³⁴, the government was able to attract different categories of private sector players to take up equity into the project. Three South African firms; Nedbank Capital, Old Mutual and Sanlam had committed to put in a total equity of US\$26 million into the project with the South African Infrastructure Investment Company (SAIIC) selected as the implementation company. In addition to equity, debt totalling about US\$71 million was secured from Standard Bank of South Africa. In order to take into account political risk, the Export Credit Insurance Corporation of South Africa was also attracted into the project to provide insurance for political risk.

³⁰ <https://www.idbz.co.zw/sector-operations/transport>

³¹ With respect to Figure 9 on risk-return profiles of infrastructure investments, these are the brownfield infrastructure projects with medium to high risk-return profiles where concessional finance can play a significant role.

³² Details found from the World Bank sources at website <https://ppi.worldbank.org/snapshots/project/Beitbridge--Bulawayo-Railway-2085>

³³ Old Mutual press statement on the deal at website <https://www.oldmutual.co.za/media-centre/newsdetail/2015/02/11/ideas-fund-finances-key-cross-border-infrastructure-deal>

³⁴ World bank at website <https://ppi.worldbank.org/snapshots/project/Beitbridge-Border-Post-5922>

However, despite the infusion of debt and equity as well as insurance for political risk and a debt guarantee, indications on the ground are that the project never took off³⁵ with the contract ending up being cancelled³⁶ by government after a review of the terms of the project. There was a general reluctance on the part of government to implement the project. In 2018, media reports indicated that a new contractor, Zimborders (a consortium of local firms) had been awarded the tender by cabinet under new terms which do not involve blending. The lessons from this experience generally is that while blending helps spread risks and helps mobilise capital from the private sector, there is still need to ensure that project terms are negotiated favourably so that there are no reversals later.

Another project in the transport sector which failed even though government had been able to devise a scheme which blended public and private resources is the Joshua Nkomo Expressway, which involved the dualisation of the road from the Harare International Airport into the city centre in 2012. A joint venture company-Sunshine Developments Limited, was established as a special purpose vehicle for the project, for which Government through Harare City Council (30%) and Augur Investments (70%) were the only shareholders. The government had to raise a total cost equivalent of about US\$80 million towards the project to fund its equity in Sunshine Development Limited by paying 90% of the cost in the form of land, construction material and services while the remaining 10%, valued at about \$8 million, was to be paid for in cash (High Court of Zimbabwe, 2016). As security, government further pledged 100 hectares of land in Gunhill Township. Augur Investments was awarded a tender to oversee the implementation of the project. Government, through City of Harare furthermore committed to giving out 4,000 hectares of land to Augur, including land on which Augur Investment had to design and construct a US\$100 million Shopping Mall in Borrowdale. Thus, through the use of land, government was able to attract private sector funding into the project, which is a form of blending public and private sector funding. However, there were a lot of challenges with the project, including allegations of corruption and misuse of funds, which eventually saw the deal being called off for failure to complete the project. ZINARA eventually took over the project to completion.

The project gives important lessons with respect to blending. While ‘sweeteners’ are needed to attract the private sector, it is important to ensure that the tendering process is not defective. Corruption allegations stemmed from the fact that Augur Investment could not be established to have a good track record in road projects and evidence that the tendering process was defective. In addition, so much land was offered as government contribution and when the contractor was replaced, government failed to recover the land as Augur won a court case against government (High Court of Zimbabwe, 2016). Thus, in blending, it is important that the blending tools and terms used ensure that contestation in the implementation do not result in undue loss of assets pledged by government in the concession agreements.

However, blending is more needed in the transport sector largely as infrastructure projects are not very profitable due to low traffic volumes. Blending for infrastructure financing should also target other local players, such as pension funds, who might be able to invest in long term projects. Interviews with the Ministry of Transport and Infrastructural Development as well as the Zimbabwe Association of Pension Funds and the Life Offices Association of Zimbabwe (insurance companies) were very revealing with respect to the ability to raise resources from pension funds and insurance companies (institutional investors) to financing road transport infrastructure. Pension Funds and insurance companies can be persuaded to finance road projects if revenue from toll fees is ring-fenced to facilitate repayment of loans to mitigate default risk. For example, toll fees from designated toll gates can be reserved and ring-fenced to repay the instrument rather than transferring them to the consolidated fund. The difficulty mainly lies in failure of road projects to be self-financing. The Ministry believes that not even one road in the whole country is viable at the moment. In general a minimum of 3,000 vehicles a day can be a yardstick for a viable road project. All roads in Zimbabwe do not have such a high volume of traffic. The loan for the Plumtree-Mutare road project is being repaid from toll gates from other routes in the country. This means that more players are needed for road projects to be profitable, especially when blended using grants and concessional long term loans. Grants and concessional long term loans can easily crowd in pension funds and other local investors under ring fencing conditions.

Interviews also showed that the railways sector has some opportunities for crowding in private sector financing. The infrastructure consists of mainly the tracks, signalling and telecoms, locomotives and wagons. The NRZ has been inviting the private sector to provide certain infrastructure and then connect to its railway line and work out arrangements, which would be reflected in reduced tariffs. One good example is that with Makomo Resources, which provided NRZ with about six locomotives for the ferrying of Makomo Resource’s coal produce. The same arrangement used to be in place between NRZ and Ziscosteel in which Ziscosteel had owned several wagons which were then moved along the NRZ tracks. Similar arrangements used to exist with some mining companies like ZIMASCO, the fuel industry and the sugar industry in Chiredzi.

The NRZ has recently entered into a new financing model with Diaspora Transnet International Group. The two created an SPV where the NRZ owns 60% of the shares while Transnet owns 40%. It is expected to be a 25 year project, to be fully operational by June 2019. The success or failure of the model will also offer lessons on the viability of blending public and private sector resources for railways. However, there are important lessons that can be drawn from the NRZ experience. It is easy for NRZ to enter into deals with the private sector, where the private sector finances for their transport needs, and then NRZ repays by giving service. Under this arrangement the private player should channel funds as a form of loan to the NRZ towards a specific objective, e.g. construction or refurbishment of wagons, under which the financier would be repaid by assured services, including dedication of some wagons or locomotives for the financier’s use. Given that there is an element of default risk involved, there is scope for including other partners into such deals, including ODA.

³⁵ <https://www.dailynews.co.zw/articles/2015/02/13/zinara-willing-to-partner-financiers> accessed 04/10/2018 and <https://www.pazimbabwe.com/business-28348-zimbabwe-loses-investments-worth-3-billion-bureaucracy-corruption.html>

³⁶ <https://www.newsday.co.zw/2013/01/beitbridge-expansion-in-limbo/>

4.4 Information and Communication Technology

Government acknowledges the inadequacy of information communications infrastructure in the country. The Zimbabwe National Policy for Information and Communication Technology (ICT, 2015) noted that whilst there has been significant roll out of communications infrastructure with 2G exceeding 75% population coverage (as at 31 December 2014), high speed broadband coverage is still patchy with most rural and remote areas remaining uncovered given the lack of a coordinated approach among the service providers. Broadband coverage in rural and remote areas remains low. Coverage is mainly concentrated in affluent urban areas. This has led to widening the urban-rural digital divide. Furthermore, there is inadequate access to reliable and sustainable electricity. Therefore a significant portion of the population depends on alternative power sources which are more expensive. Unreliable supply of electricity adversely affects the development and use of ICTs.

ICT Infrastructure is a primary focus area for government, according to key informants from the Ministry of ICT, because it is the underlying platform for the connectivity, provision and access of ICT services. This infrastructure includes physical structures, hardware and software that enable connectivity and usage. For example, the backbone infrastructure is the artery upon which all information is communicated and last mile infrastructure is the access network required for customers' access to information. Thus, for ICT to have a positive impact on economic development and transformation there is need to provide extensive, affordable and equitable access to infrastructure. High-bandwidth backbone networks are a key part of the investment needed for broadband. These networks connect towns and cities in countries and to facilitate business. Government is working on an e- government platform to reduce bureaucratic red tape under the ease of doing business reforms. This requires robust ICT infrastructure back bone which is also linked to the international submarine fibre-optic cable networks that convey communications traffic between continents.

Funding of ICT infrastructure projects has been driven by government guaranteed loans through State Enterprises like NetOne and Telone as well as private resources from companies like Econet. For example, China Exim Bank provided TelOne with a concessional loan of USD 98 million to expand its infrastructure and also provided NetOne with a loan of USD218 million dollars to upgrade its network. Econet and Telecel, have also been making their own investments to expand their networks independent of the NetOne.

Due to lack of cooperation among telecommunication companies on the use of ICT base stations, Government in November 2016 issued a Statutory Instrument compelling telecommunication companies operating in the country both public and private to share infrastructure³⁷ on purely contractual basis. The regulator, Postal and Telecommunications Regulatory Authority of Zimbabwe (POTRAZ), plays a limited oversight role in enforcing sharing. Ideally, ICT operators should compete on the basis of services provided as opposed to infrastructure. Government has pronounced itself through Zimbabwe National Policy for Information and Communication Technology that, all the ICT infrastructure required to build the backbone which is currently deployed in government departments and SOE will be pooled together to form the seed infrastructure. This approach will significantly reduce the initial setup funding requirements, will provide quicker implementation and eliminate duplication.

A mechanism for the sharing of ICT infrastructure should be developed which should be centred on the need to ensure fair compensation to those who invest in the particular infrastructure. Such a policy environment will further present opportunities to IDBZ which already has a foot print in providing ICT infrastructure development funding to scale-up mobilisation of blended funding to invest in this growing sector.

4.5. Housing Infrastructure

The provision of housing in Zimbabwe has been the prerogative of a number of players and institutions. These include local authorities (particularly provision of land), the private sector, pension funds, banks, insurance houses, government and individuals. Local authorities facilitate provision of housing by providing the land and also ensuring the necessary on-site infrastructure is in place. The type of player to provide housing infrastructure has been dictated by the type of funding for the housing developments as well as the modalities of how that funding will be provided. It has also been determined by access to land, location of the land and the cost of acquisition of that land.

A major player in the provision of housing infrastructure has traditionally been the pensions funds and insurance companies. As prescribed by the Insurance Act, pension funds and insurance firms have to invest in projects with 'prescribed asset status'³⁸. In this respect pension funds should invest at least 10% of their resources into such assets, while life insurance companies have to invest 7.5% and short term insurance firms have to invest 5% into the prescribed asset status projects.

Insurance and pension companies are already active players in housing provision. In 2011 the Insurance and Pension Housing Company (IPHC) came up with a project for the construction of low cost housing in Mbizo, Kwekwe. IPEC was involved in mobilising funding, which was for the development of about 400 housing stands in Kwekwe. The project however was not successful, despite IPHC being able to raise \$6 million through private placement in 2013. Building societies which had indicated interest in funding the housing construction pulled out of the project³⁹. IPEC also believes that the project failed because Old Mutual was the administrator and lacked an independent secretariat to carefully follow through and facilitate the project development.⁴⁰

Another notable example is the Mahombekombe Kariba Housing project in Kariba which was financed through the IDBZ. It was

³⁷ <https://www.technomag.co.zw/2017/11/10/private-companies-give-infrastructure-sharing-ict-minister/>

³⁸ A project is conferred 'prescribed asset status' if it is a project of national importance which cuts across several sectors. The Minister of Finance grants the status in terms of Section 26 (2) of the Insurance Act (Chapter 24:07)

³⁹ <https://www.pressreader.com/zimbabwe/the-herald-zimbabwe/20160517/281840052893267>

⁴⁰ In 2016, IPHC entered into partnership with IDBZ to sell the housing stands rather than building the houses

also financed by mobilising resources from the pension and insurance companies. The Bulawayo Students Accommodation Complex (BSAC) also involved the Motor Industry Pension Fund, Old Mutual and Zimnat who financed the project as partners to IDBZ. Personal housing schemes have also been done using pension money. Pension funds give loans to contributing members with a market related instrument which is paid from the member's pension.

According to the Life Offices Association of Zimbabwe (LOA) which currently boasts of 11 strong members, the members are interested in participating in infrastructure funding and are already involved in the housing sector such as Budiro with 2000 units (Old Mutual), SouthLea Park and Manresa (both developed by Fidelity) and other small ones run by small insurance companies. These investments are driven by the mortgage units within these insurance and pension firms that handle investments in properties. However, LOA has so far not been involved with any direct partnership with the public sector but can consider projects with duration of 10 – 30 years which match their liability structure. The most common financing mechanism on which pension and insurance companies can participate in blended financing projects are infrastructure bonds for projects that are assigned prescribed asset status.

4.6. IDBZ Capacity to Mobilize Blended Infrastructure Funding

Given its mandate IDBZ is involved in the business of long-term infrastructure, medium term industrial finance as well as short term commercial funding. Mobilising funding for its core mandate of infrastructure development has been adversely affected by a number of factors including the high and unsustainable domestic and external debt of the country and the high country political risks. The bank has developed a roadmap that seeks to achieve a capitalisation level of US\$250 million by 2018.

Increasing the level of capitalisation will increase IDBZ's capacity to effectively play catalytic role in the provision of infrastructure. This will further increase the capacity of IDBZ to co-finance infrastructure projects. Contribution of IDBZ's own capital into the financing of infrastructure projects is a good de-risking mechanism as it increases infrastructure investors/financiers confidence in the IDBZ promoted projects. Furthermore, investors and providers of debt/lines of credit consider the issuer or borrower's balance sheet size when making investment decisions. With a thin capital base of about US\$70 the Bank does not have enough capacity to leverage on its balance sheet to mobilise blended finance for infrastructure projects. A health balance sheet size also allows for partnership with local and international financial institutions in providing syndicated financing for infrastructure projects.

According to IDBZ documents this may include engaging potential development finance investors, especially the Brazil, Russia, India, China and South Africa (BRICS) countries. Focus areas for infrastructure development are energy, transport, water and sanitation, information communication technology (ICT) and housing sectors (basic onsite and offsite infrastructure)⁴¹. On future projects, IDBZ is also targeting the development of housing projects and student accommodation within Universities, through various financing structures which include joint venture arrangements with local authorities and private developers. IDBZ was granted authority by the Ministry of Finance and Economic Development to issue housing bonds of up to US\$100 million over a five-year period to finance various affordable housing projects across the country. The projects will be funded as and when they are fully developed and ready for market.

There are opportunities for IDBZ to partner with Local Authorities that have plans to develop housing projects and the ancillary infrastructure. For example, the Bulawayo City Council (BCC) like most local authorities is looking for more money for housing projects. It was pointed out that some Chinese institutions are offering funds at 1% interest. However, the Chinese institutions want to have the assurance that the BCC has borrowing powers. The BCC officials indicated that currently the City is not credit worthy. The BCC estimates that if they are given a loan of at least \$1 billion they will be able to put together most of the housing infrastructure requirements. The BCC has applied for a \$150 million loan from China for the Umvumela Housing project but they have to raise 15% (\$20 million) in hard currency as their contribution. However, the BCC is not able to raise this amount at the moment, and neither could they secure a government guarantee to this value. This generally shows that the opportunity to blend local authority resources and other partners for infrastructure financing exist but the failure by local authorities to raise their own contribution due to a poor balance sheet affect the project kick off. This is a typical project where the catalytic role of institutions like IDBZ in mobilising blended financing for infrastructure development can be demonstrated.

Thus, IDBZ needs to explore all models of mobilising infrastructure financing including equity participation/ shareholder loans, debt, mezzanine (hybrid) funding, co-financing and syndication, infrastructure bonds/commercial paper, climate finance, and loan guarantees among others. Financing can include equity contributions by the project sponsor with debt and credit enhancements to finance the construction and operation of an infrastructure project. IDBZ uses the cash flows of the financed project, once operational, as the source of repayment rather than the sponsor's balance sheet. Climate finance is also one of the emerging sources of funding. IDBZ was nominated as the national implementing entity by Government for the Green Climate fund. This include coordinating the project earmarked for securing funding from the Green Climate Fund (GCF) and other providers of climate finance once the Bank is accredited with the GCF. This involves promotion of low emission growth strategies in line with the Paris Agreement (2015) which Zimbabwe has ratified. In order to enhance the credit structure and attractiveness of a project to investors, IDBZ may in certain circumstances identify and ring-fence uncommitted cash flows from the project sponsor's existing operations and commit them towards debt service. Typical tenures for project finance loans will range from five to seven years including grace periods.

IDBZ should also continue to deepen its capacity to structure Public Partnership Projects (PPP) given the thrust of Government to implement infrastructure projects through the PPP framework. Some of these projects require long-term capital which range from 20 to 30 years. Under PPPs, IDBZ has competence to provide technical expertise developing the projects to bankability; packaging the

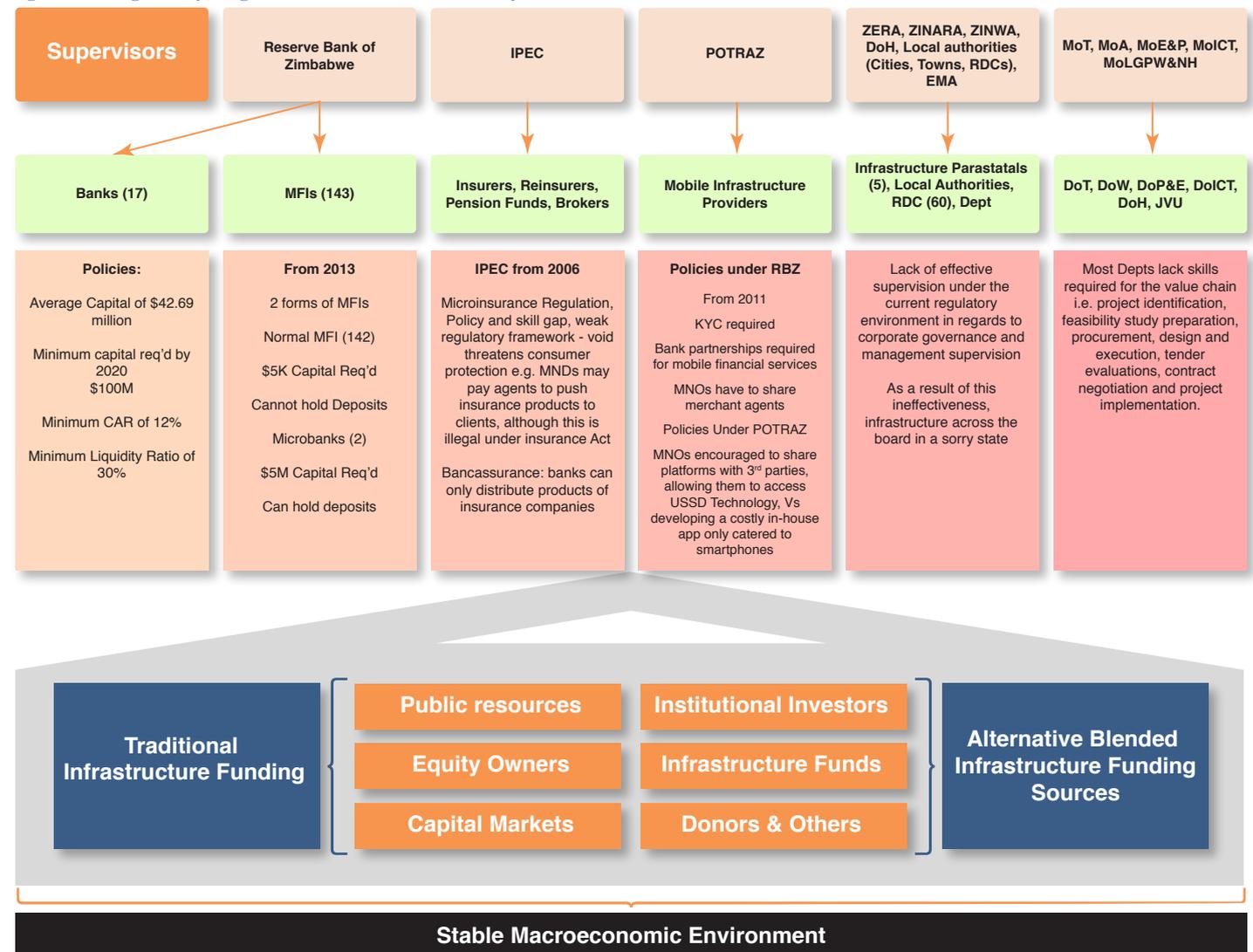
⁴¹ See IDBZ Medium Term Strategy 2016 – 2020, IDBZ Recapitalisation Proposal and Results Measurement Framework 2016 – 2020 for details.

projects to solicit for private sector participation; procurement and financing of the project and advising on the PPP contracts among other components of such transactions. IDBZ's project financing structures should be tailored to the project's financing and operational requirements and also to investor preferences particularly on the need to warehouse projects into Special Purpose Vehicles (SPVs). This is intended to facilitate the ring-fencing of the project assets and attendant cash flows as a mechanism to provide comfort to investors over the term of the project financing structure. IDBZ is also working towards blended finance initiatives which include a GCF accreditation. IDBZ is increasing its PPDF to US\$30m from US\$10m in 2018.

Chapter 5: Regulatory, Legal and Institutional and Policy Environment that Facilitates Blended Infrastructure Finance

The schematic diagram below captures the regulatory, legal, institutional policy environment that provides an enabling environment for the mobilization of blended finance infrastructure projects. Institutional capacities with regards to financial, skills and systems; adequacy of legislative and governance frameworks; capacities of infrastructure project promoters and the depth of financial institutions in terms of skills, diversity of financial products/instruments; stability and predictability of the overarching of the macroeconomic environment are all critical elements of creating an enabling environment to grow a blended infrastructure finance market. In this regard in the sections below we provide a brief review of some of the components, discuss some of the challenge and gaps that were identified which need to be addressed to facilitate growth of blended finance in infrastructure provision.

Figure 14: Regulatory, Legal and Institutional and Policy Environment that Facilitates Blended Infrastructure Finance



Source: Authors' Compilation Authors' Compilation

5.1. Macroeconomic Environment

The macroeconomic environment plays an important role in facilitate blending finance for infrastructure. There are several macroeconomic indicators that make the environment suitable for blending, which include the following.

