

Public-private partnerships and role in funding energy infrastructure

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This presentation

- PPP policy environment in Namibia and the PPP Unit at MoF
- Relevance of PPPs in Namibia, and in the electricity sector
- Discussion on developing bankable PPPs
- Comments on structuring energy sector PPPs – common issues raised and the Namibian context
 - Treatment of risk
 - Need for sovereign or other guarantees?
- Concluding – the missing link for PPPs is bringing creditable projects to market

Policy and institutional landscape for PPPs

Definition of PPP – *as per draft PPP Bill for Namibia*

- A PPP is a contract between a government institution on one side and a private party on the other:
 - for the provision of public infrastructure assets and/or services for use, either directly or indirectly, by public;
 - through investments made by and/or management undertaken by the private sector entity for a specified time period;
 - where there is a substantial transfer of risk to the private sector; and
 - the private sector receives performance linked payments or rewards

**Involves
substantial transfer
of project life cycle
risks to private
sector**

**The public sector
retains a significant
role in project,
either as the main
purchaser of the
service, or as the
main enabler**

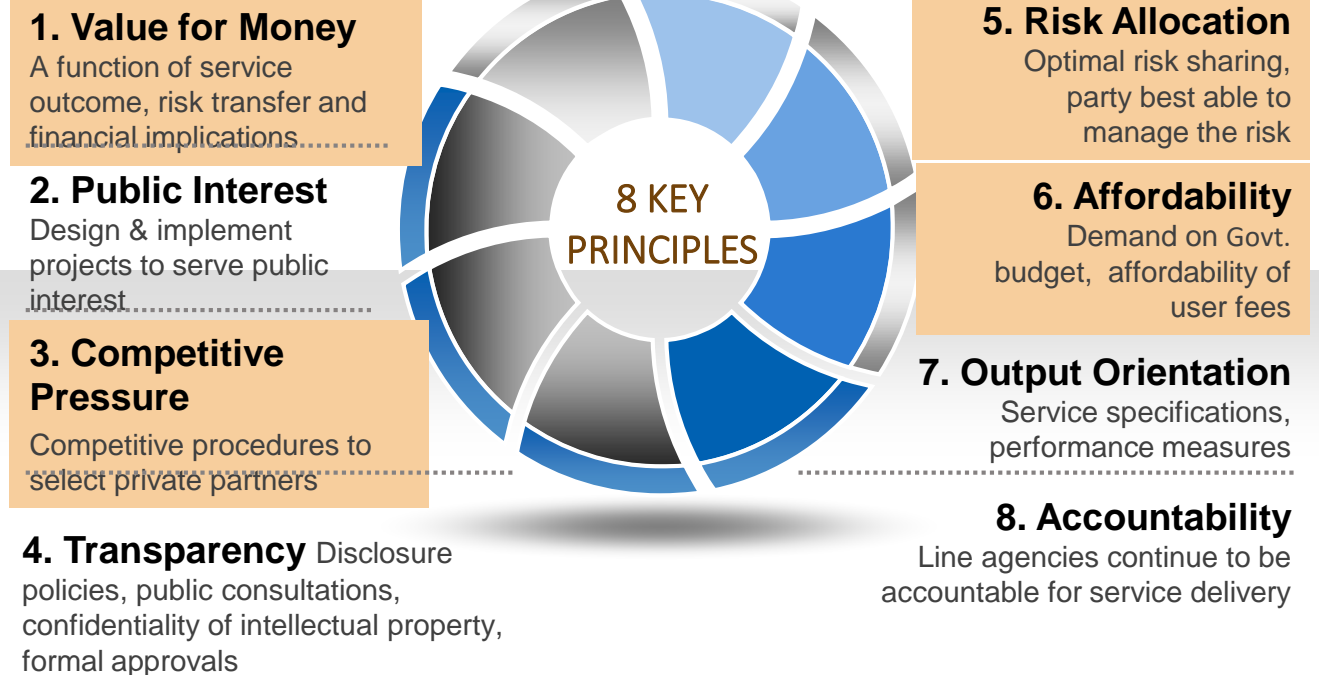
**Private sector
receives payments –
based on
satisfactory
performance - from
govt. and/or user
charges**