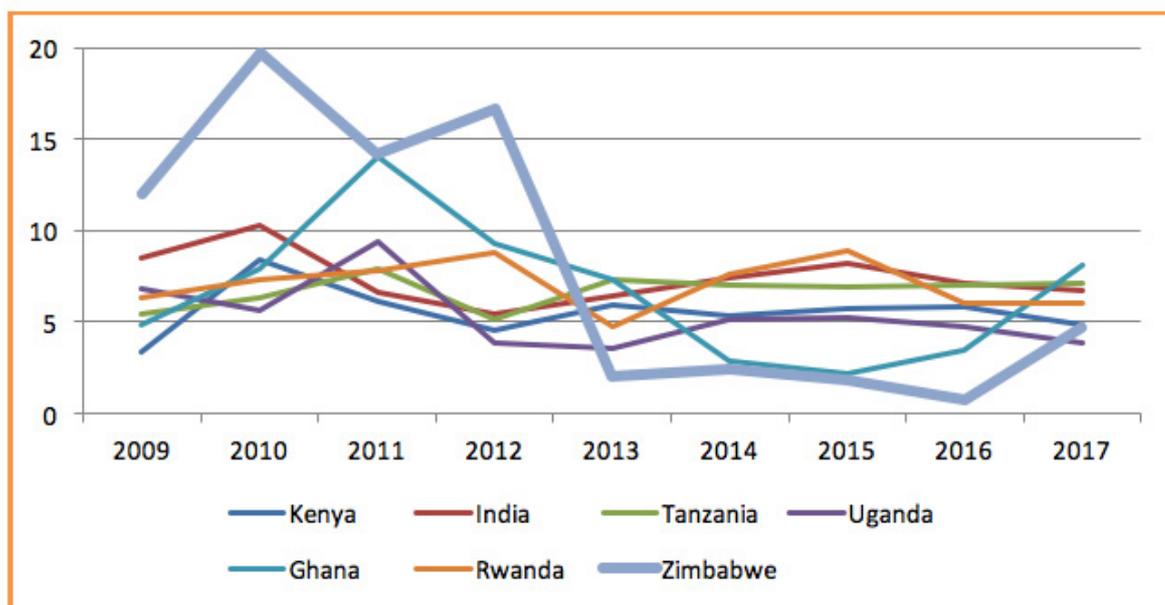
5.1.1. Economic growth

An economy that is growing would naturally attract investment, as economic growth shows that the general income levels are increasing, which also imply an increase in spending power. Given that infrastructure projects could be financed either through user fees or through loans which would need to be repaid by government, economic growth reflects an increase in the capacity to finance infrastructure, including government fiscal capacity. Blended finance for example tends to be more concentrated towards middle income countries than low income countries. Estimates by the Overseas Development Institute (ODI) show that only 3.6% of finance mobilised through blending flowed into low income countries between 2012 and 2015⁴², with the bulk going to middle income countries. Statistics show that in 2018, nearly half (49%) of blended finance transactions targeted lower-middle income transactions, while 24% targeted upper-middle income countries. Only 26% of the blended finance transactions targeted low income countries (Convergence, 2018). The World Bank classifies a lower middle-income economy as one with a GNI per capita between US\$996 and US\$3,895 and an upper middle-income economy as an economy with a GNI per capita between \$3,896 and \$12,055. In 2017, World Bank Indicators show that Zimbabwe had a GNI per capita of about US\$1,170. Thus, the country is already a lower middle income country and has the capacity to attract blended finance provided conditions are favourable.

Convergence (2018) shows that the leading country in terms of attracting blended finance in 2018 is Kenya, where about 14% of transactions on blended finance worth about US\$167 million took place. Other important destinations for blended finance included India (13% of transactions), Uganda (11%), Tanzania (11%), Ghana (8%) and Rwanda (8%). Convergence (2018) attributes this preference to the level of economic growth that had been witnessed in 2017, which influenced blending. It is therefore important to assess how Zimbabwe compares with these top countries in terms of economic growth to assess whether the level of growth matters as far as attracting blended finance is concerned.

A look at the economic growth rate trends (Figure 15) confirms that the countries where blending was mainly concentrated indeed are high growth countries and generally have been doing better than Zimbabwe, especially between 2013 and 2017. During this period, economic growth in Zimbabwe has been on the decline, reflecting declining production, weakening aggregate demand, poor export performance, low foreign investment inflows, dwindling government revenues, among others. However, the growth rate trajectory registered in 2017 is encouraging as it places Zimbabwe closer to these countries that are more favoured in terms of attracting blended finance. Thus, there is need for Zimbabwe to continue to pursue policies that are aimed at growing the economy as this would also make it attractive to investment, especially involving blended finance.

Figure 15: GDP Annual growth comparison of Zimbabwe and main blended finance countries



Source: World Bank Indicators

5.1.2. Inflation

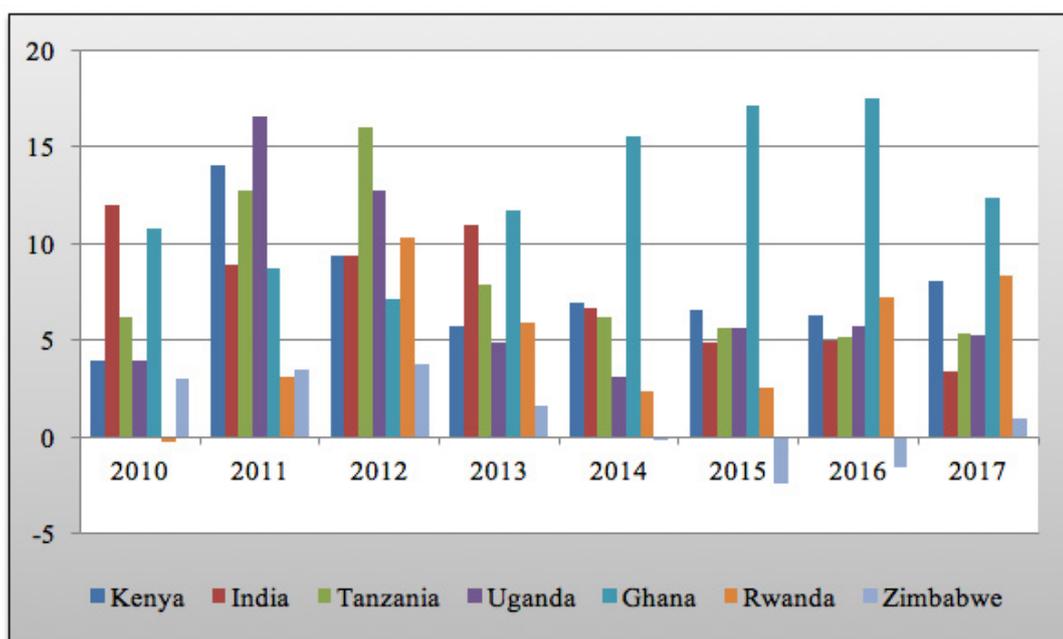
Inflation also plays an important role in making a country attractive for infrastructure financing in general and blended finance in

⁴² ODI 2018 article, 'Can blended finance work for the poorest countries?' at website <https://www.odi.org/comment/10650-can-blended-finance-work-poorest-countries>

particular. Inflation generally determines the return on investment; high inflation implies that interest rates have to be very high for the real interest rate to become positive. However, given that interest rates also represent the cost of borrowing, borrowing for investment purposes would be low in an environment of high interest rates. Thus, it is important to contain inflation at very low levels in order to attract investment, including blended finance.

Inflation was generally low during the early years of the multi-currency regime which started in 2009, which had some positive effect on disposable incomes. Increase in disposable income has an effect of improving demand for goods and services. However, there has been a built-up of inflationary pressure since the beginning of 2017 culminating in a surge of inflation to 20.85% in October 2018, followed by 31.01% in November 2018, 42.09% in December 2018 and 56.9% end of January 2019. This inflationary development does not augur well for financing infrastructure projects through issuance of instruments such as bonds unless they are inflation indexed. However, before 2018, Zimbabwe had been doing well in managing inflation, performing better than those countries which attract a lot of blended finance (Figure 16). This shows that while inflation is important, it does not work in isolation as far as attracting blending is concerned. Generally all countries, except Ghana were able to contain their inflation to single digit levels in 2017, which played a key role in attracting blended finance in 2018. This implies that Zimbabwe has to pursue a strong disinflation programme as the country's inflation rate is slowly becoming an outlier in the region.

Figure 16: Annual inflation of Zimbabwe and main blended finance countries



Source: World Bank

5.1.3. Currency and exchange rate risks

Although blending reduces risk and helps catalyse concessional funding, there is still need for the investors to be assured that they have the ability to repatriate their proceeds as well as to predict the exchange rate. Currency risk is a key consideration in negotiation of blended financing contracts hence the need for improvement in management and predictability of currency regime in any country. Currency risk also occurs when there are unfavourable currency fluctuations for projects financed in foreign currency and returns earned in local currency. This also includes the availability of foreign currency to pay back investors.

The introduction of bond notes in November 2016 combined with the expansion of the money supply propelled by increased government borrowing through issuance of treasury bills, resulted in a high volume of bank balances (often referred to as RTGS balances) failing to be sustained by the available hard local and foreign currency. For example, RBZ statistics show that in October 2018, total deposits were about \$10 billion while foreign notes in circulation were only at US\$70.4 million with balances available in nostro accounts being US\$305.5 million. The ratio of foreign currency to total deposits was only about 4%. This implies that investors can struggle to exchange the returns from projects they would have invested in foreign currency but are earning in local currency (RTGS and bond notes, which are now collectively known as RTGS dollars) into foreign currency. Thus, this fear that investors would be stuck with RTGS dollars and be unable to convert it into foreign currency is a risk that does not promote blending in infrastructure financing just as in all other investments. This is also worsened by the fact that finance for blending is mainly acquired in foreign currency from foreign investors due to the fact that domestic capital markets are shallow and underdeveloped and therefore cannot meet the required quantum of resources or term financing.

Pronouncements by the Minister of Finance that the country will soon have its own currency have partially been realised by the introduction of a local currency called the RTGS dollar announced in the February 2019 Monetary Policy Statement. Currency reforms

introduced by the Monetary Policy Statement announced in February 2019 saw the 1:1 policy peg between the USD and the RTGS/ bond note which had proved to be unsustainable being removed for a managed interbank determined exchange rate. The rate of the RTGS dollar against the US dollar has so been pegged around 2.5. What remains is the introduction of the interest rate on the RTGS\$ and the Lender of last resort facility to facilitate money market transactions. The effectiveness of new currency regime and its capacity to facilitate blended finance in infrastructure projects hinges on market confidence and stability of the currency regime.

The foreign currency risk is also amplified by the size of foreign currency reserves. A country can use foreign reserves to defend its exchange rate by running them down and increasing the availability of foreign currency in the market when the demand for foreign currency increases. However, a better strategy is to put in place the right fundamentals to build sustainable foreign reserves as running down foreign reserves to defend a currency may not be sustainable. According to Reserve bank of Zimbabwe (RBZ) statistics for October 2018, the reserves in months of imports were at 0.173 months, equivalent to only a week of import cover. Government should prioritise policies that promote the building up of reserves, with the recent measures which made foreign currency easily tradable between those firms in need of foreign currency and those with foreign currency through the banking system being among the positive steps in promoting the building of reserves.

Therefore, policies oriented towards foreign currency generation as well as foreign currency saving should be prioritised. The incentives that are given for generating foreign currency are a positive step but these should also be extended to those that are saving foreign currency. There is need for all stakeholders to see value in generating as well as in producing alternative products that save on the need to import products.

5.2. Status of the local investor base

Given that blending is intended to catalyse private sector participation, it is important to ensure that the local investors are ready to utilise opportunities availed to them. Debt financing can be used as an important tool in blending, especially through the issuance of bonds. However, bond issuances are largely successful if there is participation of local institutional investors such as pension funds and insurance companies. The profile of their liabilities which is long term drive them to look for matching long term assets such as infrastructure projects. Pension funds and insurance companies need to gain enough confidence in the operating environment and regulatory track record before they subscribe to the different instruments that could be used in blending for infrastructure.

Zimbabwe has a fairly stable institutional investor base with pension funds (insured funds; self-administered funds; and stand-alone-self-administered funds) having an estimated asset base of US\$4.38 billion as at 30 June 2018⁴³. Insurance companies, especially life insurance firms, also have the opportunity to invest in long term projects. As at 30 September 2018, life assurance firms had an estimated asset base of about \$2.76 billion⁴⁴. Although financial deepening within the context of blending for infrastructure in Zimbabwe would need to go beyond pension funds and life insurers, there is need to ensure that these sources of finance are adequately tapped into for infrastructure financing as well through incentives as well through incentives. Both pension funds and life insurers have been active in the local market, through both equity investments and subscribing to bonds and other instruments issued in the market. These include both infrastructure and non-infrastructure projects.

As prescribed by the Insurance Act, pension funds and insurance firms have to invest in projects with 'prescribed asset status'⁴⁵. In this respect pension funds should invest at least 10% of their resources into such assets. As at 30 June 2018, pension funds in Zimbabwe were holding onto various instruments which had been given the prescribed asset status by government to the tune of about \$235.2 million, resulting in a prescribed asset ratio of about 7.37%. This implies that there is still scope for investing in more prescribed asset to reach the 10% mark.

⁴³ Insurance and Pension Commission (IPEC) Pensions Report for the Quarter Ending 30 June 2018 at website <https://ipec.co.zw/findata/vfm-admin/vfm-downloader.php?q=dXBsb2Fkcy9SZXBvcnRzL1BlbnNpb25zL1F1YXJ0ZXJseSUyMFJlcG9ydHMvMjAxOC9TZWNvbmQlMjBRdWFydGVyJTlWmUyMjAxOCUyMFB1bnNpb25zJTlWUmVwb3J0LnBkZg==&h=83cd171038cefa1a6884bd1910f28e8c> accessed 5 January 2019.

⁴⁴ IPEC Life Assurance Industry Report for the 9 Months Ended 30 September 2018 at website <https://ipec.co.zw/findata/vfm-admin/vfm-downloader.php?q=dXBsb2Fkcy9SZXBvcnRzL0luc3VyYW5jZS9RdWFydGVyYHk1MjBSZXBvcnRzL0xpZmU1MjAlMjhhMmB25nJTlWVG9yYUyOS8yMDE4LzIwMTglMjBUaGlyZCUyMFF1YXJ0ZXI1MjBMaWZlJTlWUmVwb3J0LnBkZg==&h=97dcb02134cec22e4b3dd9ac5365b6a5> accessed 5 January 2019

⁴⁵ A project is conferred 'prescribed asset status' if it is a project of national importance which cuts across several sectors. The Minister of Finance grants the status in terms of Section 26 (2) of the Insurance Act (Chapter 24:07)

Life insurance companies have to invest 7.5% of their assets into the prescribed asset status projects. As at 30 September 2018⁴⁶, life assurance companies had invested about \$322.2 million⁴⁷, resulting in an industry average prescribed asset ratio of 11.7%, well above the 7.5% benchmark. This generally shows that resources from both pension funds and life assurance firms have already been tapped into various areas in Zimbabwe. However, there has been more concentration in the housing sector than the other sectors because property is a defensive asset during high inflation periods.

Interviews with the players established that while there is scope to get funding from pension funds and insurance firms, the hyperinflation environment has left them now more reluctant. Instruments used, including bonds, need to be inflation indexed to be attractive. Thus, a growing economy that has low inflation is more likely to see funds being unlocked from the pension and insurance sector. In addition, due to loss of confidence in project implementation capacity in government ministries in general and some state owned enterprises in particular, insurance and pension funds are willing to participate as consortiums provided they also participate in the implementation and management. Where SPVs are created to run or manage the projects, they would prefer taking up equity in the SPV rather than just releasing money without any oversight on how it is used. It is therefore clear that the opportunities for engaging pension and insurance firms in blended finance for infrastructure projects exist but they have to be involved in discussions on how best such projects could be structured to minimise risk on their part. However, in general there is an opportunity to access these funds either directly (equity or loans) or indirectly (issuance of interest bearing instruments).

With regards to deepening, the finance pool can be easily increased through the reforming of the public service pension scheme. Pension contributions of civil servants are treated as general government revenue and expenses are disbursed from the Government's Consolidated Revenue Fund under Constitutional and Statutory Appropriations. The public service scheme is administered by the Pensions Agency which falls under the Civil Service Commission. The public pension system currently operational in Zimbabwe is a defined benefit scheme rather than a defined contribution scheme. A defined benefit plan promises a specified monthly benefit at retirement. A defined contribution plan on the other hand does not promise a specific amount of benefits at retirement. Rather both the employee and the employer contribute to the employee's individual account with the contributions being invested on the employee's behalf. The employee will ultimately receive the balance in his or her account, which is based on contributions plus or minus investment gains or losses.

Government has already accepted the need to migrate from both the Pay-As-You-Go scheme to a fully funded scheme and from a direct benefit scheme to a direct contribution scheme as announced in the 2019 National Budget. The critical reform requirement on the Government Pension Scheme is to move from the pay-as-you-go scheme currently in place to a fully funded scheme. The funds will then be a national saving which can be invested in national projects including infrastructure. The move from defined benefit to defined contribution is a transfer of risks from employer to employee and of course an enhancement management process which deepens the markets. Thus, the public pension scheme when converted into a fully funded scheme will introduce another pool of funds which can be tapped into for infrastructure financing. Government should therefore speed up the public pension scheme reforms.

There is also scope for reintroducing municipal bonds to finance infrastructure for the local authorities, including water and sewer infrastructure as well as road rehabilitation. However, there is need for investors to invest in municipal bonds not only because there is central government guarantee and the project is assigned prescribed asset status, but also based on sound business plans from the issuing local authorities. The cities of Harare, Bulawayo, Gweru and Mutare used to issue interest bearing instruments on the merit of their balance sheets and credit worthiness. The municipal bonds need to be able to be repaid based on the income streams from the projects where the proceeds have been invested. There is need for confidence building on the part of municipalities so that they shake off the allegations of mismanagement, poor governance and lack of accountability, especially stemming from failure to produce audited financial statements. This would improve their image and open up opportunities for them to issue municipal bonds again. Being rated by reputable rating agencies would enhance their credit status. Project based bonds can also be rated on their own right and be able to attract sufficient funding.

Debt burden

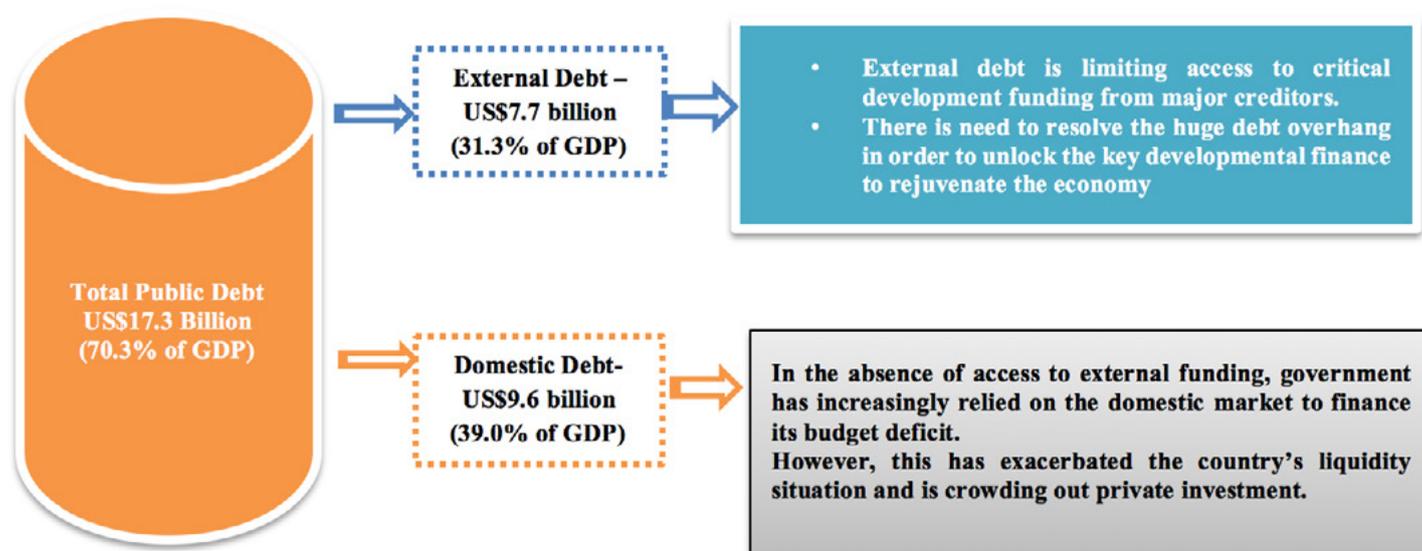
Any government's ability to partner the various players in blended financing can be easily compromised if it is highly indebted. A high level of external debt can affect blending from two perspectives. Firstly, government will not be able to attract concessional funding from the key regional and global development finance institutions without repaying previous debt. The key participating IFIs in blended finance in the region include the World Bank and the African Development Bank which are already owed by Zimbabwe. This makes access to concessional finance in infrastructure projects of a public nature difficult. Secondly, a high external debt implies that government has to devote a significant portion of the resources from the budget, which could have been devoted to infrastructure finance towards debt repayment. This limits the ability of government to raise domestic resources for infrastructure financing.

A huge domestic debt also has an impact on blending, especially if the debt arose not due to the need to finance infrastructure but due to the need to finance recurrent expenditure. However, government would be borrowing from the same sources which the private sector would be trying to unlock funding for infrastructure. Thus, a huge domestic debt crowds out private sector investments. The impact of a huge domestic and external debt are summarised in Figure 17.

⁴⁶ Insurance and Pension Commission (IPEC) Pensions Report for the Quarter Ending 30 June 2018 at website <https://ipec.co.zw/findata/vfm-admin/vfm-downloader.php?q=dXBsb2Fkcy9SZXBvcnRzL1BlbnNpb25zL1F1YXJ0ZXJseSUyMFJlcG9ydHMvMjAxOC9TZWNvbmlmBRdWFydGVyJTl-wMjAxOCUyMFBlnNpb25zJTlUwVvb3J0LnBkZg==&h=83cd171038cefa1a6884bd1910f28e8c> accessed 5 January 2019.

⁴⁷ Ibid

Figure 17: Implications of Zimbabwe's huge public debt



Source: Figures obtained from Ministry of Finance & Economic Development, 2018

During the first two years of the multi-currency regime (2009 and 2010), the country almost balanced the fiscal budget. However, from 2011 onwards, Government pursued an expansionary fiscal policy that resulted in rising government expenditures against available fiscal revenues resulting in the accumulation of fiscal deficits. Zimbabwe is now burdened by a huge external debt estimated to have increased by more than US\$1 billion between 2015 and 2018 (Table 9). Domestic debt also increased tremendously from only about US\$2 billion in 2015 to about US\$9.6 billion in 2018. According to Convergence (2018) the distribution of all the transactions involving blended finance that took place in 2018 shows that blended finance projects range from about \$5 million to over \$1 billion, with a median deal size being \$56 million. This means that the projected incremental total debt for Zimbabwe of about US\$3.4 billion in 2018 alone was enough to have funded more than 60 blended finance projects. Furthermore, the linkage between debt and blended finance can also be explained in another way. Government debts constrain the Government to offer guarantees, increases sovereign risk and also reduce credit worthiness of government as a credible partner.

Table 9: Zimbabwe's Domestic and External Debt, 2015 - 2018

	Dec 2015	Dec 2016	Dec 2017	Sept 2018	Proj. Dec 2018
Total DEBT (US\$ million)	9,005	11,254	14,641.7	17,282.3	18,076
% of GDP	45.1	54.8	66.4	70.3	57.3
Domestic Debt (US\$ million)	1,905	4,014	7,133.6	9,624.9	9,571.1
External Debt (US\$ million)	7,100	7,240	7,508.1	7,657.4	8,505.9

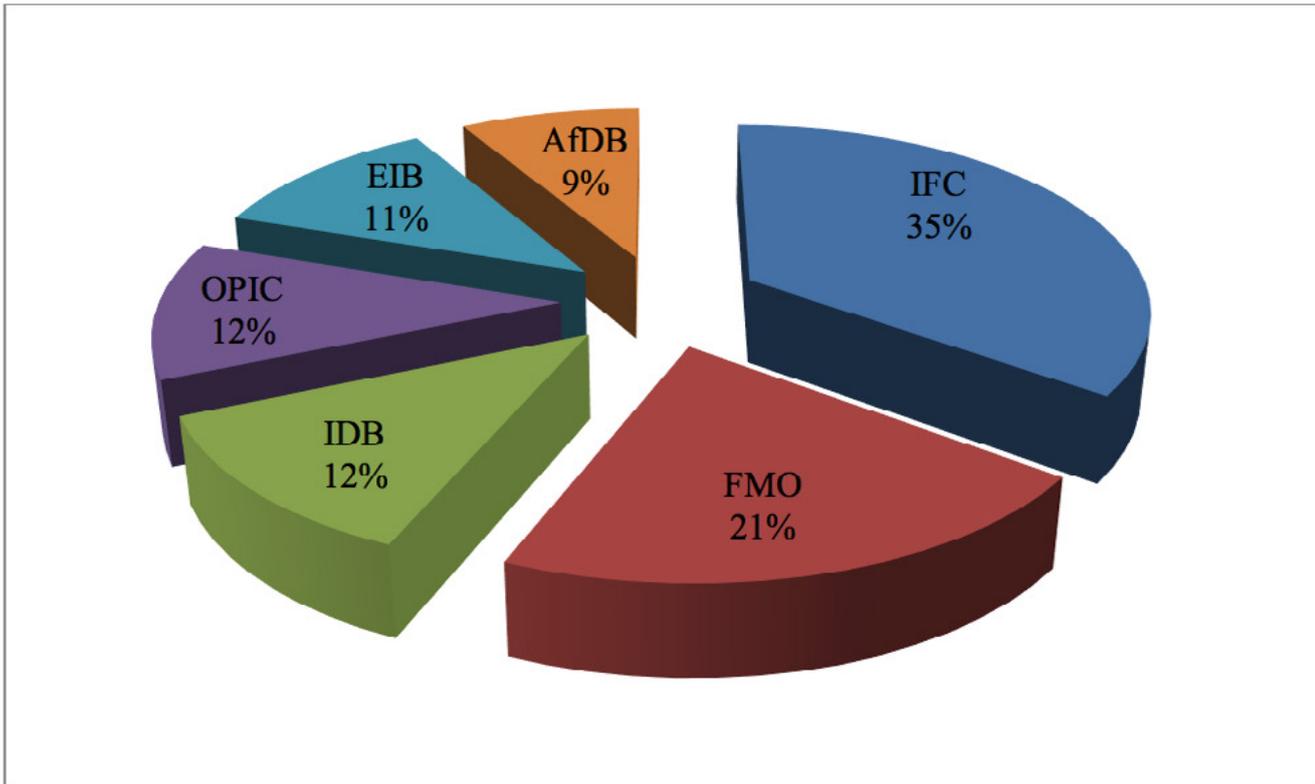
Source: Ministry of Finance & Economic Development, 2018

This therefore implies that the current ongoing fiscal reforms to contain government expenditures are central to attracting blended finance. The fiscal reform measures are expected to help generate surpluses which would be useful in retiring debt, especially domestic debt.

Capital Budgetary Performance

Although there are a number of players involved in blended finance, it is important that government plays the most important role in the process as most infrastructure projects are of a public nature. Government should take a lead in demonstrating that infrastructure projects should be funded, especially by funding the initial stages of the projects, including project preparations to come up with a pipeline of bankable infrastructure projects that can be used to solicit for private sector participation. Thus, the total resource envelope that is earmarked for capital expenditure is important in influencing blending. For the period 2010 to 2017, government allocation to capital expenditure ranged from US\$200 million to US\$400 million. Given that these figures include net lending by Government it

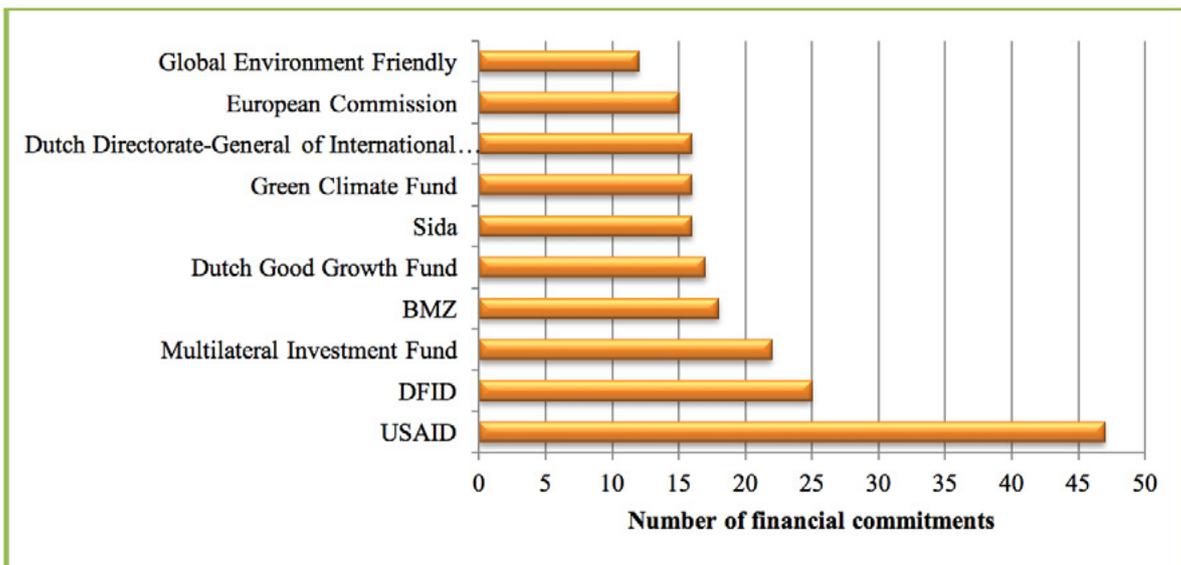
Figure 19: Top DFIs involved in blended finance



Source: Convergence 2018

In addition to DFIs that offer concessional finance, ODA that can be used for blending can also come in the form of grants by development partner institutions. Such institutions include the United States Agency for International Development (USAID), Department for International Development (DFID) and the Multilateral Investment Fund among others (Figure 20). This generally implies that while there is still scope to pursue other avenues for ODA, the relationship that Zimbabwe has with these key players in blended finance through ODA plays a larger role in influencing the extent to which the country can leverage on ODA.

Figure 20: Top Public Investors with Development Mandates by Number of Deals in 2018



Source: Convergence 2018

Given that both USAID and DFID are already active in Zimbabwe, it is important to try and engage them to re-orient their intervention from humanitarian aid and technical assistance to providing concessional funding to de-risk some infrastructure projects and make them viable for the participation of the private sector. USAID has a facility that provides access to credit using guarantees, including first loss guarantees as a tool to promote lending. DFID also supports blended finance by focusing on climate change, renewable energy,

water supply management and infrastructure in general through a combination of loans and grants (Savoy & Milner, 2018). Given that ODA would include both grants and concessional loans, tapping into such schemes would also call for the addressing of the general macroeconomic environment to make it more conducive.

In addition to engagement of development partners to re-orient their interventions there is also scope for government to forge new relationship within the context of its re-engagement initiatives particularly with development partners already engaged in blending infrastructure financing. However, the major impediment for such reorientation is the economic sanctions imposed on Zimbabwe. In this regard discussion of re-orienting the focus of ODA support should be part and parcel of the reengagement efforts.

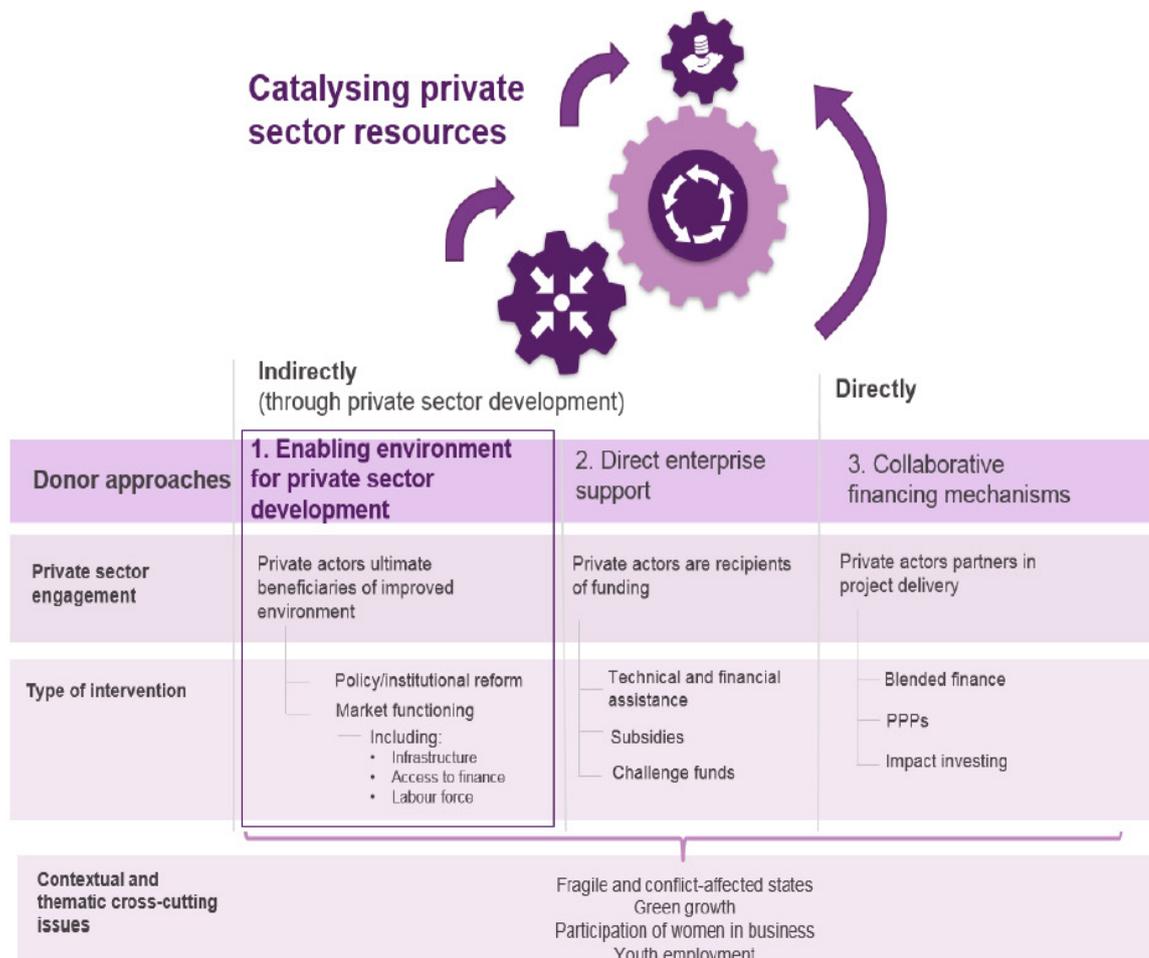
Zimbabwe has been getting some grants to undertake some infrastructure projects, which however could have been blended with private sector resources to increase the scope. For example, in June 2018, a grant of US\$21 million was received from the Japanese government to improve the steep gradients on the Makuti– Chirundu section of the Harare-Chirundu highway⁵¹. This grant came at a time when government was also trying to get investors for the dualisation of the Chirundu-Harare road. This was an opportunity to leverage on this grant and crowd in other potential investors as it reduces the final cost of rehabilitating the Harare-Chirundu highway.

This therefore implies that there is need for a clear strategy to expand the scope and leverage on available ODA support in the infrastructure development through blended financing. Improvement in the general macroeconomic environment, including addressing barriers to investment through business climate reforms as well as deepening local capital markets will stimulate such partnerships. Development Initiatives (2018) argues that blended finance through donor approaches appear to mainly target countries with relatively high ease of doing business and Global Competitiveness Index scores such as Turkey, India and Indonesia neglecting those with lowest scores where need may be greatest.

Donor approaches to catalysing private finance are categorised according to the role played by private actors and their level of involvement in delivering interventions (Figure 21). For instance, enabling environment interventions (approach 1) benefit private actors but do not directly engage them in the delivery of activities and thus do not rely on the existence of a functioning, vibrant private sector. On the second approach, private sector benefits directly through funding such as technical and financial assistance and subsidies. Collaborative financing mechanisms (approach 3) instead requires direct engagement with private actors as partners in the delivery of activities/projects and call for considerations around the supply of commercially viable projects in the country. This can be done through blended finance.

⁵¹ Embassy of Japan in Zimbabwe, 'Japan's Development Cooperation in the Republic of Zimbabwe' Available at <https://www.mofa.go.jp/mofaj/gaiko/oda/files/000430558.pdf>, accessed 30 January 2019

Figure 21: Schematic Presentation of Donor Approaches



Source: *Development initiatives (2018)*

As the country focuses on achieving a middle income status by 2030 the scope of engaging development partners/donors can be expanded to focus on bridging the infrastructure gaps in areas with severe deficits. The need to achieve vision 2030 should guide donor interventions, particularly in the development of priority infrastructure.

5.4. Legal Environment and Institutional Issues

A comprehensive and effective legal system; adequate protection of property and creditor rights; and a reliable, efficient and independent justice system are essential for the participation of the private sector and ODA in infrastructure development (Thorne, 2011). The Zimbabwe constitution provides the overall parameters which bind the behaviour of all economic and socio-political agents in the country. It has very specific provisions that are aimed at protecting economic rights, including property rights, which are fundamental in the attraction of both short term and long term investments. Section 71 of the Constitution alludes to the protection of property rights, Subsection (3) observes that “Subject to this section and to section 72, no person may compulsorily be deprived of their property except where the following conditions are satisfied.”, and the law requires that in the event of acquisition, the acquiring authority should (i) give reasonable notice; (ii) pay fair and adequate compensation; and (iii) if the acquisition is contested, to apply to a competent court before acquiring the property. Therefore, the supreme law has the pillars to protect private investment, including infrastructure related investments.

Chapter 14 of the Constitution of Zimbabwe on Provincial and Local Government Subsection (c) of the Preamble recognises that “*the equitable allocation of national resources and the participation of local communities in the determination of development priorities within their areas; there must be devolution of power and responsibilities to lower tiers of government in Zimbabwe.*” Section 264 of the Constitution goes further to elaborate on Devolution of governmental powers and responsibilities. Section 1 notes that, “whenever appropriate, governmental powers and responsibilities must be devolved to provincial and metropolitan councils and local authorities which are competent to carry out those responsibilities efficiently and effectively.” Section 2 underscores the objectives of the devolution of governmental powers and responsibilities “to provincial and metropolitan councils and local authorities”.

Among these objectives is (a) to give powers of local governance to the people and enhance their participation in the exercise of the powers of the State and in making decisions affecting them; (b) to recognise the right of communities to manage their own affairs and to further their development; (c) to ensure the equitable sharing of local and national resources; and (d) to transfer responsibilities and resources from the national government in order to establish a sound financial base for each provincial and metropolitan council and local authority. In this regard therefore the Constitution gives the foundation for the empowerment of local authorities which should be the basis for their abilities to enhance their participation of promoting investment, including infrastructure related investment, at the local level.

There are a number of other secondary pieces of legislation that are in place to promote and protect investors. These include the Joint Ventures Act (Chapter 22:22), the Special Economic Zones Act (Chapter 14:34) and the Zimbabwe Investment Authority Act (Chapter 14:30). The Joint Ventures Act seeks to provide for the implementation of joint venture agreements between contracting authorities and counterparties. The Special Economic Zones Act provides for the establishment of the Zimbabwe Special Economic Zones Authority and special economic zones. The Zimbabwe Investment Authority Act established the Zimbabwe Investment Authority to provide for the promotion and co-ordination of investment through the repealing of the Zimbabwe Investment Centre Act [Chapter 24:16] and the Export Processing Zones Act [Chapter 14:07]. However, the process of merging the three pieces of legislation and related institutions to form the Zimbabwe Investment Development Authority (ZIDA) through the ZIDA Act, is already underway. ZIDA will be a “one-stop-shop” responsible for all the investment related issues in the country.

One of the instruments that the country has been using to promote and protect investment is the Bilateral Investment Promotion and Protection Agreement (BIPPA). A BIPPA is an agreement establishing the terms and conditions for private investment by nationals and companies of one state in another state and the type of investment is in the form of foreign direct investment (FDI)⁵². According to the United Nations Conference on Trade and Development (UNCTAD)⁵³ Zimbabwe has Bippas with 35 other countries. However, out of the 35 agreements, only 10 of them are in force. These are Denmark (1999); China (1998); Germany (2000); Iran (2015); Kuwait (2008); Netherlands (1998); Russia (2014); Serbia (1997); South Africa (2010); and Switzerland (2001). The other 25 Bippas, although signed several years in the past, have not yet been activated.

Other important pieces of legislation are those tasked with the mobilisation of funds for long term investments. The Pensions and Provident Fund Act (Chapter 24:09) provides for the registration, incorporation, regulation and dissolution of pension and provident funds. On the other hand, under the Insurance Act, pension and insurance firms have to invest in projects that have been given the “prescribed asset status” by government. Accordingly, pension funds should invest at least 10% of their resources into such assets, while life insurance companies have to invest 7.5% and short term insurance firms have to invest 5% into the prescribed asset status projects.

The Sovereign Wealth Fund of Zimbabwe Act [Chapter 22:20] (No.7 of 2014) also provides for the operationalisation of the Sovereign Wealth Fund of Zimbabwe. The key objectives of the fund include (1) to make secure investments for the benefit and enjoyment of future generations of Zimbabweans; and (2) to support the development objectives of the Government, including its long-term economic and social development; (3) to support fiscal or macroeconomic stabilisation, in particular to supplement (in accordance with this Act and the Finance Act) the revenues of Zimbabwe when these are prejudiced by the fluctuation of prices payable for those minerals on which royalties and other taxes are collected for the benefit of the Consolidated Revenue Fund⁵⁴; and (4) to contribute to the revenues of Zimbabwe from the net returns on its investments in accordance with section 21. Therefore, once the Sovereign Wealth Fund becomes fully operational, it will provide an avenue for mobilisation of blended infrastructure finance.

On the international front the Zimbabwe Democracy and Economic Recovery Act (ZIDERA) introduced by the United States Senate in 2001 and revived by President Trump in 2018 gives certain restrictions for finance and investment in Zimbabwe on United States companies and individuals. The piece of legislation requires the Government of Zimbabwe to uphold certain democratic and human rights principles including the rule of law in order to access United States funding and investment. This resulted in restrictions in trading and investment between Zimbabwe and the United States, declining aid assistance, and tension in bilateral ties. The ZIDERA Act continues to thwart any attempts by companies, including local authorities, from being able to access offshore long term funds for investment in infrastructure. In fact, through the enactment of ZIDERA, Zimbabwe’s access to off shore finance and credit facilities has been severely curtailed.

The experience in Zimbabwe with respect to transfer of assets particularly infrastructure previously developed, owned and operated by local authorities when new public entities are created specifically to deal with a particular infrastructure highlight some flaws which can undermine the mobilisation of blended infrastructure funding. Information obtained from field interviews indicated that when the

⁵² https://en.wikipedia.org/wiki/Bilateral_investment_treaty

⁵³ <https://investmentpolicyhub.unctad.org/IIA/CountryBits/233#iiaInnerMenu>

⁵⁴ Most countries set a separate Fund for this purpose usually called The Stabilization Fund”

Energy and Power function was transferred from local authorities to the Zimbabwe Energy and Power Supply Authority (ZESA) there was no compensation for the assets and properties built by local authorities. The local authorities were simply given directives to transfer the assets to the new entity. The directives to the Cities of Harare and Bulawayo to transfer ownership of thermal power stations to ZESA were done without any compensation for the construction of the power stations, even though some loans from banks and other debt instruments had been used to secure resources to construct them. In 2006, a directive was issued that all water and sanitation infrastructure must be handed over to ZINWA from all the local authorities⁵⁵ without any consultations with the local authorities and other stakeholders. This has had serious implications for infrastructure investors in water and sanitation provision. The practice creates uncertainties and erodes confidence of partners seeking to invest in infrastructure within the jurisdiction of local authorities thus undermining their capacity to mobilise blended finance.

In the same vein, ZINWA Act (Chapter 20:25) (section 3 of the Schedule) gives power to the Zimbabwe National Water Authority “*To recommend to the appropriate Minister that any property relating to water be acquired or expropriated for development or utilization in the national interest or for the benefit of the inhabitants generally in the area concerned.*” This section of the Act is a major disincentive to any would be investor in water infrastructure in the country⁵⁶ Legal instruments should be enablers rather than disincentives. As it stands currently ZINWA is struggling to construct new water reservoirs in the country and private players/investors cannot invest their resources under the current situation.

In respect of the above, there should be a clear policy of transfer of assets and compensation based on professional valuation of such assets and in line with international standards. Therefore the review of legal, framework has shown the need to align subsidiary legislation with the Constitution with regards to protection of property rights. Protection of property is key to facilitating the blending of private and public funding for infrastructure development. This should apply at central Government, local government and other agencies that may hinder or facilitate progress in infrastructure delivery. Zimbabwe has a window of opportunity to address the identified flows in the legislative framework through engagement of all players in the infrastructure delivery value chain within the context of easy of doing business reforms.

5.4.1 Other Aspects of the existing legal environment that limit the scope of blended finance projects

The laws require that before a blended finance infrastructure project can proceed, particularly where powers and duties of a public entity are being delegated to a third party, it is necessary to follow a formal bidding or procurement process. These processes are guided by the Public Procurement and Disposal of Public Assets Act [Chapter 22:23]. The Act provides for the control and regulation of public procurement and the disposal of public assets so as to ensure that such procurement and disposal is effected in a manner that is transparent, fair, honest, cost- effective and competitive.

The print media has been awash with reports of corruption and bribes in the public procurement. Some matters have gone unreported despite having been unearthed by the internal or external auditors. Most of the individuals who have taken advantage of the economic policies are influential government officials and other powerful high ranking political officers with access to funds and capital⁵⁷. By using its powerful influence and relevant governmental connections, this elite group of corporate actors finds it easy to manipulate the procurement system and obtain preferences from institutions established under procurement legislation. Such a scenario erodes the integrity of the public procurement system and damages system transparency.

While the rules and regulations on public procurement attempt to plug loopholes for corrupt practices there seem to be no enabling legal framework to allow bidder’s enforceable right to review when public entities breach the rules. The statutes are clear on the oversight role of PRAZ on procuring entities but it appears the law is silent on who oversees PRAZ itself. Literature has shown that, the most successful procurement systems are those that provide bidders a legal basis to challenge the actions of public procurement officials when they breach rules (Hunja, 2001). Furthermore, even where this provision is available the key issue that guarantees the integrity of the system is enforceability and precedence in dealing with those who breached the rules.

5.5 Institutional Enablers

Government has taken the important and necessary steps to encourage the blending of public-private resources through PPP by instituting an enabling legal instrument (J.V. Act Chapter 22.22) and providing the framework through the PPP Guidelines. However, it should be recognized that at the lower levels of Government such as rural district councils, town boards, and small urban towns it is difficult to initiate public-private-partnership type projects targeted to save the local communities. Creation and adequately capitalised dedicated financial institutions for infrastructure financing is a critical institutional enabler to facilitate blended infrastructure financing. In particular growth in asset base of institutional investors like pension funds and insurance companies necessitates the channelling of investable funds to long term infrastructure projects. Improving the governance of local authorities will improve the risk profiles of infrastructure projects implemented within their jurisdiction thus making projects in local authorities attractive to private investors who want to participate in infrastructure development projects at the lower levels of Government.

Government created the Infrastructure Development Bank of Zimbabwe (IDBZ), whose mandate is to mobilise funding for infrastructure development in the country. Huge infrastructure deficits at national level and within local authorities present opportunities for blending public and private sector funding to finance the provision of infrastructure. IDBZ can leverage the resources that it mobilises by entering

⁵⁵ However while this takeover took place in most of the local councils, Bulawayo City Council refused to hand over its facilities to the government up to today.

⁵⁶ While the intention of this clause is to protect national interest, there could be unintended effects arising from misapplication of the law in practice where it becomes a disincentive.

⁵⁷ See for instance The Standard ‘Indigenization: Public policy for private gain’ September 3, 2010.

into partnership/consortia with other private financiers particularly pension funds which are looking at growing their asset base. An adequately capitalised IDBZ can create innovative products or structuring of projects that respond to the diverse opportunities for infrastructure finance at both national and local authorities level.

Once IDBZ is adequately capitalised it can explore the opportunity to establish a limited liability fund to channel private capital into infrastructure projects. A venture capital (VC) business advisory board can provide technical advice, business guidance and links with up-line and down-line value chain players. The VC would earn an annual management fee to run the operation of the Fund and splits the profits between the entrepreneur, the investor and the fund manager.

According to Tyson (2011)⁵⁸, if properly designed and governed, such an infrastructure entity would overcome weaknesses in the current selection of projects by removing funding decisions from politically volatile appropriation processes. He further points out that it is common that projects are often funded on the basis of politics rather than efficiency. If lower level local authorities could borrow from a special entity that has access to funding from capital markets and banks this would improve the provision of services. The special entity would also assist in independently carrying out cost-benefit analysis and provide technical advice to the local authorities.

5.6. Governance issues

One of the major policy issues, which is also a governance issue, is that there is an opportunity for more resources from the National Social Security Authority (NSSA) to contribute more towards infrastructure financing. However, NSSA is not regulated by the regulator of nonbank financial institutions (IPEC), which has seen a lot of political interference and more discretion on the part of the line Minister on how resources from NSSA are to be invested. NSSA was created through an ACT of Parliament [Chapter 17:04] and enjoys certain privileges not enjoyed by other employee schemes. This implies that NSSA has a captive market and does not compete with similar organisations in attracting resources that it manages. Players in the sector highlighted the need to relook at the governance structure of NSSA in line with international best practices in order to unlock more resources for blending in infrastructure financing.

There is also a general lack of confidence among the private sector, with regards to the capacity within government and government related institutions to manage the design and implementation of complex infrastructure projects. Institutional investors who are the source of long-term funds expressed concern that they are not adequately consulted in the design of the instruments used to mobilise funds for infrastructure projects. Such consultations would have allowed the financial experts in the private sector to flag out some issues which would allow for negotiations on the conditions and terms of the financing facilities. For example, discussions with the Zimbabwe Association of Pension Funds (ZAPF) and IPEC, revealed that the uptake for most government-issued financial instruments for infrastructure development by pension schemes is low due to lingering fear that the funds would not be recovered due to mismanagement or diversion of the resources away from the intended infrastructure project. The private sector generally lacks confidence in the manner in which the projects would be governed by the public institutions as there is a perception that the poor governance at these institutions would affect profitability. As a result, involvement of the private sector in the governance of the infrastructure projects in which blending of resources would have been used would go a long way in instilling confidence. In this regard, giving the private sector equity in the project through the establishment of an SPV might help enhance confidence as they would be involved in management of the project as opposed to just subscribing to an infrastructure bond or advancing a loan to a public entity.

The manner in which politics has also been used to interfere with the profitability of infrastructure projects is also a critical issue which has been raised as needing to be addressed. Cancellation of bills owed by residents to local authorities by Government on the eve of the 2013 elections has been cited as a politically motivated directive. Local Authorities are owed large amounts of money with businesses and residents now owing the City of Harare in excess of US\$750 million. Strategies to improve settlements of rate payers' debts include discount offers of up to 50 percent payable within stipulated time frames, e.g. 90 days. Improving rate payers' payments will also necessitate improved service delivery, as often rate payers complain of being asked to pay for non-existent services, like fixed water charges where water supply is non-existent. Debt recovery strategies would need to also take account of this (Transitional Stabilisation Programme 2018.p. 76).

The scepticism that greeted the intentions of local authorities to introduce pre-paid water meters was also highlighted as an issue that undermine governance and service delivery by local authorities. Human rights advocates on the other hand highlighted that water was a basic right and therefore introducing pre-paid water meters would severely restrict access by very poor families⁵⁹. This notwithstanding, mobilising blended financing for water infrastructure would require ring fencing of water revenues for investors to recoup their investments. In this regard there is need to balance the rights and provision of guarantees of income streams from water infrastructure investments.

There have been reports in the public media of non-payment of water and electricity bills by politically connected individuals over the years.⁶⁰ While there may be very sensible reasons for a law restricting disconnections of consumers who fail to pay their bills, such as the

⁵⁸ Tyson L. D. 2011 'A better stimulus plan for the US economy' Harvard Business Review, 89(1/2); 53.

⁵⁹ Providing alternative sources of water prior to introducing water meters like boreholes could circumvent the risk of violating this basic human right. Furthermore, privatization of water supply has generally been resisted in many jurisdictions because it is politically unpalatable. I guess solution may lie in blended finance, accessing philanthropic, grants, PSIP and other concessional funding

⁶⁰ **Major councils owed \$1bn in unpaid bills:**

<https://www.herald.co.zw/major-councils-owed-1bn-in-unpaid-bills/>

principle that citizens should not be deprived access to essential services, this may stop the operators from having an effective weapon against bad debtors. Cancellation of owed bills by residents of local authorities coupled with non-payment of bills by the politically connected undermines viability of local authorities and their capacity to provide service. Consequently, impaired balance sheets of local authorities will further undermine their capacity to attract private partners to participate in blended financed infrastructure projects.

Lack of effective supervision under the current regulatory environment with regards to corporate governance and management of public sector enterprises has undermined investment in infrastructure developments. Weaknesses in governance and regulatory frameworks will further undermine initiatives to mobilise blended finance to address the infrastructure deficits that are prevalent in most sectors of the economy. In this regard strengthening the supervisory capacity of regulatory institutions, improving levels of accountability; enhancing co-ordination, synergies and flow of information among regulatory institutions, infrastructure project promoters/implementers and prospective financiers will improve the general environment to facilitate the growth of blended finance market in Zimbabwe. This entails addressing the skills and experience gaps within the regulatory institutions to better understand the nature of the business of the institutions under their purview.

It is also imperative for government to strengthen the legal framework by ensuring that matters to do with concessions, ownership and procurement systems are clearly spelt out in the country laws. For example the legal provision for the treatment of unsolicited bids need to be spelt out to enhance transparency in the process. Clarity of the legal provisions on unsolicited bids will promote private sector initiated proposals to partner with government/state owned enterprises in the delivery of infrastructure projects. The current initiative to craft the Zimbabwe Investment Development Authority Act presents an opportunity to deal with these issues. The Act should ensure that the legal provisions clearly spell out the responsibilities, division of power and coordination of the relevant institutions involved in promoting investment in infrastructure projects.

According to Hodges & Dellacha (2007),⁶¹ the most common systems that governments use to manage unsolicited proposals are commonly referred to as the “bonus system,” the “Swiss challenge system,” and the “best and final offer system.” The bonus system as used in Chile and Korea grants an advantage to the original project proponent in the form of a premium used in the bidding procedure. The “bonus,” usually between 5 percent and 10 percent, is credited to the original proponent’s bid in the open tender. The Swiss Challenge System – used in the Indian States of Andhra Pradesh and Gujarat, Italy, the Philippines and Taiwan – also allows third parties to compete but the original proponent is granted the right to counter-match the best offer and secure the contract. The best and final offer system used in Argentina and South Africa is similar to the Swiss challenge in approach, but only grants the original proponent the advantage of automatically competing in the final tendering round. Zimbabwe should consider providing guidelines for such standards in order to promote transparency and attract private sector participation in infrastructure projects.

5.5.1 Challenges Associated with the Investment Climate in Zimbabwe

It is fundamental to note that the laws are only as good and effective to the extent to which they are reasonably applied. Therefore it is important that the authorities follow through the dictates of the constitution and the laws in order to instil investor confidence. This is especially the case with regards to infrastructure investments given that they are long term in character.

Establishment of rights and title over and use of land is key to infrastructure projects where private service providers are investing in assets attached to such land. Private lenders often seek security over those assets. The Government will also be anxious to ensure that it is able to maintain title in public assets and obtain title to assets that it or the public is paying for over time. A system that is unreliable or does not afford protections to land users will discourage private sector investment and raise concerns for the Government.

One sticking issue which infrastructure investors often make reference to is the fast track land reform programme (FTLRP) in which agriculture related infrastructure was compulsorily acquired by the Government and yet the previous owners have not been compensated. Although the Government has been highlighting the need to provide compensation, budget limitations and scarcity of funds from other sources have not enabled this to happen. In the 2019 national budget \$53 million has been set aside for this purpose, but the figure is nowhere near being adequate given that the amount required is estimated to run into several billion dollars.

The compulsory acquisition of land under the fast track land reform programme infringed on the right to private property and disregarded some of the country’s bilateral investment protection and promotion agreements (BIPAs). This has affected the flow of ODA an important source of blended finance. For example, the EU and USAID have categorically stated that they will not fund projects that are located on “contested land”. This is highlighted in one of the EU project document on Zimbabwe where it is stated that the main reason for the protracted decline in agricultural production is the “unresolved issue of contested land, with unclear ownership and tenure, being the result of the agrarian reform undertaken in 2000”⁶². This means that ODA and other private investors will continue to shun channelling investments in the former commercial farming areas as long as the compensation issues to the former owners of the land have not been adequately resolved. The other issue of concern that has potential to militate against mobilisation of ODA for blended

Pay your council debts, Government tells residents

<http://www.newsdezimbabwe.co.uk/2018/01/pay-your-council-debts-govt-tells.html>

Councils plunge into crisis

<https://www.financialgazette.co.zw/councils-plunge-into-crisis/>

⁶¹ Hodges J. T. & G. Dellacha (2007), “Unsolicited Infrastructure Proposals: How Some Countries Introduce Competition and Transparency”, WORKING PAPER NO. 1, Public-Private Infrastructure Advisory Facility, World Bank

⁶² https://ec.europa.eu/europeaid/sites/devco/files/aap-supporting-zimbabwe-p4-integrated-program-af-20111130_en.pdf

infrastructure funding is the violation of the terms of some of the BIPPAS especially with regards to farm related investments. These developments have played a major part in shaping investor perception in the country, not only in agriculture but in all other sectors of the economy as well.

There has also been instances of enactment and enforcement of laws that undermined investor confidence over the years. A case in point is the Indigenisation and Economic Empowerment Act which was amended by Section 42 of the Finance Act (No.1, 2018). The implementation of Indigenisation and Economic Empowerment Act had caused significant discomfort among investors. Thus, a key lesson drawn from this experience is that the effectiveness of a law should not be judged by what it seeks to achieve, but by what it actually succeeds in achieving.

There have also been cases of intentional misinterpretation of the law by officials in order to unduly benefit from contracts. A good example of this is found in the provision of housing. According to the urban Councils Act (Chapter 29:15) Subsection 7, “*Any land reserved for State purposes, whether in terms of an approved town planning scheme or in terms of the approval of the Minister in terms of subparagraph (ii) of paragraph (a) of subsection (4), which is required for the purposes of a police station or school shall, upon the sale, exchange, lease, donation or other disposition of land in terms of this section and upon request of the Minister, at the cost of the council, be transferred to the President and the council shall not be entitled to any payment or compensation for any such land so transferred but shall be entitled to recover the costs incurred by the council in surveying such land: Provided that—*

(i) where the reservation is situated on township land granted to the council in trust for the inhabitants of the council area in terms of a deed which stipulates that a certain percentage of such township land shall be surrendered free of cost for State purposes, any land transferred to the President in terms of this subsection shall, if the balance of the percentage of land remaining is equal to or greater than the land transferred, be deducted from that percentage”.

However, in their interpretation of this provision successive Ministers of Local Government have specified that 10% of the land offered to housing developers should be left for the construction of public facilities such as schools, hospitals, recreation facilities, etc. The research was however informed that officials from the Ministry of Local Government misinterpreted this to mean that 10% of developed/ serviced stands must be ceded to the Government by the developers. According to the key informants this was done by officials who wanted to personally benefit from council housing projects.

There are concerns in the manner in which infrastructure projects are being managed. There is need for the private sector to be involved in the development of the financing instruments. Consultations are not being done with the players yet they are expected to provide funding for the projects. As a result, the needs of the private sector are not taken into account when crafting the instruments. When the paper comes into the market, it therefore tends to be unattractive. This explains why in cases where it is compulsory for pension schemes to finance, they will just take the barest minimum rather than showing desire to put more resources.

Consultations are important as they would allow the private sector to flag out some issues which would allow for negotiations on the conditions. It was highlighted by the Zimbabwe Association of Pension Funds (ZAPF) that they used to have such dialogues with the IDBZ in the past and these worked well. Dialogue would also give the necessary assurance and help allay any lingering fears. Proposed schemes such as ‘command housing’ may need broader consultations with all key stakeholders including institutional investors to enhance uptake. Such consultations should demonstrate the business case of the proposed schemes as well as the integrity of the governance framework in order to build confidence in the providers of blended finance.

Operators of infrastructure projects and any other investors or lenders will want to ensure the stability of income from blended finance infrastructure projects and, where relevant, the expected return on capital and new investment. If the income is coming from a single off-taker, such as the government or a utility, then the legal issues associated with the revenue stream may be limited. More complex issues arise where the operator or project or company collects revenues directly from customers.

The research established the mechanisms involved in the setting of utility tariffs. According to key informant at ZERA, once tariffs are approved by ZERA they have to be implemented as is, for example prices of diesel, petrol, electricity etc. The operators have got to apply for a review of the prices if they want these to be changed (increased). They should provide reasons and justifications for the proposed changes. There is a Tariff Code in the electricity sector which gives guidelines on what should trigger price/tariff increases and the processes to be followed. The Code also recognizes the differences in types of technologies, for example, solar powered versus coal versus hydro generated electricity. The same situation applies to other sectors such as ICT and water and sanitation. According to the ZERA the tariff model is agreed with the operator from the stage of the development of the project proposal. There are also no restrictions prohibiting the operator as a private entity from collecting tariffs from consumers. The project company is also entitled to disconnect or convert illegal connections.

5.7 Capacity Issues

Stakeholders also believe that capacity issues generally explain why there are few infrastructure projects being undertaken involving the private sector. Limited capacity within the infrastructure project promoters to undertake feasibility studies means the project ideas are not developed to bankability. It also emerged that the limited number of projects with updated feasibility studies is due to lack of capacity among the project promoters/owners to develop the projects from project concept to a bankable project. Ideally Government should provide adequate funding to finance feasibility studies for its solicited projects, and then invite bidders who would use government funded feasibility studies. It emerged from discussions at the inception workshop that some projects where feasibility studies were done

a long time ago have not been updated due to capacity issues. Furthermore, institutions like IDBZ should have a well-resourced Project Preparation/Development Fund to develop a pipeline of well packaged bankable projects that will be used to mobilise blended funding and facilitate project implementation. In its re-engagement efforts Government can also mobilise funds from the development partners to build capacity for project preparation/development within the country.

It was also raised during the inception workshop that university infrastructure projects where feasibility studies exist are gathering dust without being considered for funding. This is an area that IDBZ needs to consider and understand the inhibiting factors.

Chapter 6. Opportunities for Blending in Infrastructure Funding

The schematic diagram (Figure 22) shows opportunities for possible collaborative relationship that can be forged between IDBZ and a diverse set of institutions in mobilising resources for blended infrastructure financing. Line Ministries and State Owned Enterprises with mandates to put up infrastructure be it in Energy; Power, ICT; Water etc; Local Authorities; Universities all have infrastructure gaps and project ideas that have to be developed to bankability and packaged to solicit for funding from prospective financiers. Blended finance in this regard can be used to reduce the gap between real and perceived risks, thus making it possible to crowd in commercial investors.

Figure 22: opportunities for possible collaborative relationship



Prospective funders include Institutional Investors (Pension Funds and Insurance Companies); Banks; Development Partners (with concessional funding); Impact Investors (who may include high net worth individuals; corporate foundations; non-governmental organisation) among others. For example, Impact investors whose investment philosophy is guided by the desire to make an impact can be targeted to provide guarantees or first loss capital in water and sanitation infrastructure projects whose desired impact might be improving access to clean water to the generality of the population.

The re-engagement initiatives being undertaken by government will also open up opportunities for bilateral grants focused on infrastructure and presence of well-resourced development agencies running programs in the country. The re-engagement and full implementation of the debt and arrears clearance programme will also create opportunities to mobilise concessional funds/grants; impact investment funds; commercial capital and public (both local and international) funds which are all critical ingredients for the growth of the blended finance market in the country. The existence of infrastructure development gaps presents immense opportunities for mobilising blended infrastructure finance from investors who are looking for high impact; high return or some combination of both.

6.1. Unlocking developmental finance from the IFIs

International finance Institutions like the World Bank (WB), African Development Bank (AfDB) and European Investment Bank (EIB) provide long term funding for infrastructure development through various: grants. The International Finance Corporation an affiliate of the World Bank can participate via the equity route. The government's re-engagement and the arrears clearance processes is a key

pre-requisite to accessing new funding from the IFIs. In particular the mobilised funds from IFIs can be used to boost the projects preparation funds which will be used to finance feasibility studies and develop a pipeline of bankable projects which will be used to attract private sector participation in infrastructure projects. Opportunities for gap funding and provision of guarantees from IFIs also exist.

6.2. Access local institutional investor base (pension funds & insurance companies)

Zimbabwe has a fairly established and stable institutional investor base (pension funds and insurance companies) with an estimated asset base of US\$2.7 billion. The large component of these institutions' liabilities which are long term, match the funding tenor of most infrastructure funding requirements. There is an opportunity to access these funds either directly (equity or loans) or indirectly (through issuance of interest bearing instruments/bonds). This channel of financing would be significantly improved as the reform of the Public Civil Servants pay-as-you-go scheme is converted into a fully funded scheme as stated in the Budget Statement of 2019. During the field interviews, institutional investors indicated that they can participate in infrastructure bonds/instruments provided the instruments satisfy the prescribed asset requirements. Active involvement of institutional investors in the blended finance market may require a change in the modus operandi, from an intermediary to a collaborative model that is being suggested in Figure 22.

6.3. Opportunities for Recapitalizing IDBZ

As noted earlier IDBZ has developed a roadmap that seeks to achieve a capitalisation level of US\$250 million by 2018 by attracting international and regional shareholders to dilute Government shareholding. This thrust has been buttressed by the policy decision by Government to partially privatise IDBZ as part of the Transitional Stabilisation Programme (TSP). Capitalisation of IDBZ is a critical pre-requisite for the IDBZ to mobilise blended funding for infrastructure development. The recapitalisation and repositioning of IDBZ may entail bringing in strategic institutional investors to inject new capital into the Bank, restructuring the Bank and building the necessary technical base to fully perform the role of an infrastructure bank.

For a development finance institution (DFI) such as the IDBZ, resource Mobilisation is a critical operation that should focus on bank-wide funding requirements in order to enhance the Bank's capacity to fund infrastructure projects whilst also addressing funding requirements for all the Bank's operations. Other DFIs pursue a holistic approach to resource mobilisation aimed at building balance sheet capacity, with resource allocation to infrastructure projects, corporate lending (trade finance) and treasury investments being a secondary consideration. Examples of such DFIs that are in the infrastructure space include the African Development Bank (AfDB), Development Bank of Southern Africa (DBSA) and Islamic Development Bank (IDB)⁶³.

IDBZ's resource mobilisation efforts are currently being constrained due to the following reasons:

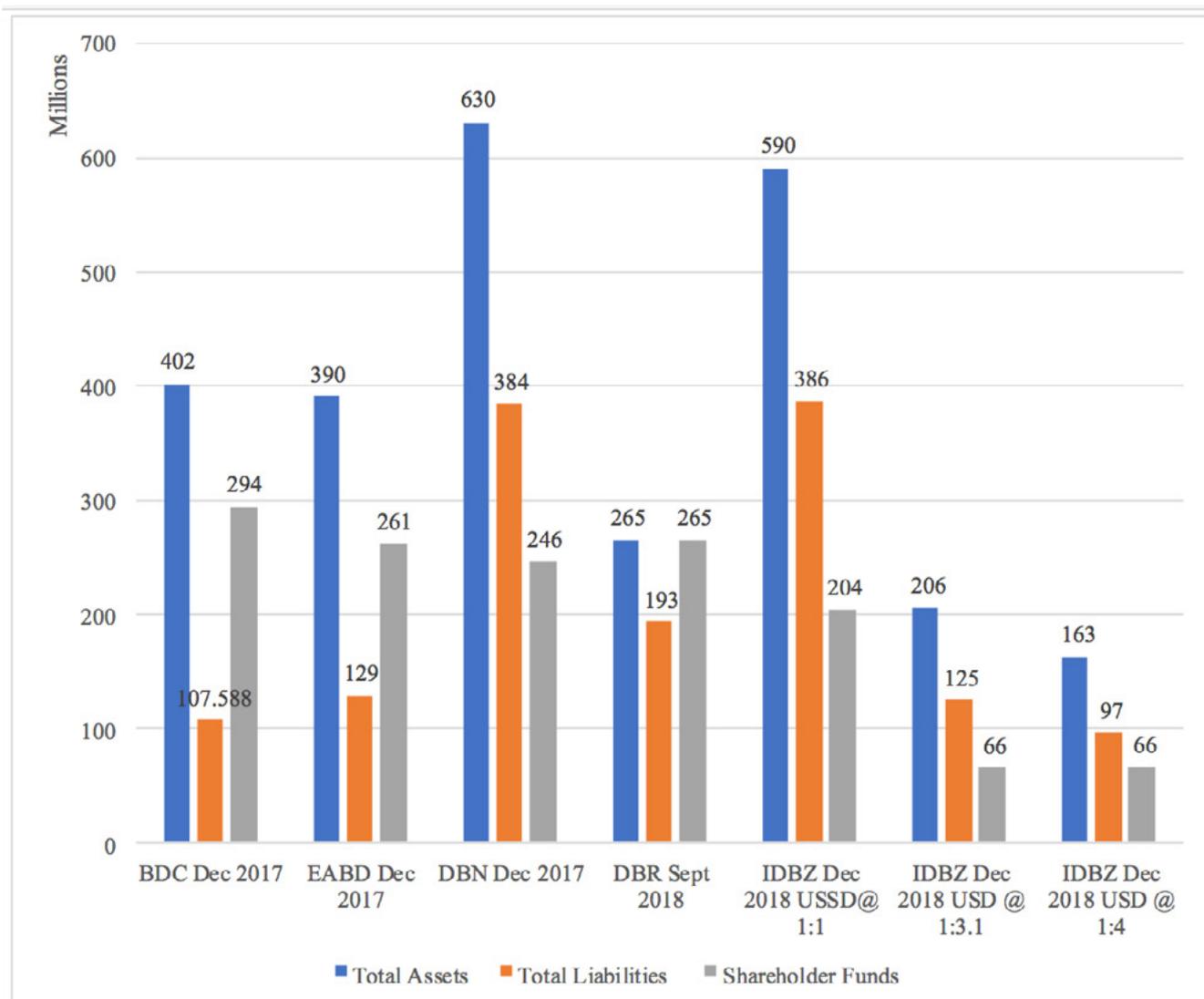
- lack of capacity to co-finance projects - without IDBZ contributing its own capital into the financing of projects as a de-risking mechanism, investors/financiers are showing limited confidence in the bank-promoted projects; and
- investors and providers of debt/lines of credit consider the issuer or borrower's balance sheet size when making investment decisions.

Figure 23 below shows the balance sheets of regional development banks and the figures show that IDBZ was the least capitalised when compared with the other four. In the context of the scale of funding required to close the infrastructure deficits in the country, the IDBZ is grossly undercapitalized. This level of capitalization also limits the Bank's capacity/ability to attract substantial volumes of blended finance for deployment towards priority infrastructure projects.

A comparison between IDBZ and selected regional and national development banks in the region reveals that IDBZ is not adequately capitalized to fulfil its mandate. This is despite the fact that as at December 2018, IDBZ's capitalization levels was almost similar to that of Development Bank of Namibia (DBN), the most capitalised development bank among selected development banks (Figure 23). IDBZ's asset value of US\$590 million in December 2018 was very close to DBN's US\$630 million and the shareholders' equity value of US\$204 million was slightly less than that of DBN which had US\$246 million. IDBZ's balance sheet was stronger than that of Botswana Development Corporation (BDC), East African Development Bank (EADB) and Development Bank of Rwanda (DBR) following the Government of Zimbabwe's recapitalization with US\$150 million in August 2018. The introduction of the RTGS dollar through the Monetary Policy Statement presented in February 2019 weakened IDBZ's balance sheet through introduction of an official exchange rate of US\$1: RTGS\$2.5, which would subsequently be determined by market forces through the interbank rate system. As end of March 2019 the interbank exchange rate depreciated to US\$1: RTGS\$3.1 which resulted in the loss of value of assets and shareholders' equity by about 65.1%, 67.4% to US\$205.9 million and US\$65.8 million respectively. However, taking into account the parallel market exchange rate of US\$1: RTGS\$4 recorded in March 2019, it further weakens the balance sheets of IDBZ. Hence, IDBZ remains one of the least capitalised development banks at a time when Zimbabwe has backlog of infrastructure projects which are critical in order for the country to realise the Vision 2030 of becoming an upper middle-income economy by 2030. This shows that IDBZ requires an injection of more capital to strengthen its balance sheet to facilitate the Bank to adequately fulfil its mandate.

⁶³ See IDBZ "Refined Resource Mobilisation Strategy", produced by the Resource Mobilisation Division 2016 for more details.

Figure 23: IDBZ's capitalisation levels compared to selected other development banks in other countries⁶⁴



Source: Various Financial and Annual Reports of Development Banks

Key:

- BDC - Botswana Development Corporation
- EADB - East African Development Bank
- DBN - Development Bank of Namibia
- DBR - Development Bank of Rwanda

The infrastructure deficits in the country and the country’s desire to achieve Vision 2030 present huge opportunities for long term investors looking for a return provided the business operating environment is conducive. This reality provides a rational basis for favourable consideration by the policy makers to implement the proposed capitalisation strategy and road map for IDBZ.

6.4. Listing IDBZ on the Zimbabwe stock exchange.

Within the context of partial privatisation as enunciated in the TSP, IDBZ can start by exploring a capitalisation strategy that involves strategic partnerships with like-minded institutions as the risk-return profile for Development Finance Institutions (DFIs) might not be aligned to what the general investor looks at. Listing on the stock exchange is also an option that can be considered for capitalisation of IDBZ. The advantage of listing is that it normally leads to more efficient use of resources by minimizing the costs of production, as well as monitoring, assessing and controlling managers’ performance. Listing on the stock exchange also generally unlocks value of the company thereby generating additional resources.

IDBZ was primarily set up as a vehicle for the promotion of economic development and growth, and improvement of the living standards of Zimbabweans through the development of infrastructure⁶⁵. This infrastructure includes but not limited to energy, transport, water and sanitation, ITC and housing. The Bank is also enjoined to develop institutional capacity in undertakings and enterprises involved in infrastructure development in Zimbabwe (IDBZ Act (Chapter 24:14). The Bank, therefore, operates primarily as an infrastructure

⁶⁴ Ruling exchange rates used to convert values reported in local currency for Botswana, Namibia and Rwanda was retrieved from <https://www.xe.com>

⁶⁵ <https://www.idbz.co.zw/about-us>

development finance institution (DFI). Given the thrust of the major shareholder, Government, which is developmental, it may be difficult for IDBZ to list on the stock exchange as achievement of social developmental goals may not be consistent with profit maximisation goals. However, if IDBZ is restructured to become strictly an infrastructure fund (organisation) then they may have scope for considering listing on the ZSE to unlock value. There are many examples of infrastructure companies the world over which are listed on various stock exchanges such as Siemens, General Electric, Lazard Global, etc.⁶⁶.

Alternatively, IDBZ may not have to directly list itself, but it can arrange Special Purpose Vehicles bonds or pools of projects and list them on the stock exchange on their own merit. Such bonds or pools of projects will have to be rated by credible rating agents and their cash flows ring-fenced to repay the bond. Potential greenfield projects in health, transport and in utilities would qualify for such listing.

6.5. Ratings by Regional and Global Credit Rating Agencies

The IDBZ currently enjoys a good rating by peer regional development banks using PSGRS system. However, there is a good opportunity for the bank to be rated by a credit rating agency such as the Global Rating Company initially, and later by the likes of Moodys, Fitch and Standard and Poor. These ratings will improve the credit rating of the Bank and open channels to access global funding.

6.6. Funding Opportunities some Critical issues to consider

1. The issue of engaging the local institutional investors is very critical for both expanding the base (reform of the government employee pension fund) and encouraging the use of local currency funding mechanism. In a way issuing instruments in local currency (RTGS\$) minimizes the exchange rate risk and this needs to be considered within the context of the currency reforms being pursued by Government. However, to be attractive, local instruments will have to be indexed to inflation.
2. The IDBZ should engage bilateral and multilateral development finance agencies to mobilize long term lines of credit, inflation hedging tools and sovereign credit enhancements;
3. Consideration can be made to explore support to secure long term financing supported by the World Bank Partial Guarantee Program (WBPGP) as government pursues the Arrears clearance program. If this option is available or whenever it will be available the IDBZ through the Government should endeavor to access this facility as it reduces the cost of project finance;
4. Experiences from global trends have shown that the private sector is best suited to bring efficiency and capital. Going forward, IDBZ should work on strategies and initiatives to crowd in private sector funding dedicated to infrastructure development. To achieve this objective it is important to:
 - i. Mitigate foreign exchange related risks by encouraging the participation of local private sector. However, when regional and international private sectors participate in these projects (and foreign exchange risk is unavoidable) hedging strategies should be employed to minimize the impact of currency risk.
 - ii. Reduce risk by credit profiling – i.e. obtain guarantees, letters of credit from international banks, good international rating, and investment by international organisations such as the IFC. These credit enhancements will open up access to international financing and also reduce the cost of accessing finance.
 - iii. Deepen institutional investor pool in Zimbabwe i.e. pension funds, insurance companies especially life policy among others. Zimbabwe is already endowed with a good base of industry based pension schemes such as the Mining Industry Pension Scheme, the Local Authorities Pension Scheme, the National Railways of Zimbabwe Pension Scheme, etc. combined with a fairly diversified insurance industry comprising of life insurers (8), short-term insurers (25) and re-insurers (9). There is also a good number of asset managers (15), stockbrokers, dealers and the National Social Security Authority (NSSA). If the Government Employees Pay-As-You-Go pension scheme is reformed and funded the local financial markets will greatly be deepened providing a diversified menu of financial instruments to be accessed for infrastructure financing.
 - iv. Leverage on the capacity local authorities to mobilize funds for infrastructure development- in the past the large municipalities such as City of Harare, City of Bulawayo, City of Gweru and City of Mutare had the capacity to access finance through loans and issuance of municipal bills and bonds on the strength of their credit rating (rated by international rating agencies such as Global Credit Rating Company (GCR)). There is room for local authorities to regain this status and in partnership with infrastructure development parastatals such as ZINARA, ZINWA, ZESA, POTRAZ, etc. and IDBZ collaborate in mobilizing funds for infrastructure development. Furthermore, the credit standing of local authorities and infrastructure parastatals can be enhanced to allow them to access funding in their own rights. This backstopping will greatly complement the efforts of the IDBZ in accessing finance for infrastructure development.
 - v. Introduce inflation adjusted/indexed instruments. This will protect the investors against volatile inflation given that the tenors for infrastructure investments are long term.

⁶⁶ There are certainly a lot of global companies whose specific objectives are to finance infrastructure. In India there are 34 such companies of which the top 4 are Larsen (Cap Rs 182,309.67), Adani Ports (Cap Rs 68,910.92), Siemens (Cap Rs 37,355.09) and ABB India (Cap Rs 26,765.09). Elsewhere, we have Lazard Global listed Portfolio that invests in long term, defensive low volatility infrastructure companies with min mkt cap of US\$250 million.

The IDBZ can continue to use the existing funding models (i.e.-subventions from government, use of own balance sheet to issue interest bearing instruments) which are diverse and still relevant and/or consider alternative and innovative (incremental) infrastructure funding models for the rehabilitation and expansion of infrastructure to meet the challenges presented by the current and growing imbalances between the supply of and demand for the various infrastructures in Zimbabwe. New and modified funding models could take the form of one or a combination of the following:

Existing Funding Models

- i. Funding by the Consolidated Revenue Fund (on budget);
- ii. Funding through grants (various grants provided – through municipalities, conditional grants from the Consolidated Revenue Fund (on-budget);
- iii. Funding through the development of a tariff model (via balance sheet). Innovative tariff models, for example, can be used by city councils to develop physical infrastructure, say housing infrastructure, by setting a building tariff or strategic land infrastructure contract. Once developers have agreed to pay standardised contributions per residential dwelling and per hectare of commercial land using the legal framework, the city council can use the strength of its balance sheet to borrow money from homes and communities agencies ((building societies) to prefund infrastructure against expected tariff receipts. Under such tariff models, developers pay, say 75% of the charge on completion rather than upfront thus reducing their need for borrowing and allowing for greater certainty for all parties.

New paradigm – Alternative and Innovative (incremental) Infrastructure funding models:

- i. Fund raising on financial markets (off- budget) – requires instruments enhancement through tax incentives and prescribed asset status, credit enhancement through the rating of the issuer or rating of the instrument itself;
- ii. Funding through public-private partnerships (PPPs) hybrid of on-and off-budget) – this can include equity placement, issuing of instruments such as bonds, ODA support, government guarantees, etc.;
- iii. Funding from private sector markets i.e. fixed income (loans, bonds), mixed (hybrid of subordinated loans/bonds, mezzanine finance and these could be in the form of build own operate-transfer schemes;

The study has already discussed and encouraged the deepening of the financial markets mainly through the reform of the pension fund and insurance companies industry in order to diversify the investor base. An alternative is to involve superannuation pension funds, insurers and other financial institutions by encouraging them to set infrastructure oriented funds which provide funding for infrastructure projects which can leveraged on to mobilise blended finance. The advantage of the superannuation funds is that their liabilities are long term in nature and so naturally match with the long term inflation indexed returns of many infrastructure projects. Table 10 is an attempt to suggest some of the options available to the country in funding infrastructure projects.

Table 10: Options for funding Infrastructure Projects in Zimbabwe

Options	
Infrastructure Debt Funds	<p>The idea is to entice the local institutional investors, government entities and international institutions contribute to setting up debt fund. This Fund should have a target amount to be raised. The Fund's aims should be to invest in subordinated debt with a 4–7 year tenor. It's target sectors should be regulated utilities (water, electricity), transport (airports, toll roads, ports), ICT and social infrastructure.</p> <p>The Government (Joint Venture Unit)/Securities Exchange of Zimbabwe Board should prepare guidelines to facilitate the creation of infrastructure debt funds.</p>
Infrastructure Investment Platforms	<p>The Government can sign MOUs with the National Association of Pension Funds and Life Offices Association of Zimbabwe to set up an investment platform to facilitate investment in infrastructure by pension funds and insurers and call it the Pension and Insurance Infrastructure Plan (PIIP). This will address the relative lack of experience of the institutional investors in infrastructure investment. The PIIP can invest both in equity but primarily debt investments. The end aim is to increase pension fund allocation to infrastructure to a target percentage</p>
Specialist Infrastructure Investment Funds	<p>At the moment, there are a few dedicated funds in housing and one at IDBZ for project feasibility studies. The idea is to have specialist infrastructure fund managers that focus on blended infrastructure investment. However due to the lower level of risk taken on by equity investors in availability type PPP structures, debt levels tend to be very high and equity only represents a small proportion of overall financing. Experience in other countries has shown that IRR returns from these financial investors range from 10% for secondary assets to mid-teens for primary assets (with construction risk).</p>
Infrastructure Trusts	<p>Infrastructure trusts aim to facilitate identification, management and investment of major projects in the country or regions. In fact, this is where the IDBZ Fund belongs.</p>

Chapter 7. Recommendations and Conclusion

7.1. Recommendations

1. Blending of private and public funding for infrastructure development requires a conducive legal, policy and institutional environment which entail:

Fiscal and Monetary Policy Environment

The study observed that the Reserve Bank overdraft facility availed to Government has been flouted many times in violation of the statutory borrowing limits as per the RBZ Act [Chapter 22:15] section 11 (a) that states that the “Bank shall not lend or advance moneys directly to or buy, discount, rediscount bills, in excess 20% of the previous year’s ordinary revenue of the State”. The violation reflects an institutional weakness and lack of independence by the Reserve Bank. Improving coordination between the Monetary Authorities and the Fiscal Authorities will:

- Foster and reinforce policy consistency;
- Enhance adherence to fiscal rules to ensure that excessive government expenditure does not fuel inflation which in turn erodes value of funds particularly RTGSS\$ earmarked for blended infrastructure funding;
- Ensure Central bank independence to enforce Government borrowing limits as set out in the RBZ Act and strengthening the role of oversight institutions like Parliament which is critical in this regard.
- Addressing the unsustainable budget deficit which has been funded by borrowing from the domestic financial sector mainly through issuance of Treasury Bills (TBs) thus crowding out private sector borrowers thereby weakening the key pillar of prudent macroeconomic management.

Prudent macroeconomic management fosters:

- Stability of the financial system-maintenance of low and stable inflation. High inflation reduces the appetite for fixed income securities and increased demand for listed equities as investors seek a hedge against rising inflation. This has negative implications on expected returns on Infrastructure Bonds and/or infrastructure projects. Improving the soundness of the financial sector will improve liquidity in the market and build confidence of the public which facilitates mobilization of domestic savings especially at the long end of the market which can be used for financing infrastructure projects.
- Stability and predictability of exchange rates in the medium to long term in line with the gestation period of infrastructure projects is very important. The recently introduced interbank foreign exchange market though good in principle still needs to be transparent (show volumes of trade) and main transactors. In the absence of abundant foreign exchange the exchange rate can be subject to very wide fluctuations. Hence, at this early stage the system should be closely monitored.
- Building of international reserves which needs Government to vigorously pursue an export oriented strategy to expand exports combined with an inward looking import substitution strategy. This will reduce the trade deficit and stabilize foreign currency availability which helps to avert currency risks.
- Rebalancing the budget with respect to the sharing of resources between the capital budget (the bulk of which should go to infrastructure funding) and the recurrent budget. In the past scales were tilted towards recurrent expenditure. A budget surplus has been recorded in January 2019, which is a positive development and good news for project sponsors in terms of signaling government’s intentions to maintain fiscal stability if it can be sustained Government now has the opportunity that if it borrows the funds will have to be directed towards investment (PSIP) instead of consumption. This will avert the current under allocation for capital expenditure leading to under investment in infrastructure development.
- Stability in the funding of critical imports and discouraging importation of luxury goods, and more importantly mobilizing and building international reserves to ensure stability in the newly created interbank foreign exchange market.
- Debt and arrears clearance: The debt burden facing the country is a double edged sword for the Government in that both domestic debt and external debt are now at very high and unsustainable levels of 39.0% and 31.3% of GDP, respectively. External debt is limiting access to critical development funding from major creditors while domestic debt is contributing to the crowding out of the private sector. There is need, therefore, to resolve the huge debt overhang in order to unlock the key developmental finance through re-engagement of the international community and to carry out fiscal consolidation which is a policy aimed at reducing government deficits and debt accumulation.

Institutional Strengthening

The study observed the need to strengthen institutions responsible for Infrastructure development with the requisite capacity to initiate infrastructure projects which IDBZ would leverage on to mobilize blended finance. The areas that require institutional strengthening initiatives include:

- Strengthening the design; implementation and management of complex infrastructure projects within government and government related institutions that play key roles in the infrastructure value chain;
- Deepening financial market by creating an environment that facilitates mobilization of long term savings through the pension, insurance and other savings industry. Already there exist some industry based pension schemes, corporate based pension

schemes and NASA as good pillars for the mobilization of long term savings. A fully funded government pension scheme in the realm of the South African Government Employee Pension Fund (GEPF) will become a major source for blended infrastructure funding.

- Diversification of the financial markets: The Central Bank should come up with a five year Strategy (package of policies) for developing a diversified and deep financial market. There is need for different types of players with diverse skills i.e. stockbrokers; banks (provide direct loans and issuance of instruments which match liability profiles); ZSE- listing of bonds on the stock exchanges; diversified instruments in the market- having different types of instruments trading at different times thus facilitating a liquid market. This should be accompanied by skills (people who understand the business; traders of financial instruments with capacity to price these instruments) and institutions to regulate the financial sector manned by professional people with practical market experience.
- Consolidation of Treasury Bills and Bonds into few larger bonds that will be allowed to trade transparently and eventually embark on establishing a benchmark bond⁶⁷. Treasury bills and Treasury bonds in the market are currently fragmented and some of them too small and not trading in the secondary market. In the TSP government pronounced that future issuances of treasury Bills and Bonds should be advertised, bids openly invited and the allocation done through an auction system. This will allow for proper “price discovery” and transparency.
- State Enterprises with potential capacity to issue bonds such as ZPC, ZINARA, ZINWA among others should draw lessons from institutions like Eskom (the integrated power corporation) of South Africa which has a good track record of issuing bonds in local Rand currency and also in Euro and US dollars. The other good example is the South African National Roads Agency (SANRAL) which also has a track record of bond issuance. These entities would then co-invest in infrastructure with the IDBZ in their respective mandated areas. However, for these entities to be able to issue paper on their own account there is some serious need to revamp their credit worthiness, governance structures and management.
- Adherence to good corporate governance and management practices in public sector enterprises will improve the performance of these entities which in turn strengthens their balance sheets and capacity to mobilize blended financing for infrastructure projects they superintend.
- Ring-fencing infrastructure project income streams: This mechanism will instil confidence in infrastructure financing and encourage blending of pension funds and public funds as they will be guaranteed of infrastructure project incomes streams and viability of the infrastructure projects. For example, if it is the financing of road infrastructure, reserved tollgate can be ring-fenced to pay back rather than putting the resources in a consolidated fund.
- Leveraging on the opportunities for possible collaborative relationships with a diverse set of institutions in the country to mobilize resources for blended infrastructure financing. Capacity of IDBZ to effectively leverage of these opportunities entails:
 - Full implementation of IDBZ roadmap to achieve a capitalisation level of US\$250 million by 2018 through attracting international and regional shareholders to dilute Government shareholding;
 - Improving the capacity of IDBZ to co-finance projects - without IDBZ contributing its own capital into the financing of projects as a de-risking mechanism, investors/financiers will show limited confidence in the bank-promoted projects;
 - Reposition IDBZ as a vibrant infrastructure bank that has capacity to mobilise resources and make significant interventions to catalyze investment in infrastructure development in the country;
 - IDBZ should explore the funding opportunities and options for funding Infrastructure Projects in Zimbabwe discussed in section 6.6 of the paper.
 - IDBZ needs to develop a product to harness University infrastructure projects where feasibility studies exist and are gathering dust without being considered for funding;
 - IDBZ in partnership with Infrastructure project promoters should mobilise resources and technical assistance expertise to enhance capacity/knowledge in dealing with some of the intricacies of infrastructure projects. Facilitating blended finance projects requires certain human skills across the whole value chain i.e. project identification, feasibility study preparation, procurement, design and execution, tender evaluations, contract negotiation and project implementation. Notwithstanding the existence of these skills in the country, there are still some gaps on the nodes of the value chain with respect to the skills needed where continuous training programmes across the board would certainly enhance the skills.
 - IDBZ advocating that (i) infrastructure projects are granted the prescribed asset status and (ii) that a certain percentage of the ratios is set aside for infrastructure projects.

Regulatory and Legislative Environment

- The Constitution has the pillars to protect private investment, including infrastructure related investments (see Section 71 subsection (3) and Section 72). It is recommended that all Acts of Parliament that violate the nation’s Constitution be amended and aligned with it.
- Contrary to the good legal parameters of the national Constitution, citations of cases such as the violation and disregard of the BIPPAs, the Indigenization and Empowerment Act before it was amended⁶⁸ and the transfer of assets at the local entity level without compensation suggested weak implementation and mere disregard of the legal framework. Restoration of violated BIPPAs and/or compensation of beneficiaries will remove uncertainty with regards to the country’s commitment to upholding

⁶⁷ A benchmark bond is a bond that provides a standard against which the performance of other bonds can be measured. Government bonds of specified maturities e.g. 5 year, 7 years, 10 years are almost always used as benchmark bonds.

⁶⁸ The Indigenization and Empowerment Act was amended by Act, 2018 (No. 1 of 2018) which was published as law in the Zimbabwean Government Gazette Extraordinary dated 14th March 2018 due to contestations raised by investors.

the rule of law, increase investor confidence in the economy, unlock ODA capital and private capital from countries which have BIPAs with Zimbabwe.

- Expediting harmonization of secondary pieces of legislation (Joint Ventures Act (Chapter 22:22), the Special Economic Zones Act (Chapter 14:34) and the Zimbabwe Investment Authority Act (Chapter 14:30)) through the enactment of the Zimbabwe Investment Development Authority (ZIDA) Act will enhance efficiency and remove unnecessary delays in the implementation of infrastructure projects. Furthermore, ZIDA must be a streamlined and lean entity, manned by professionals with the requisite skills and experience.
- Zimbabwe should consider adopting legal provisions for the treatment of unsolicited bids submitted by private companies. Such provisions promote transparency and attract private sector participation in infrastructure projects particularly at the feasibility level. Lessons can be drawn from legal provisions on unsolicited bids in line with the most common systems that other governments use to manage unsolicited proposals (i.e. bonus system; Swiss challenge system and best and final offer system (see section 5.6)).
- There is need to provide clarity on compensation mechanisms when transfer of assets particularly infrastructure previously developed, owned and operated by local authorities is being transferred to new public entities created specifically to deal with a particular infrastructure to avoid undermining initiative to mobilise blended infrastructure funding by these entities.
- Adherence to the provisions of Public Procurement and Disposal of Public Assets Act [Chapter 22:23] will plug loopholes for corrupt practices including the right to review when public entities breach the procurement rules.
- Addressing challenges related to transferrable title on agricultural land will increase land agricultural infrastructure projects i.e. dams and irrigation infrastructure. This will encourage long term infrastructural investments on land and allows economic agents and investors to use land as collateral security for borrowing for further investments on farms.
- The National Social Security Authority (NSSA) has been given certain privileges not enjoyed by other pension schemes such as being given a captive inflow of pension contributions and operating outside the regulation and supervision of IPEC. First, it is recommended that it be placed under the supervision of the non-bank supervisor, IPEC. Second, there is an opportunity to prescribe that a certain percentage of the funds under NSSA management be invested in infrastructure.

2: Possible options/strategies to leverage on Official Development Assistance (ODA) to facilitate the blending of private interest-bearing instruments and grants

- Re-engagement and arrears clearance will create a conducive environment for mobilizing blended finance;
- The IDBZ should take advantage of the multi-donor trust fund model (i.e. ZIMFUND and ZIMREF) concessional finance and leverage on them to mobilise more blended finance from the private sector for the same purpose;
- The IDBZ can grow/expand the project development fund which is currently aimed at carrying out feasibility studies to include other aspects such as covering part of the project start-up costs.
- The IDBZ must consider setting up an IDBZ Infrastructure Fund in the realm of IFC's Blended Climate Finance (BCF) by mobilizing concessional funding from donors which can be used to crowd in private and public sector funding for infrastructure projects in specific areas including infrastructure for SMEs.
- Some of the sticking issues that are affecting the mobilization of ODA include but not limited to the following:-
 - Lack of compensation of previous farm owners for land/properties acquired by government under the fast track land reform programme (FTLRP)-this has militated against mobilization of ODA funding to support agricultural related investment including agro-infrastructure development;
 - Lack of compliance with the signed Bilateral Investment Promotion and Protection Agreements;

The rising inflation has turned returns including infrastructure project negative and increased both interest rate and exchange rate risks making it difficult to entice ODA concessional finance into the country.

7.2. Conclusions

A review of the global and regional experiences show that blending of public and private sector resources for infrastructure funding is increasing especially in line with the resolution of the Third International Conference on Financing for Development in July 2015⁶⁹. For example, data released by DFI Working Group in October 2018 shows tremendous uptake in private sector blended concessional finance for new projects to the tune of US\$8.8 billion in 2017. Furthermore, a common thread running through all the Global Infrastructure Investment Funds and Platforms funds is the ability to mobilise additional blending funds mainly from institutional investors and other interested investors.

Regional experience shows that having laws and policies is not enough as this needs to be complemented by increased human resource capacity; improved market confidence and reduced risk profiles for the initiatives concerned. The study has also established that there is scope for issuing infrastructure bonds, provided there is an improvement from the current approach, where government bonds are issued with a promise to spend the money in infrastructure investment, with no income stream associated with the underlying asset. This results in cash flows for the bonds being paid directly out of government tax revenues. Furthermore, the bonds that are issued as infrastructure bonds have no guarantee that the money raised goes into the project as promised, and neither is there a dedicated Fund Manager.

Case studies reviewed in Zimbabwe show that most projects were funded through public procurement. Infrastructure funding is also undermined by skewed structure of the government budget in favour of recurrent expenditure at the expense of capital expenditure.

⁶⁹ See http://www.un.org/en/development/desa/population/migration/generalassembly/docs/globalcompact/A_RES_69_313.pdf

However, the need to address the country's infrastructure deficits requires huge capital injection. Thus, the initiatives to close the infrastructure deficits present opportunities for exploring innovative blended infrastructure funding models. Some of the infrastructure particularly in the water and sanitation has been funded through pooling of donor funds. In this regard there is opportunity for IDBZ to leverage on multi-donor funds to mobilise more funds for the same cause. The study also identified opportunities for possible collaborative relationships that can be forged between IDBZ and a diverse set of institutions (including government institutional investors, donors, infrastructure project promoters etc.) in mobilising resources for blended infrastructure financing.

The study also established that while there is scope to get funding from pension funds and insurance firms, the hyperinflation environment has left them now more reluctant. Instruments used, including bonds, need to be inflation indexed to be attractive. This applies especially where fixed income instruments are used. In addition, due to loss of confidence in the implementation and management capacity for complex infrastructure projects within government in general and some state owned enterprises, insurance and pension funds are willing to participate as consortiums provided they also participate in the management of the projects. Some of the projects amenable to equity participation include energy and housing projects. Where SPVs are created to run or manage the projects, they would prefer taking up equity in the SPV rather than just releasing money without any oversight on how it is used.

Review of global and regional experiences revealed that a comprehensive and effective legal system; adequate protection of property and creditor rights; and a reliable, efficient and independent justice system are essential for the participation of the private sector and ODA in infrastructure development. Zimbabwe has a window of opportunity to address the identified flows in the legislative framework through engagement of all players in the infrastructure delivery value chain within the context of easy of doing business reforms. For example, the merging of the three pieces of legislation and related institutions to form the Zimbabwe Investment Development Authority (ZIDA) as a "one-stop-shop" responsible for all the investment related issues in the country is likely to enhance the scope of mobilising blended infrastructure finance.

Prudent macroeconomic management is key to addressing the twin deficit (fiscal and current account) which have been associated with economic instability in the country. Government borrowing from the domestic financial sector mainly through issuance of Treasury Bills (TBs) has been associated with crowding out private sector borrowers. This has further undermined the capacity of private sector investors to scale-up their investments including infrastructure investments due to binding credit constraints. Thus, stability and predictability of the overarching of the macroeconomic environment creates a conducive environment for the growth of a blended infrastructure finance market

The study noted that DFIs are the main source of long term infrastructure funding. Furthermore, a significant amount of ODA with respect to blended infrastructure finance comes through concessional loans offered by development finance institutions (DFIs). In this regard, the international engagement efforts by Government can make a deliberate to focus on mobilising ODA for infrastructure development in the country. There are also opportunities to leverage on funds mobilised under the multi-donor platforms such as ZIMFUND and ZIMREF, to increase the amount of resources raised for the same cause. Government policy is also key in engaging and guiding donor interventions in line with country's needs and national development priorities.

The study has also established that most roads in Zimbabwe do not have enough traffic to sustain private tolling of roads without government support through such schemes as shadow tolling or viability gap funding⁷⁰. Due to the social nature of roads projects, their ability to spur economic growth, regional integration and address poverty Gap funding, grants and other instruments can be used to attract private sector. There are also opportunities for the railways sector, where NRZ can enter into deals with the private sector that need transport, who would give out loans for rehabilitation of the track, wagons and locomotives and the loan is paid out through assured transport services.

The Annexure provides details of the review country and regional case studies that informed the conclusions and recommendations of this study. For example, Lekki-Epe Expressway project in Nigeria also shows that even though Government can be able to blend private, state and development partner resources towards a project, it can fail due to lack of user buy in into the project. Thus, community involvement and engagement is necessary for the users to be willing to pay the user fees for the project. The Henri Konan Bedie Bridge project in Cote d'Ivoire on the other hand shows that Government has to be heavily involved to make a project attractive to private sector players. This includes subsidising, providing a minimum revenue guarantee, coming up with its own contribution and taking equity in the project in a ratio related to its investment. This is critical as the private sector would need assurances that government is committed and is prepared to share in the risk, rather than getting equity in a manner that is not commensurate with the funding.

Finally, the study also noted from the country case studies that there is scope for reintroducing municipal bonds to finance infrastructure for the local authorities, including water and sewer infrastructure as well as road rehabilitation. However, the motivation by investors to invest in municipal bonds should not only be based on central government guarantee and prescribed asset status of the project, but should also be based on sound business plans and governance frameworks of the issuing local authorities. The municipal bonds need to be able to be repaid based on the income streams from the projects where the proceeds have been invested.

⁷⁰ Viability **Gap Funding** (VGF) Means a grant one-time or deferred, provided to support infrastructure projects that are economically justified but fall short of financial viability. The lack of financial viability usually arises from long gestation periods and the inability to increase user charges to commercial levels.

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Annex L: Local Case Studies of Blended Infrastructure Finance Projects

L.1. Beitbridge Bulawayo Railway Project

This was a greenfield project worth about \$85 million initiated in 1998. This was a 30 year PPP project of the BOT type. A new company, Beitbridge Bulawayo Railway (PVT) Limited (BBR) was established for the implementation of the project, which is a 350km railway line from Beitbridge to Bulawayo, built in over 18 months. The private sector is recovering costs from user fees, as BBR is still managing this section of the railway. The financing for the project was wholly from the private sector, although a national government guarantee was secured from government. In addition, government also gave some incentives to attract the private sector players, including exemption of duty on imported rail equipment and spares, tariffs which are discounted and tax holidays.

The four sponsoring firms hold equity in BBR as follows:

• Nedcor Investment Bank Ltd-South Africa	13%
• New Limpopo Project Investment-Mauritius	36%
• Old Mutual-South Africa	17%
• Sanlam Group-South Africa	17%

Government, through the National Railways of Zimbabwe, got a 15% stake in BBR. Although there was no financial injection from Government for the transaction, the provision of a government guarantee and the various incentives provided sweeteners to crowd in private funding into the project thus qualifying as a blended financing project.

L.2. Joshua Nkomo Expressway (Airport Road)

This project involved engagement of a contractor for the design and construction of the Joshua Nkomo Expressway, which is a dualised road from the airport. In 2012, Augur Investments was awarded a tender through a joint venture company-Sunshine Developments Limited, which was established for the purpose. Government through Harare City Council (30%) and Augur Investments (70%) were the only shareholders of Sunshine Development Limited. The project was valued at \$68.6 million and government also had to fund its equity in Sunshine development Limited by paying 90% of the cost in the form of land, construction material and services while the remaining 10%, valued at about \$8 million, was to be paid for in cash (High Court of Zimbabwe, 2016). As security, government pledged 100 hectares of land in Gunhill Township.

Government, through City of Harare also committed to giving out 4,000 hectares of land to Augur, including land on which Augur Investment had to design and construct a \$100 million Shopping Mall in Borrowdale. Thus, through the use of land, government was able to attract private sector funding into the project, which is a form of blending public and private sector funding. However, there were a lot of challenges with the project, including allegations of corruption and misuse of funds, which eventually saw the deal being called off for failure to complete the project. ZINARA took over the project to completion. This key lesson drawn from this example is the need to avoid defective tendering process because of the contestation that arise during the project execution.

Box 1: Plumtree-Harare-Mutare Highway Project

This project, which was initiated by development partners, involved the rehabilitation of the highway from Plumtree to Mutare via Bulawayo and Harare. A total of 820 km was to be rehabilitated at a cost of about \$206 million. The project was initially intended to be a rehabilitate-transfer type of PPP project, where the private sector had to be engaged for project design, provision of technical support and equipment as well as the rehabilitation of the road. The project also involves the construction of nine toll gates.

The project was financed from a loan from the Development Bank of South Africa which has to be repaid with interest. The loan has to be repaid over a 10 year period together with interest. A special purpose vehicle, Infra-Link, was created which was used to secure the loan. Infra-link is a joint venture between government, through ZINARA, and Group Five of South Africa. ZINARA owns 70% of Infra-Link while Group Five owns 30%. Group Five is responsible for the project implementation, including construction works, rehabilitation and tolling. As initially scheduled, user fees from the road were to be used to retire the loan and interest. The project was structured with the knowledge that traffic volumes will not be enough to fund the project. In this regard licensing fees were included in the project as part of source of funding for this project.

Although government, through ZINARA, owns 70% of Infra-Link, there was no blending involved in the project as the entire funding came from the loan secured from DBSA.

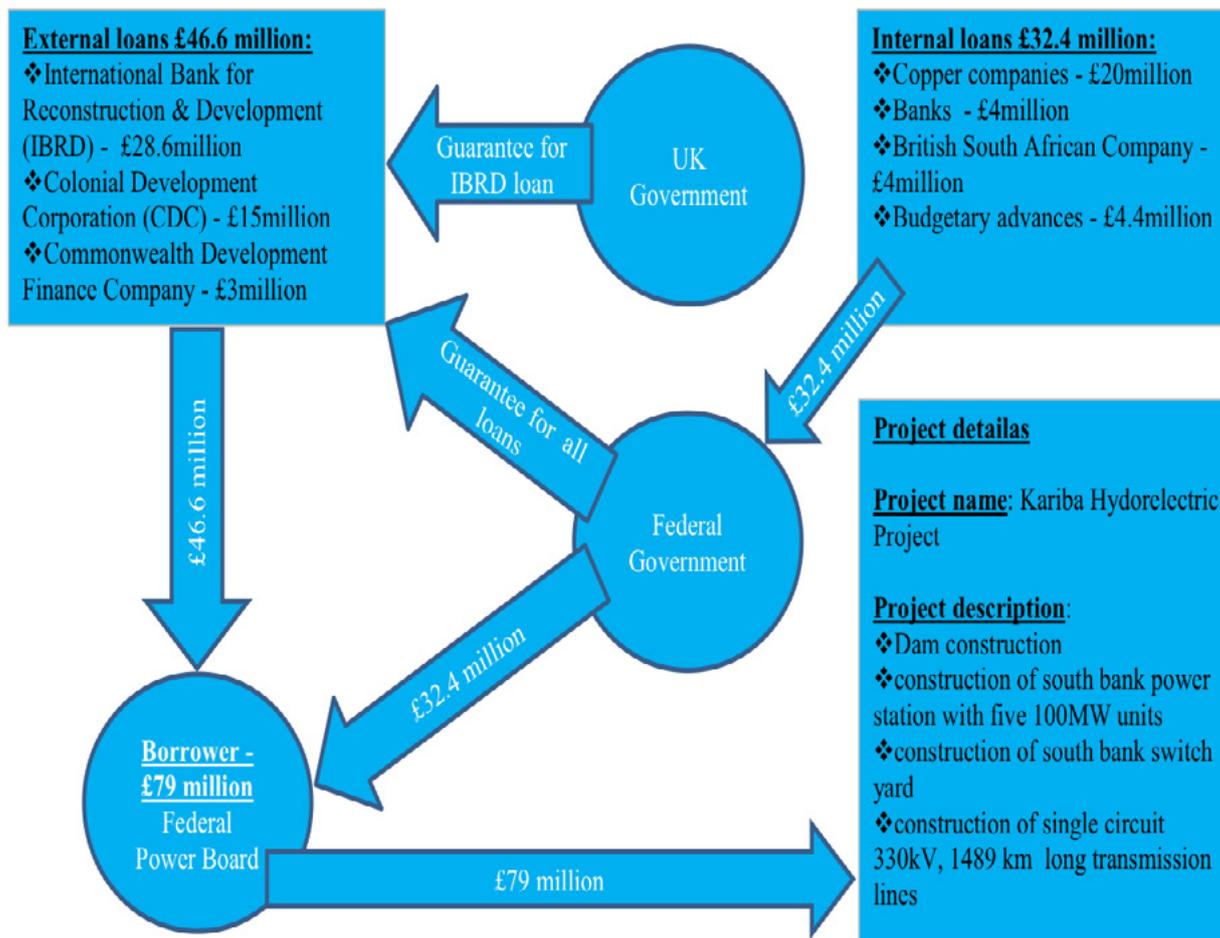
Lessons from the project

The project generally underlines the need for government to undertake feasibility studies for its projects. Allegations of overestimation of traffic volumes through the route, would not arise. The project also faces implementation challenges related to rent seeking behaviour. In this regard strengthening capacity of institutional governance becomes a key in projects of this nature.

L.3. The Kariba Hydroelectric Project

The total cost of the Kariba Hydroelectric Project was £79 million (IBRD, 1956)⁷¹. The project was funded through external and internal loans. The external loans were obtained from the International Bank for Reconstruction and Development (IBRD), Colonial Development Corporation (CDC) and Commonwealth Development Finance Company (CDFC) – see Figure 24. The loans were guaranteed by the UK Government and Federal Government of Rhodesia and Nyasaland. The guarantees enhanced the credit worthiness of the Federal Power Board and therefore facilitated lending by the DFIs to the Board at reduced the cost.

Figure 24: Financing mechanism for the Kariba Hydroelectric Project



Source: Authors' compilation

The internal loan was contracted from copper companies, banks and British South African Company (BSAC) and budgetary advances from the Federal Government as balancing loan. The Federal Government borrowed the money using bonds from copper companies, banks and BSAC and then on-lent the money to the Federal Power Board on the same terms as it had borrowed except that the Board was supposed to start servicing the loan after five years. This effectively lowered the Federal Power Board's cost of borrowing because (i) the government borrowed at a lower cost due to its relatively high creditworthiness and (ii) the government deferred the servicing

⁷¹ International Bank for Reconstruction and Development (1956). Appraisal of the Kariba Hydroelectric Project in the Federation of Rhodesia and Nyasaland. <http://documents.worldbank.org/curated/en/250771468179932152/pdf/multi-page.pdf>

of the loan. The later point is important because it was going to be difficult for the Federal Power Board to borrow directly from the private companies and start servicing the loan in a year's time given the lead time between construction of the power plant and revenue generation from the sale of electricity from the power plant.

The money which was advanced to the Federal Power Board from government budget had terms equivalent to those that would have been given government if it were the borrower under a similar circumstance. This ensured that the Federal Power Board got funds on favourable terms through riding on the credit worthiness of the Federal Government of Rhodesia and Nyasaland.

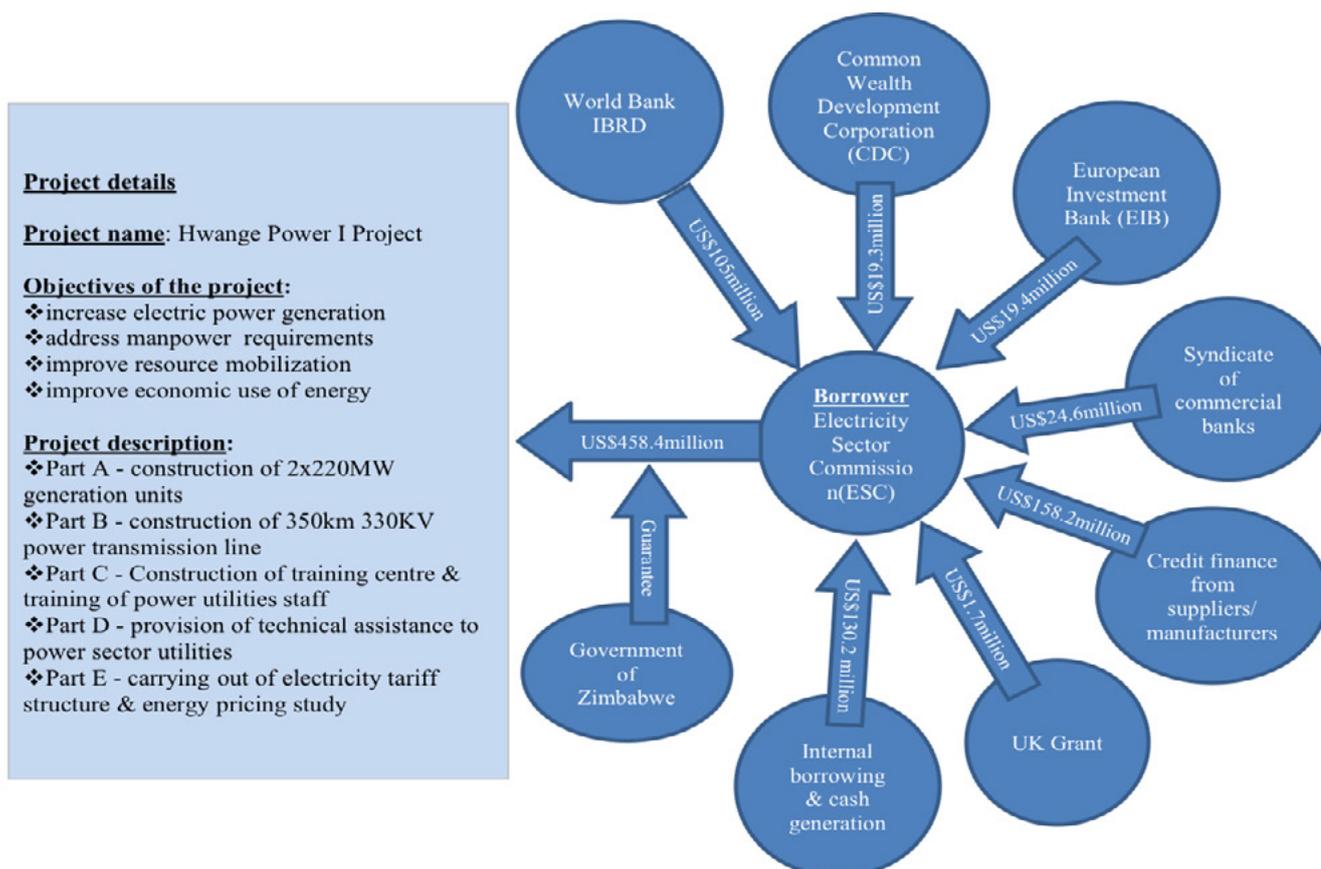
The funding mechanism of the project also used subordination, which encouraged DFI and the private sector to lend to the Federal Power Board and the Federal Government. The internal loan was subordinate to the external loan, as long as the government was the beneficial owner on the internal loans. This effectively prioritized the external loan repayment ahead of the internal loans and therefore encouraged DFIs to lend money towards the project. However, in the event that the primary holders of the bonds disposed of their holdings, the subordination of internal loan to external loan would cease.

While the internal loan was subordinate to the external loans, the Federal Government loan was also subordinate to both the external loans and the internal loans provided by private companies. Thus, the Federal Government would claim loan repayment after all the other scheduled loan repayments for external and internal loans were made. This provided some security to the external and internal loan providers in the event that the project revenues would not be adequate to meet all the scheduled loan repayments. Drawing from this experience there is scope for the current RBZ savings bond to be channelled towards infrastructure development.

L.4. The Hwange Power I Project

The total project cost for the Hwange Power I Project was US\$458.4 million. The project was funded by loans from the World Bank, Commonwealth Development Corporation, European Investment Bank and a syndicate of commercial banks. It was also funded through credit financing from suppliers and manufacturers (Figure 25) of materials used in the project. The UK Government provided a grant towards the project.

Figure 25: Funding Structure of Hwange Power Extension Project



Source: Authors' compilation

The Government of Zimbabwe provided the guarantee for the loans extended for the project. Interest payments during construction, which amounted to US\$130 million up to 1986, were added on the loans provided by the lenders. This was meant to give reprieve on the government since there was a long time lag in building up revenues from the project, inadequate cash flows from the power sector and that even tariff increases could not meet the interest during construction.

Annex R: Regional/International Blended Infrastructure Finance Projects

R.1. Financing the Eastern Africa Submarine Cable System

In 2003 the NEPAD E-Africa Commission presented the proposed East Africa Submarine Cable System Project, deemed essential to providing broadband access to countries along the East African coast (Figure 26). Countries in that region had until then relied mostly on foreign-owned satellites for internet access. In 2010 the Eastern Africa Submarine Cable System (EASSy) project was then commissioned. EASSy is a 10,000km submarine cable system deployed along the east and south coast of Africa to service the voice, data, video and internet needs of the region. With more than 10 Tbps of capacity, EASSy is one of the highest capacity systems serving Africa.

Figure 26: The East African Submarine System (EASSy)



Source: <https://www.icafrica.org/en/topics-programmes/case-studies/ict-the-east-african-submarine-system-eassy/>

The EASSy cable runs along the east African coast, from the southern tip of the continent to the African horn – it links South Africa with Sudan via landing points in Mozambique, Madagascar, the Comoros, Tanzania, Kenya, Somalia and Djibouti. With extensions to 13 adjoining landlocked countries as well as to the Comoros Archipelago, 21 African countries have been provided high-quality internet and international communication services and a missing link to the larger global network of submarine cables has been closed. By now, some 250 million people are benefitting from improved service quality and a reduction in bandwidth costs. The system serves as an example of how African and global telecommunications companies can work with regional institutions to develop telecoms infrastructure. It enables telecommunications operators to access growing markets in voice, mobile and internet communications and reduce their dependence on satellite.

Role of involved parties

The underwater cable is owned by the EASSy special purpose vehicle (SPV), as well as any investors in the SPV. The EASSy project purchases data in the cable and is entitled to sell capacity to other parties. The project has got support from the DBSA, AfDB, EIB, AFD, KfW and the World Bank's IFC; international operators and Government and regulatory authorities. The EU-Africa Infrastructure Trust Fund and the New Partnership for Africa's Development-Infrastructure Project Preparation Facility (NEPAD-IPPF) made available grant funding to recruit early stage management capacity for the project.

Financing of the project

The project was developed and funded through a major institutional effort combining many divergent African institutions. EASSy acts as a medium of internet connectivity carrying telecom traffic for all African operators from the Eastern and Southern African markets to connecting Cable networks in Europe, Asia and the Americas.

An initial grant of US \$499,372 from NEPAD-IPPF Special Fund triggered this important transformational regional project, the first of its kind in Africa.

Recipient: East African Community (EAC)

Year of Approval: April 2005

Amount of Grant: US \$499 372

AfDB funding was a vital element in the setting up of the West Indian Ocean Cable Company (WIOCC), which was established as a “Special Purpose Vehicle” (SPV) and largest shareholder in the EASSy submarine cable system. WIOCC bundles the efforts of 14 shareholding telecommunication companies in the region. AfDB and WIOCC/EASSy obtained support from World Bank/IFC, AFD and KfW through loans.

The project was financed through equity contributions of US\$ 20 million and a syndicated loan of US\$ 70.7 million from KfW, the African Development Bank (AfDB), the European Investment Bank (EIB) and the International Finance Corporation (IFC). There have also been additional direct capital investments of major African and international telecommunication companies.

The initial feasibility study was completed in 2005 and concluded that the construction of the cable would be financially viable. Environmental and social impact assessments, funded by KfW and AfDB, were also carried out. The African Development Bank, together with several African Governments, provided funding. The EASSy project faced delays as it was originally scheduled to be operational by the end of 2006. Financial closure was reached in March 2007 and the total project cost was \$248 million.

Financing arrangements of the development banks included specific covenants to strengthen price and service competition for promoting economic development in the target region.

Lessons learned

The initial timelines for the project were not maintained, mainly as a result of disagreements between various parties over the funding structure and ownership of the project. There was disagreement between private investors who had a profit motive, and Government whose motive was to provide low cost bandwidth access. These disagreements resulted in project delays. South African and Kenyan Governments had disagreements regarding the cost of access to the fibre optic cable also contributed to delays. The numbers of participants to projects exponentially add to the complexity of running such projects and require a great deal of cooperation and communication to remain on track.

R. 2. Central African Backbone Program

The Central African Backbone project entails developing a fibre-optic Internet backbone to connect the countries of the Economic Community of Central African States in Africa via high speed internet. The Project endorsed by the CEMAC Head of States is expected to decrease prohibitive telecom costs in landlocked countries, improve quality, route diversification and coverage of telecom services, and enable regional integration through Public-Private Partnership implementation. The countries included in the CAB project are: Cameroon, the Central African Republic, Chad, Democratic Republic of the Congo, Gabon, Republic of the Congo and São Tomé and Príncipe.

The project was split up into five phases, each phase focusing on the fibre rollout in one or more countries. Of these phases, the objective of the CAB program is to contribute to increase the geographical reach and usage of regional broadband network services and reduce broadband prices. In Cameroon the CAB runs from the coast, through the capital of Yaoundé, to the north east where it meets up with the Chadian part of the backbone. The deployment of the CAB in the Central African Republic was slowed down by the political instability in 2012-2013. It runs from Chad in the north to the capital of Bangui. In Chad the CAB runs from N’Djamena towards the south where it forks off in two directions, one towards Cameroon and one towards the Central African Republic. In Democratic Republic of the Congo the CAB will run from Kinshasa to Lubumbashi and Kisangani. In Gabon the CAB runs from Libreville to Franceville, and from thereon it splits in two directions, one towards Lékoné and another towards Kouilamoutou. In São Tomé and Príncipe the CAB runs in the capital of São Tomé

There are four components to the project.

The first component is promoting the enabling environment. This component aims to: (i) promote further regional market integration; (ii) strengthen the legal, regulatory, and institutional framework; (iii) support market liberalization; and (iv) promote the establishment of infrastructure that once in place is accessible to all service providers on open, transparent, competitive, and non-discriminatory terms. The second component is the connectivity. This component will leverage the existing fibre-optic network laid along the Chad-Cameroon oil pipeline that will form the core CAB network and support the deployment of interconnected networks to form a regional network. The third component is the eGovernment and flagship Information and Communication Technology (ICT) applications. The program will seek to improve the Government efficiency by supporting development and rollout of selected eGovernment applications making use of the improved connectivity.

Finally, the fourth component is the project management. This component will consist of support to finance management related issues at the project level. Depending on the specific implementation arrangements for each country, this component may include elements such as human resources support with management, procurement, financial management, Monitoring and Evaluation (M&E), internal

and external audit, communications expertise, operating expenses, and equipment.

Table 11: Central African Backbone (CAB) Program Project

Item	Details
Borrower	Government of Cameroon, Car and Chad
Implementing Agency	Relevant Ministries in Charged with Telecommunication & IT
Lender	The World Bank
Total Project Cost**	US\$ 26.73 million
Commitment Amount	US\$ 26.20 million

Sectors covered by the Project

Sector	Funding Size
Public Administration - Information and Communications Technologies	13%
ICT Infrastructure	61%
Social Protection	13%
Other Industry, Trade and Services	13%
Total	100%

Funding

Phase 1 of the CAB project focused on Chad, Cameroon and CAR and involved approximately US\$30m financing. Phase 2 of CAB Project included other Central African Countries as well as Nigeria and could mobilize up to US\$130m additional financing.

Project CAB Project Funding Structure

Funding Partner	Type of Funding	Amount	Time Period
World Bank	Loan	USD160 million	
World Bank	Loan	USD206 million	As of 2015
World Bank	Loan	USD273 million	by 31 December 2019

The entire project is scheduled to be completed by 31 December 2019, when the network in the Democratic Republic of the Congo will be operational, as the last of the five phases.

R.3. Multinational (Niger and Chad): Trans-Sahara Optical Fibre Backbone (TSB) Project

The project involves laying of 1 510 km of optical fibre linking Niger, Algeria, Nigeria and Chad. The projects were in line with the countries development plans. The project also intends to establish pilot data centres, eGovernment platforms and an Integrated Management System for the Electronic Identification of People (SIGIEP) in all the four participating countries. The EU also plans to provide institutional support for the conduct of feasibility studies on the continuous implementation of the project, support ICT regulatory authorities, other relevant government agencies, academic institutions and women's empowerment organisations. The project is being implemented over a four-year period from 2017 to 2020 for a total cost estimated at UA 62.262 million distributed as in the following table.

Trans-Sahara Optical Fibre Backbone Project Funding Structure

Funding Partner	Type of Funding	Amount
European Union/Africa Investment Facility	Loan	UA 24.889 million
European Union/Africa Investment Facility	Grant	UA 9.9929 million (to Niger)
Country contributions	Counterpart Funds	UA 4.502 million
Total		UA 39.3939 million

Project Scope

The project interconnects three regions of the continent (West, Central and North) by optical fibre. It involves the development of international communication systems for Niger, Algeria, Nigeria and Chad. The project scope includes laying long distance underwater cables. On completion the project gives alternative access to international traffic at optimum, capacity speed and costs through the Algerian and Nigerian coasts. The project will help to reduce fragility by strengthening administration and social cohesion.

Borrower:	Republic of Niger
Project name:	Trans-Sahara Optical Fibre Backbone (TSB)
Project location:	Regions of Agadez, Diffa, Dosso, Niamey, Tillabery and Zinder (Niger) Regions of Hadjer-Lamis, Lac, Kanem and the Town of Ndjamena (Chad)
Executing agency:	Ministry of Post and Digital Economy (MPTEN) of Niger Ministry of Post and New Information Technologies (MPNTI) of Chad

Table 12: Financing Plan

Source of Financing	Source of Financing Amount in CFAF Billion	Amount in EUR Million	Amount in UA Million	Instrument
African Development Fund (ADF) [Loan]	20.571	31.361	24.889	Project Loan (PBA Niger)
ADF (Grant)	8.206	12.51	9.929	Project Grant (PBA Niger)
EU (AfIF)	18.962	28.907	22.942	Project Grant
Government of Niger	2.119	3.231	2.564	Universal Assess Fund (Public)
Government of Chad	1.602	2.442	1.938	Universal Assess Fund (Public)
Total	51.46	78.451	62.262	

Table 13: African Development Fund (ADF Key Financial Information)

Loan/Grant Currency	Unit of Account UA
Interest Type	Not applicable
Interest Rate Margin	Not applicable
ADF Loans Service Charge	0.75% per annum on the disbursed and outstanding loan amount
ADF Loans Commitment Fee	0.50% per annum on the undisbursed loan amount, commencing 120 days after the signing of the Loan Agreement
ADF Loans Tenor	40 years
ADF Loans Grace and Repayment Period	10 years
FIRR, FNPV (baseline scenario)	21.17%; EUR 261.320 million (at 2%)
EIRR, ENPV (baseline scenario)	25.61%; EUR 102.876 million (at 10%)

Challenges and lessons learnt

The major constraints and problems encountered, especially in the implementation of infrastructure projects in both countries, include: (i) the slow pace of procedures for the procurement of goods, works and services; and (ii) the delayed mobilization of national counterpart funding.

In view of the challenges the implementers learnt to capitalize on some measures that had been already taken or planned such as: (i) use of the advance contracting (AC) method to minimize procurement delays; and (ii) steps taken by the ministries concerned in both countries to ensure the inclusion of national counterpart contributions (for financing compensation, among other things) in universal access funds throughout the project since 2017. The ICT sector-related challenges in the countries were anticipated by taking into consideration the strengthening of the regulatory framework.

R.4. Kigali Bulk Water Project, Rwanda

The Kigali bulk water supply project is PPP between the Government of Rwanda, represented by the Ministry of Infrastructure, Water and Sanitation Corporation, the government water utility company and Kigali Water Limited. The project scope involves the development, design, financing, construction and operation of 40,000m³/day bulk water facility south of Kigali in Rwanda and is due for completion in 2020. The scope of the project comprised of a water treatment plant, a well field with 38 wells, three pumping stations, pipelines and three storage reservoirs. Under the public-private partnership (PPP) arrangement, Kigali Water Limited will supply bulk water to the Water and Sanitation Corporation, which will then be sold to local consumers.

Failure to meet the water supply needs of the rapidly growing population of Kigali led the government to partner private sector to diversify and improve water supply for the country's fast growing capital city through a PPP. The project was meant to increase water supply in Kigali by 40%, with 150,000 customers expected to benefit in the first phase (IFC, 2015, Cattaneo, 2018). In September 2010, the Government of Rwanda engaged the International Finance Corporation (IFC) as lead advisor to develop and structure this bulk water supply PPP. Due to the limited capacity within Kigali's public water utility, both in terms of developing and implementing the PPP, IFC assisted Rwanda with the preparation, design, and implementation of private sector participation in the project. IFC attracted private sector investors due to its established financial standing and experience in the development, management, operation, and maintenance of a bulk water supply facility. IFC assisted in the identification of the most appropriate location of the project as well as demand assessment to determine the plant sizing and competitive selection of investors to implement the PPP project. IFC mobilised funding from the Public-Private Infrastructure Advisory Facility (PPIAF) to support capacity building for the water utility and the water sector reform process in addition to transaction advisory mandate. A detailed legal, financial, technical and environmental assessment of the project was conducted to assess the feasibility of the proposed project.

The project is a 27-year concession on a Build, Operate and Transfer (BOT) arrangement. Under the BOT structure, the private investor, (the Concessionaire), would finance the design, construction, financing, operation and maintenance of a water production and treatment facilities to deliver up to 40,000 m³/day. The bid criterion was to engage a bidder with the lowest tariff. Metito consortium comprising of Metito Utilities Ltd and Metito Overseas Ltd won the concession through a competitive bid and committed US\$ 75 million to develop the scheme, the largest amount for many years invested by the private sector in the water sector in Sub-Saharan Africa (IFC, 2015). Three companies, the Emerging Africa Infrastructure Fund (EIAF), the Technical Assistance Facility (TAF) and Devco helped to finance the project at different stages of its development. EIAF led an arrangement of financing for the US\$61 million plant, providing a US\$40 million, 18 year long term long-term loan jointly with the African Development Bank (AfDB). The US\$61 million was finance on a non-recourse basis at a leverage of 78.5%. The funding mix comprised debt facility with an 18 year door-to-door tenor and grant funding. Devco, the specialist PPP advisory facility provided funding to help structure the transaction and preparation of tender documents. TAF granted US\$6.5 million in crucial viability gap funding to reduce upfront costs and allow the number of people connected to a reliable water supply without raising tariffs. The balance required was provided by Metito as equity. The well-coordinated package of blended finance led to the success of the PPP project since both the Government of Rwanda and Metito had the necessary assurance and security and the project was affordable to all the parties including the end users. The project also had a Multilateral Investment Guarantee Agency (MIGA) guarantee to hedge against political risk and to act as a credit enhancement guarantee. The main source of revenue for the project was the purchase agreement on transmission fees with the public entities.

Metito was supposed to complete the project in the first two years and then operate and maintain it for the remaining 25 years. The PPP agreement was signed on March 31, 2015. The sole off-taker for the project is the national water utility (Water and Sanitation Corporation), while the Ministry of Infrastructure was the guarantor of the project on behalf of the Government.

Box 2: New Cairo Waste Water Plant, Egypt

The project consisted of the design, finance, construction, operation, and maintenance of a new wastewater treatment plant with a capacity of 250,000m³ per day in New Cairo City. It is a satellite town of greater Cairo meant to decongest the center of Cairo (World Bank, 2014). The transaction structuring was supported by IFC under a 20-year BOT agreement.

Bidding involves a competitive technical and commercial bid which required a bidder to pass the technical bid before proceeding to the commercial bid. Seven bidders prequalified out of 10 applications received by the government, of which five bids were from consortia comprised of local, regional, and international firms.² The selection process of the private sector included an initial pre-qualification of prospective bidders based on financial and technical criteria, such as minimum net worth and experience with BOT projects, especially with similar wastewater treatment plants. The winning bidder was selected on the basis of the lowest net present value of the overall sewage treatment charge throughout the concession period. A consortium of Egyptian firm Orascom Construction Industries (OCI) and Spanish firm Aqualia was awarded the contract in June 2009.

The project was the first successful transaction under the Egyptian government's PPP programme and a model for future PPPs (World Bank, 2014). The deal mobilized US\$140 million in private investment which comprised of capital structure of 70/30 debt /equity ratio. The debt was provided by four local banks and equity from Orascom (55%), Aqualia (40%) and Aqualia infrastructure (5%) (Ruiz de Velasco, 2012). The banks acting as lenders were National Société Générale Bank SAE (32.99%), Commercial International Bank (Egypt) (32.77%), Arab African International Bank (17.12%) and Ahli United Bank (Egypt) (17.12%). The debt structured as project finance without recourse, amounted to E£566 million (US\$103.47) million in two tranches, E£550 million (US\$100.55) million in the form of a long-term facility (15 years) to finance up to 70% of the project's investment cost (EPC cost) (Salvador et al., 2016). The remaining 30% was in equity E£16 million (US\$2.93 million). Another tranche was in the form of operation performance letters of guarantee issued during the operation periods.

Success and failure factors

The success factors of the project included factors such as high level of commitment by the Ministry of Finance and a transparent process which included an investor conference, objective evaluation and no post bid negotiations. The main source of revenue for the project was the purchase agreement or transmission fees with the public entities. The Government of Egypt supported the project through providing revenue subsidy. IFC team continued to support the project until financial close on the 4 February 2010 (Ruiz de Velasco, 2012). The new plant was completed and commissioned in March 2012.

The consortium experienced difficulties due to the absence of a specific PPP law (one was approved a year after financial close) and the limited experience of Egypt's public administration in PPPs (Salvador *et al.*, 2016).

Lessons learnt

- Government commitment is critical for the success of PPPs.
- PPP legislation integral before undertaking any PPP project for the provision of guidance and giving legal force.
- Good selection process is critical for the success of PPPs. IFC experience in managing PPPs played a critical role to enhance selection of a private player.

R.5. The Lekki-Epe Expressway, Lagos Nigeria⁷²

The project construction started in 2007 and was completed in 2011. It involved the upgrading and rehabilitation of the 49.5km long road, constructed in 1983. The road connects Lekki and Epe to the rest of the Lagos State. The total cost for the project was US\$382 million. It also involved the widening of the road from a four-lane design into a six-lane highway. The project was the first PPP project by the Lagos Authority.

Asset and Resource Management Company (ARM) was the project contractor. A special purpose vehicle company, Lekki Concession Company (LCC) was created by ARM for the purpose (Bolton Consulting Group and Africa Finance Corporation, 2017). ARM also appointed Hitech Construction Company Limited as the engineering procurement and construction management contractor while Aurecon, along with its partners, was engaged as the designer, quality assurance and quality control for the project. A BOT toll road concession type model was adopted, where LCC would upgrade the road and collect the toll for 30 years before handing over to the State.

Financing was originally sought from Nigerian lenders but the project failed to find takers. This resulted in a blending approach being adopted as a strategy to attract the private sector. First, the African Development Bank (AfDB) was approached for longer-term concessional financing. Second, Standard Bank was approached to mitigate the foreign currency risk by structuring a swap facility where LCC's exposure to dollar denominated obligations would be mitigated. Third, the Lagos State government also contributed by underwriting the project with debt financing of about 10% of the total project costs. This also served as a risk mitigation strategy. The State also included a provision under the contract promising compensation to the contractor in the event that other transport projects within a 10km radius of the Lekki-Epe Expressway would be developed which would affect toll revenue collection (Bolton Consulting Group and Africa Finance Corporation, 2017).

⁷² In addition to the referenced BCG (2017), this project information was sourced from two main online sources; Trinity International article of 2009 at website <http://www.trinityllp.com/a-review-of-the-lekki-epe-expressway-toll-road-concession-project/> and an AfDB 2008 article at website <https://www.afdb.org/en/news-and-events/nigeria-afdb-approves-us-85-million-for-lekki-toll-road-project-3427/>

The key funding partners for the project were the following:

- African Development Bank-\$85 million
- Lagos State Government -\$42 million
- Standard Bank (S.A) through Stanbic Nigeria-\$93 million
- Indigenous Banks-First Bank and United Bank for Africa-\$80 million

A sovereign guarantee was needed to cover default risk from the Lagos state. This proved difficult to get from the federal Government, mainly due to political differences. The political party that was controlling the State was different from the one at Federal level. Thus, the project had to delay for two years as the sovereign guarantee was being sought (Bolton Consulting Group and Africa Finance Corporation, 2017).

When tolling was eventually commenced in 2010, there was a lot of resistance to the project expressed through street protests. This also affected the ability to introduce the second and third toll plazas. The project was eventually taken over by the State in 2012 through buying back the project from LCC. Just like any other contract, LCC was entitled to compensation.

Some important lessons can be drawn from this project. Although the Lagos State Government in Nigeria blended private, state and development partner resources to fund the project, successful operation failed due to lack of user buy in into the project. Community involvement and engagement is necessary for the users to be willing to pay the user fees for the project. However, the ability to unlock funding for the project is commendable as it shows the following which can serve as lessons (Bolton Consulting Group and Africa Finance Corporation, 2017):

- Considerable commitment shown by the state by agreeing to guarantee the investment required to enable the pre-financial works to proceed and then to providing a loan to LCC to assist in overall project financing.
- The ability to secure long term funding from AfDB and Standard Bank of up to 15 years was also key in attracting local lenders.
- The local lenders were also buoyed by consolidation and an extended bond yield curve, which saw them willing to offer 12 year tenors, which had not been previously seen in the Nigerian market.

Box 3: The Henri Konan Bedie Bridge- Cote d'Ivoire

This case is an example of a successfully blended project, whose financial closure took place in 1999 but political unrest and civil war which took place until 2011 prevented the project from being implemented. It was eventually initiated in 2011 and construction was completed in 2014. The project was designed as a BOT 30 year PPP project where the investment costs would be recovered through user fees. The project consisted of a 6.4km highway and 1.9km bridge with three lanes across Ebrie Lagoon. It connects Abidjan's residential Riviera district directly with the commercial district of Marcory.

The Bouygues Group was the anchor investor and carried out construction, operation and infrastructure management. As a way of attracting private investment, Government gave a sizable subsidy worth about US\$81 million and also undertook to provide a minimum revenue guarantee during the loan repayment period.

This was a US\$365 million PPP project in which Africa Finance Corporation was the mandated lead arranger and contributed an aggregate commitment of US\$55 million loan facility plus equity. In addition to the subsidy and guarantee, government also contributed in excess of US\$90 million (50 billion CFA), entitling it to 18.65% shareholding. The Multilateral Investment Guarantee Agency (MIGA) provided US\$145 million in insurance cover for equity investment and loans, risk of transfer restrictions, expropriation, war and civil disturbances and breach of contract. Other partners who chipped in with financing include Bouygues Group; AFC; African Development Bank (AfDB); FMO; PAIDF; Banque Quest Africaine de Developpement (BOAD); Banque d'Investissement et de Developpement de la CEDEAO (BIDC); and Banque Marocaine du Commerce Extérieur (BMCE).

Lessons from the project

Important lessons from the project include the following;

- In addition to giving out a subsidy of about \$81 million and providing a minimum revenue guarantee, the Government also came up with its own contribution and took up equity in the project in a ratio related to its investment. A number of projects have seen government emerging as the majority shareholder even without putting any significant financial resources;
- Risk management went beyond the taking up of equity by the different players. The World Bank (MIGA) had to be roped in to separately bear the risk of transfer restrictions, expropriation, war and civil disturbances and breach of contract as the contribution into the project. Risk management that also offers a business opportunity for insurance firms to participate in infrastructure projects is important.

Sources: (Bolton Consulting Group and Africa Finance Corporation, 2017) and AFC. Available at <https://www.africafc.org/What-We-Do/Projects/Henri-Konan-Bedie-Bridge-%E2%80%93-Cote-d%E2%80%99Ivoire.aspx>

R.6. Bujagali Hydropower Project

The Bujagali hydropower project is a 250MW electricity power generation project located on the river Nile in Uganda. It is the first independent power project and the largest in terms of investment (US\$900 million) in Sub-Saharan Africa (see Table 14). The project was funded through equity (22%) from Sithe Global Power, Aga Khan Fund for Economic Development (AKFED) and the Government of Uganda and debt (78%) from multilateral development institutions, bilateral institutions and commercial banks. The MIGA provided

political risk guarantee against equity provided by Sithe Global Power (see Table 14). The project provides up to 50% of electricity demand in Uganda.

Table 14: Factsheet for the Bujagali Hydropower Project

Country	Uganda				
Project summary	250 MW hydro-electric power project on the River Nile, 10 km from Lake Victoria, plus management of the construction of approximately 100 km of 132 kV transmission line, sub-stations, and related works on behalf of UETCL (the interconnection project). Includes creation of a 3.88-km reservoir inundating Bujagali Falls.				
Project company	Bujagali Energy Ltd. (BEL)				
Contract type	Power-Purchase Agreement (PPA) for 30 years from commissioning				
Project cost / funding	Total	Equity	Debt		
			Total	subordinated	senior
	\$902m	\$200m (22%)	\$702m (78%)	\$68m (8%)	\$634m (70%)
Investors	Organisation	Amount	Guarantor	Risk	
	Sithe Global Power (Sithe)	\$115m	MIGA	political	
	AKFED and affiliates	\$65m			
	GoU	\$20m ^a			
	Total equity	\$200m			
Lenders	Organisation	Amount	Subordinated	Guarantor	
	IFC	\$128m	\$30m		
	EIB	\$136m			
	AfDB	\$110m			
	Total multilateral DFI debt	\$374m			
	FMO (Dutch)	\$82m	\$28m		
	Proparco/AFD (French)	\$72m	\$10m		
	DEG / KfW (German)	\$59m			
	Total bilateral DFI debt	\$213m			
	ABSA (Barclays Africa Group)	\$58m		IDA	
	Standard Chartered (UK)	\$58m			
	Total commercial bank debt	\$115m			
	Total debt	\$702m			
		Senior debt: 16 years; subordinated debt: 20 years			
EPC contractor	Salini Costruttori SpA; Alstom (main subcontractor)				
O&M contractor	Gas Natural Fenosa				
Public-sector support	GoU Implementation Agreement grants right to construct and operate the project & guarantees UETCL's payment obligations				
Project development	<u>Bujagali I</u>				
	1994	Unsolicited bid from AES Corporation and signature of letter of intent			
	2000	Bujagali PPA approved by parliament, despite objections that a project at Karuma would be more cost-effective. World Bank withdrew from project twice, once after NGO objections and once because of bribery accusations.			
	2003	AES withdrew from project just before Financial Closer.			
	<u>Bujagali II</u>				
	2004	New international competitive bidding process selected Sithe / AKFED			
	2005-7	Negotiations with EPC contractors, environmental review, resettlement			
	2007	Financial closer			
	2012	Commercial operation			

Source: Yescombe (2017)

Notes: AKFED - Aga Khan Fund for Economic Development; GoU - Government of Uganda; EIB - European Investment Bank; IFC - International

The key lessons that arise from the Bujagali Hydropower project financing structure include the following:

- There is high currency risk that needs to be managed because most of the funding is acquired in foreign currency due to the fact that domestic capital markets are shallow and underdeveloped and therefore cannot meet the required quantum of resources or term financing;
- The tariff structure can be frontloaded to accelerate the repayment of debtors in cases where lenders perceive the tenure of the PPP project to be lengthy and unwilling to be paid off at the end of the PPP tenure;
- The key project technical partner may be restricted by the Public Authority or the lenders from disposing of their shareholding to ensure that the project is completed and is operating successfully according to expectations. The exit of a key technical partner reduces the confidence of lenders in the project;
- Innovation is required to balance the divergent interests of project shareholders. In the case of Bujagali project, Sithe wanted to invest more than US\$100 million but did not want to have a long-term investment, while AKFED wanted a long-term investment and control in the project but did not have more money. To reconcile the differences, AKFED invested less than Sithe but the class of shares for AKFED had more voting powers;
- To encourage the private commercial banks into investing in the project, the IDA provided political risk guarantee, while the MIGA provided political risk guarantee to the equity investment by Sithe; and
- Project costs were elevated due to separate social and environmental reviews that were undertaken by the three multilateral development finance institutions (MDFI) that financed the project. There is therefore need for mechanisms that harmonize the undertaking of such social and environmental reviews by different MDFI.

Boxes below shows fact sheets for the following Projects: KivuWatt (Rwanada) and Cenpower (Ghana)

Box 5: KivuWatt (Rwanda)

PROJECT	KivuWatt	
Country	Rwanda	
Project summary	Extraction and processing of methane gas from Lake Kivu, used to power a 26 MW independent power project; a second phase will increase capacity to 100 MW; first project in the world to use methane on such a large scale	
Public authority	Energy, Water and Sanitation Authority (EWSA) of Rwanda	
Project company	KivuWatt Ltd	
PPP contract type / term	Power-purchase agreement / 25 years	
Project cost / funding	\$142.25m / Equity \$50.75m (36%) + debt \$91.5m (64%)	
Investors	Contour Global (USA)	
Lenders	FMO (Dutch DFI)	\$31.5m
	African Development Bank	\$25.0m
	Emerging Africa Infrastructure Fund (EAIF); owned by Private Infrastructure Development Group (PIDG); portfolio previously managed by Frontier Markets Fund Managers, a division of Standard Bank; portfolio management transferred in 2016 to Investec Asset Management.	\$25.0m
	BIO (Belgian DFI)	\$10.0m
	Total	\$91.5m
	All loans are pari-passu, with a term of 15 years	
Other public-sector support	Government of Rwanda (GoR) guarantees EWSA offtake and termination payment obligations	
Other DFI support	MIGA political-risk guarantee for equity investment	
Construction contractor	Civicon Ltd., a majority-owned subsidiary of the Kenyan conglomerate Trans-Century Ltd (cf. Rift Valley Railways); replaced in 2013 by Koch Engineering and Construction (Portugal). The power station uses Wärtsilä generators.	
Fuel supply	Fuel supply is part of the project. Under the Gas Concession Agreement, GoR receives a royalty payment for the gas used.	
O&M contractor	None; O&M is carried out by KivuWatt staff	
Project development	2002	GoR signed MOU with Dane Associates
	2005	GoR signed shareholder agreement with Dane Associates to build 5MW pilot plant Kibuye Power 1 ('KPI'), to be completed 2006; was to be followed by a 35MW plant
	2007	GoR refused to provide a \$18m loan and terminated agreement with Dane Associates (on grounds that they did not account for \$3m development costs); then completed KPI; it also took back the site for the full-scale plant.
	2008	EAIF and IFC appointed to arrange funding; ContourGlobal selected as investor; PPA negotiations began
	2009	PPA signed
	2011	Financial close
	2015	Completion scheduled 2012, but did not take place until 2015 following dispute with and replacement of Civicon

Box 6: Cenpower project

Project	Cenpower
Country	Ghana
Project summary	340 MW power-generation project near Tema, 24 km from Accra and close to the landing terminal for the West Africa Gas Pipeline; the largest (and first 'green field') IPP in the country. Project scope includes a 161 kV sub-station, and delivery and storage facilities for the initial fuel, light crude oil (LCO). It is intended that plant will eventually convert to natural-gas firing.

Public authority	Electricity Company of Ghana (ECG)		
Project company	Cenpower Generation Company Ltd (Cenpower)		
PPP contract type / term	Power-purchase agreement (PPA) / 20 years		
Project cost / funding	Senior debt	\$557m	(62%)
	Mezzanine debt (fuel finance)	\$93m	(10%)
	Equity	<u>\$250m</u>	(28%)
	Total	\$900m	
Investors	<u>Pre-financial Close:</u>		
	Africa Finance Corporation (AFC)		46%
	Cenpower Holdings, owned by Reltub Company Ltd, Ghana		30%
	Infraco Africa (owned by Private Infrastructure Development Group (PIDG)), advised by eleQtra		24%
	<u>Post-financial Close: – \$250m equity provided by:</u>		
	AFC		32%
	Sumitomo Corporation		28%
	Cenpower Holdings		21%
	Mercury Power (owned by African Infrastructure Investment Fund II),		15%
	Netherlands Development Finance Company (FMO)		4%
In June 2016 AFC announced that it was to inject its shareholding in Cenpower into a new joint venture with Harith General Partners, a South African infrastructure fund manager.			

Lenders	<ol style="list-style-type: none"> \$446m 15-year commercial-bank tranche, insured by Export Credit Insurance Corporation of South Africa (ECIC), arranged by Rand Merchant Bank (RMB). ECIC provides lenders with 100% political-risk cover and 85% commercial-risk cover. \$110m 15-year DFI tranche, led by FMO, provided by: <ul style="list-style-type: none"> DEG, Germany; OPEC Fund for International Development; Industrial Development Corporation, South Africa; Emerging Africa Infrastructure Fund (owned by Private Infrastructure Development Group (PIDG); PIDG portfolio managed by Frontier Markets Fund Managers (owned by Standard Bank) until 2016, when it was transferred to Investec Asset Management); Development Bank of Southern Africa \$93m 15-year mezzanine fuel finance from same DFI lenders (with a 5-year grace period from the commercial operation date)
EPC contractor	Group Five, South Africa
Fuel supplier (LCO)	Vitol Group, Netherlands—also responsible for fuel storage
O&M contractor	Cenpower Operations and Services Ltd, a joint venture of AFC, Sumitomo Corporation and Cenpower Holdings
Public-sector support	Government of Ghana (GoG) Government Consent & Support Agreement covering ECG's financial obligations. (GoG was supported by USAID, which paid for its advisers)
Project development	<p>2003 Original developer Cenpower Holdings made an unsolicited bid for the project</p> <p>2006 Joined by Infracore Africa as development partner</p> <p>2010 AFC became lead developer</p> <p>2012 PPA signed</p> <p>2013 Fuel Supply Agreement signed</p> <p>2014 Financial close</p> <p>Commercial operation expected 4th quarter 2017</p>

R.7. Department of Trade and Industry (DTI) Campus (South Africa)

The DTI Campus construction project, involved the offices of the Department of Trade and Industry (DTI) and other players. The project provided 43,000 m² of office space, along with basement parking space and was completed in 2004. Sustainability is an important part of the design, as is communication flow between the buildings as well as integration with the surrounding urban environment.

The decision was taken to use a PPP structure to procure the building, rather than the DTI building its own offices, which would have been difficult given budget constraints at the time. A key aspect of this approach was that the DTI did not design the offices itself, but merely set out design principles and the outcomes required. It was then up to private-sector bidders to come up with innovative solutions that also ensured efficient construction and long-term maintenance.

This was the first government-accommodation PPP in South Africa, but the institutional framework for PPPs was fully-established by the time procurement began in 2001⁷³. Successful PPPs had already been concluded in the road (Platinum Highway) and water (Mbombela Water) sectors. Based on this experience, a strategic framework for PPPs was published by the government in 1999. In 2000 the National Treasury issued regulations for PPPs under the Public Finance Management Act 1999 and a PPP Unit was established in the National Treasury⁷⁴. During the period that the project was being procured the PPP Unit was also developing a PPP Manual and a standard form of PPP contract (based on the contract used in the British Private Finance Initiative (PFI) programme). These both came into effect in 2004. The PPP Unit provided support to DTI in its procurement.

⁷³ Other central government departments followed this approach thereafter (the Department of Education in 2007, the Department of Foreign Affairs—now the Department of International Relations and Cooperation—also in 2007 and Statistics South Africa in 2014).

⁷⁴ The PPP Unit is now part of Government Transaction Advisory Services (GTAC), based in the National Treasury.

The project procurement was through a competitive bidding system and a preferred bidder was chosen in 2002 but failed to reach agreement on a key risk issue during negotiations. Part of the project site had been occupied by a petrol station and hence was contaminated with hydrocarbons. The preferred bidder wanted the DTI to take the risk as they argued that removing this contamination would cost more than had been budgeted. DTI was not prepared to take the risk, and, as a result opted to take the second bidder, the Rainprop consortium. Financial close was reached in August 2003, some 27 weeks after negotiation had begun. In fact, to keep to the very tight construction timetable, Rainprop even began enabling works in February 2003, five months prior to financial close in August.

FACT SHEET

PROJECT	DTI Campus															
Country	South Africa															
Project Summary	Government offices, Pretoria. The first PPP for Government accommodation in South Africa. The campus consists of (seven) buildings (about 43,000 m ²), housing [2,400] staff.															
Public authority	Department of Trade and Industry															
Project company	Rainprop (Pty) Ltd															
PPP contract type/term	Availability payments/25 years															
Project cost/funding	<table> <tr> <td>Senior debt</td> <td>R455.0m</td> <td>(90%)</td> </tr> <tr> <td>16% mezzanine debt</td> <td>R35.5m</td> <td></td> </tr> <tr> <td>Preference shares</td> <td></td> <td></td> </tr> <tr> <td>Ordinary shares/shareholder subordinated debt</td> <td>R15.5m</td> <td></td> </tr> <tr> <td>Total</td> <td>R506.0m</td> <td></td> </tr> </table>	Senior debt	R455.0m	(90%)	16% mezzanine debt	R35.5m		Preference shares			Ordinary shares/shareholder subordinated debt	R15.5m		Total	R506.0m	
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Preference shares																
Ordinary shares/shareholder subordinated debt	R15.5m															
Total	R506.0m															
Investors	<p>Ordinary shareholders</p> <p>55% of the ordinary shares are owned by Historically Disadvantaged Individuals (HDI), through Rainbow Construction (now insolvent), (10%), Prop 5 Corporation (20%), Zwelinzima Holdings (15%), WDB Investments (WDB) and The Association for people with disabilities (APD) (10%).</p> <p>(The 10% shareholding held by WDB and APD was funded by an interest-free loan from the construction joint venture, repayable from dividends)</p> <p>The remaining 45% shareholders are: Reserve Facilities Management (20%), Transnet Property, a division of Transnet (20%), WBHO, Atterbury Property and Parkdev (5%)</p> <p>Preferred shareholders</p> <p>Infrastructural, Developmental and Environmental Assets (IDEAS) fund, managed by Old Mutual (87%)</p> <p>Village Trust-Parkdev (6%)</p> <p>WBHO (6%)</p>															
Lenders	21-year senior debt arranged by Standard Bank															
Construction contractor	Joint venture of WBHO (47.5%), Zwelinzima Holdings (10%), & Rainbow Construction (42.5%)															
Facilities-management contractor	FM is provided by a special purpose company, Experience Delivery Company. Its shareholders are Prop 5 Corporation, Zwelinzima Holdings, Propnet Properties, Mvelaphanda Services, to whom work is subcontracted.															
Public sector support	All payments under the PPP are obligations of the South African government															
PROJECT	DTI															
Project Development	2001: Competitive bidding; 2002: Negotiation with preferred bidder failed; 2003: Reserve bidder Rainprop reached financial close in 27 weeks; 2004: Construction completion															

Lessons

The contractor set out the design principles and the outcome required. This allowed the private sector to come up with innovative solutions that ensured efficient construction and sustainability including long term maintenance.

The successful bidder wanted to negotiate the revision of the terms of the agreement immediately after signing, to include what they called an unforeseen risk at the time of the negotiation. That risk was not an issue with the second bidder. In this regard Public sector contractors need to be wary of clauses that are brought in immediately after signing as these may push the deal amount to unsustainable levels.

The establishment of IDEAS Fund in South Africa is a key learning point for Zimbabwe in its quest to finance infrastructure development. The IDEAS FUND is the largest domestic infrastructure equity fund and invests in economic infrastructure (roads and railways), social infrastructure (housing and public private partnerships) and renewable energy infrastructure (solar and wind projects) in the SADC region. While infrastructure investments are vital for economic growth and have tangible social and environmental impacts, the fund targets investments with potential to deliver strong long-term returns and simultaneously seeks to meet both social and environmental objectives⁷⁵

Box 7: Tšepong Health System Innovation (Lesotho)

In 2000, it became apparent that the national referral hospital and district hospital for Maseru (Lesotho's capital), Queen Elizabeth II (QEII) required replacement. After conducting a feasibility study and engaging transaction advisors, the Government of Lesotho issued a competitive tender for a PPIP project. Tsepong (Pty) Ltd, a consortium comprised of the private South African hospital operator Netcare and various local partners was selected as the preferred bidder. A design, build, equip and operate (DBEO) PPP project began in 2008 and is to last for 18 years up to December 2026, after which the assets will be handed over to Government of Lesotho. Tsepong's role was that of funding and offering operational support to the project. The Government on the other hand, acts as the project manager and also co-finances one-third of recurrent and capital costs (MEFMI, 2016). The main sources of finance for the project were equity and debt.

The Government made significant up-front payments for hospital construction and construction site preparation (approximately US\$58 million) to reduce the risk profile of the project and reduce downstream annual unitary payments. Approximately US\$95 million in financing was arranged through the Development Bank of Southern Africa (DBSA) and the Tsepong consortium contributed approximately US\$500,000 in equity towards capital expenditures. Annual unitary payments of approximately US\$30 million, which reimbursed Tsepong's capital and operating expenses, were not scheduled to begin until hospital construction was complete. A US\$6.25 million grant from the World Bank's Global Partnership for Output-Based Aid (GBOPA) was arranged as part of the PPP contract.

After a decade-long planning effort, Queen 'Mamohato Memorial Hospital (QMMH) opened to serve the people of Lesotho on October 1, 2011. The project was also the largest Government procurement of health services in Lesotho's history. With the contract, the Government greatly expanded the scope, quality, and volume of services available through the new national referral hospital as compared to QEII, with 110% increase in total annual outpatient visits (World Bank, 2016). User fees at QMMH were equal to fees at other public hospitals, so patients paid no more for significantly improved care at QMMH. Maternal deaths and overall death rates fell by 10% and 41%, respectively and still births were down by 22% (World Bank, 2016). Mortality rate has been reduced; a neo-natal care (neo-natal ICU) has been built and this has saved lives of newly born infants. In addition, a new durable structure of the referral hospital was built as compared to the old Queen II hospital. The PPP further brought with it new modernised and advanced medical equipment (CT Scan, MRI scan etc.)

Some of the challenges that have been noted in the implementation of PPPs in Lesotho include:

- a. Disputes between Tšepong (the private consortium) and Government with no dispute resolution mechanisms in place.
- b. Lack of capacity in management of PPP projects on the side of Government. Public authorities can either have internal capacity to manage PPPs or can outsource this function. It is advisable not to outsource processes that the outsourcing entity does not have capacity to monitor or evaluate effectively.
- c. Cost escalation. The financial model had estimated that costs would be at a certain level, but they were in the end more than it was previously anticipated, mainly due to the changing environment the concessionaire had no control over.
- d. Tax – Because of lack of the legal framework, there has been problems regarding different taxes (company tax, VAT, withholding tax, fringe benefit). Some of these taxes were not properly stipulated in the financial model but the Lesotho Revenue Authority is applying them now. Some of these taxes are applied inconsistently and retrospectively.

Despite the challenges that the project faces, it is considered successful because it has been able to achieve what it set out to achieve and investment into the project has grown (MEFMI, 2016).

Lessons learnt

- a. The Government lacked capacity for implementing PPPs, hence it engaged consultants to capacitate officials from the ministry on the PPP operations and necessary skills were created. However, retaining trained staff with necessary skills was difficult due to staff turnover. The long standing policy on staff rotation sometimes also affected specialized trained staff as they were moved to other departments.
- b. The risk of cost overruns and delays in the implementation of the projects were managed through transferring them so that they are borne by the private sector. Construction and operational risk were all transferred to the private operator. The risk that service providers would compromise service quality and delivery was managed through instituting an independent monitor to oversee the clinical portion of the PPIP and also administer the financial penalties resulting from any failure to meet the predefined performance standards (PWC, 2013).
- c. Only variable costs subject to inflation should be inflation indexed. Fixed costs of the contract should not be indexed to inflation.
- d. There is need to allow for some degree of flexibility in long term contracts as long as project risk is not increased.

⁷⁵ See https://aiimafrika.com/funds/funds_ideas/ for details

FACT SHEET: Tšepong

PROJECT NAME	Tšepong																			
Country	Lesotho																			
Project summary	Construction and operation of the 425-bed Queen 'Mamohato Memorial Hospital (QMMH) and related clinics. QMMH is the national referral (tertiary) hospital, and provides primary care to the 500,000 inhabitants of Maseru																			
Public authority	Lesotho Ministry of Health, advised by International Finance Corporation (IFC)																			
Project Company	Tsepong (Pty) Limited Tsepong																			
PPP contract type/term	Availability-based (re hospital building), plus medical services / 18 years																			
Project cost/funding	<p>Total project cost M1.2bn, funded 33% (M400m) by Government of Lesotho (GoL), and 67% (M800m) by Tšepong, as follows:</p> <table border="0"> <tr> <td>Equity (ordinary shares)</td> <td>M10m</td> <td></td> </tr> <tr> <td>Shareholder subordinated loan</td> <td>M40m</td> <td></td> </tr> <tr> <td>Mezzanine loan</td> <td>M60m</td> <td></td> </tr> <tr> <td>Senior loan</td> <td>M690m</td> <td>86%</td> </tr> <tr> <td>Total</td> <td>M800m</td> <td></td> </tr> </table> <p>GoL also funded M86m of ancillary capital works including access roads, electricity, sewerage and telecommunications Global Partnership for Output-Based Aid provided a grant of \$6.25m over the initial years of the project to aid affordability.</p>		Equity (ordinary shares)	M10m		Shareholder subordinated loan	M40m		Mezzanine loan	M60m		Senior loan	M690m	86%	Total	M800m				
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Investors	<table border="0"> <tr> <td></td> <td>Equity</td> <td>subordinated loan</td> </tr> <tr> <td>Netcare Ltd. (South African healthcare company)</td> <td>40%</td> <td>100%</td> </tr> <tr> <td>Afri'n nai Health (Pty) Ltd (investment company for Bloemfontein-based doctors) (Afri'n nai)</td> <td>20%</td> <td></td> </tr> <tr> <td>Excel Health (Pty) Ltd (investment company for Lesotho- based doctors) (Excel)</td> <td>20%</td> <td></td> </tr> <tr> <td>Basotho Women Investment Company (WIC)</td> <td>10%</td> <td></td> </tr> <tr> <td>D10 Investments (investment arm of the Lesotho Chamber of Commerce)</td> <td>10%</td> <td></td> </tr> </table> <p>Equity held by Lesotho-based investors will increase from the current 40% to 45% in year 8 and 55% in year 13 Non-Netcare shareholders funded by separate loans from DBSA</p>			Equity	subordinated loan	Netcare Ltd. (South African healthcare company)	40%	100%	Afri'n nai Health (Pty) Ltd (investment company for Bloemfontein-based doctors) (Afri'n nai)	20%		Excel Health (Pty) Ltd (investment company for Lesotho- based doctors) (Excel)	20%		Basotho Women Investment Company (WIC)	10%		D10 Investments (investment arm of the Lesotho Chamber of Commerce)	10%	
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Basotho Women Investment Company (WIC)	10%																			
D10 Investments (investment arm of the Lesotho Chamber of Commerce)	10%																			
Lenders	Development Bank of Southern Africa (DBSA) M690m senior loan @ 11.6% for 15 years, and M60m mezzanine loan on behalf of the non-Netcare shareholders																			
	<p>Clinical, Soft FM & Equipment Contractor</p> <p>Hard FM contractor</p> <p>Provision of Doctors for private beds</p> <p>Security, gardening, linen & laundry</p> <p>Catering, vending machines, office stationary</p> <p>Procurement & Maintenance of medical equipment & furniture (Maintenance element of this contract has been terminated)</p>	<p>Netcare hospitals (Pty) Ltd</p> <p>Botle Facilities Management</p> <p>Affrinnai & Excel</p> <p>WIC*</p> <p>D10 Investments</p> <p>Medical Equipment Procurement Company (Pty) Ltd *, a joint venture of Affrinnai & Excel</p>																		
Public sector support	All payments under the PPP are obligations of GoL Repayment of senior and mezzanine debt on termination for contractor default																			
Project development	2007: RfP issued; 2007: Tšepong consortium selected as preferred bidder; 2008: Project agreement signed (= commercial close); 2009: Financial close; 2010: Completion of construction of clinics; 2011. Key lesson learnt is that the Hospital construction was completed.																			