**Department's
focus shifts from
managing inputs to
managing the
outcomes**

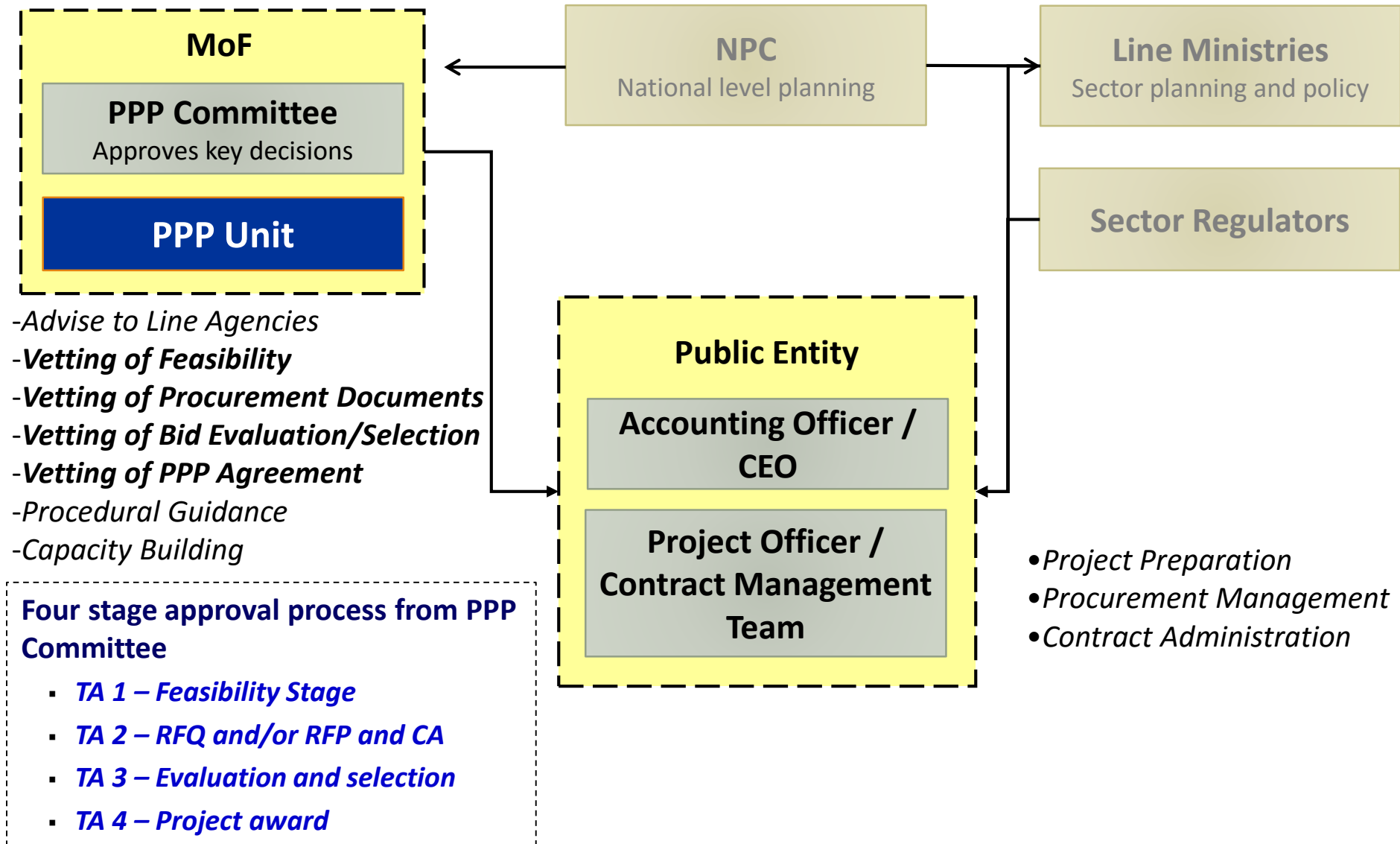
PPP policy and legislation in Namibia

- PPP policy for Namibia was approved by the cabinet in 2012 (available at: www.mof.gov.na)
 - Provides a definition for PPPs
 - Establishes institutional roles – including PPP function at MoF
 - Articulates core principles that PPPs must adhere to
- PPP Legislation under preparation
 - Working draft of the PPP bill ready at the MoF, two rounds of stakeholder consultations have happened
 - Bill has been discussed at the Cabinet Committee on Legislation (CCL) and shall not be passed on for legal drafting and subsequent submission to the Office of the Attorney General

As per the national PPP policy – key principles to be followed while structuring a PPP project



Key institutional roles



PPP Unit has been set up at the MoF - key updates

■ Works in progress

- Development of PPP legislation, cabinet (in-principle) and CCL approvals received – next step is legal drafting and submission to AG Office
- Engagement with the African Development Bank grant funding approved for PPPs related activities: feasibility studies for pilot PPP projects, capacity building (**GPN published on 28 Oct**)
- **Preparing PPP projects:** ongoing engagement with MURD and MME in the areas of affordable housing and renewable energy

■ Other fronts being opened up

- Past work done on identifying candidate PPPs – discussions can be initiated for the next 2-3 most promising projects
- Initiating interactions with additional multilateral agencies to get funding streams for PPP Transaction Advisory works
- Developing internal processes (including setting up of PPP Committee, and process for PPP applications evaluation)
- Staffing: plans to recruit 4-5 staff members, near term plans to have a 7 member PPP team

Relevance of PPPs, and potential in energy sector

PPPs – some representative examples



- Transport
 - Toll roads
 - Airports
 - Railways – integrated concessions (including track infra and operations), operating licenses
 - Port terminals
- Energy
 - Power generation
 - Distribution franchises
 - Transmission infrastructure development
- Urban
 - Water infrastructure and distribution
 - Solid waste management
 - Municipal e-governance

Why PPPs?

- **Availability of Private sector finance (most commonly cited reason):**
 - Through PPPs government can leverage private sector finances to meet infrastructure needs

- **Achieving greater value for money through efficiency gains:**

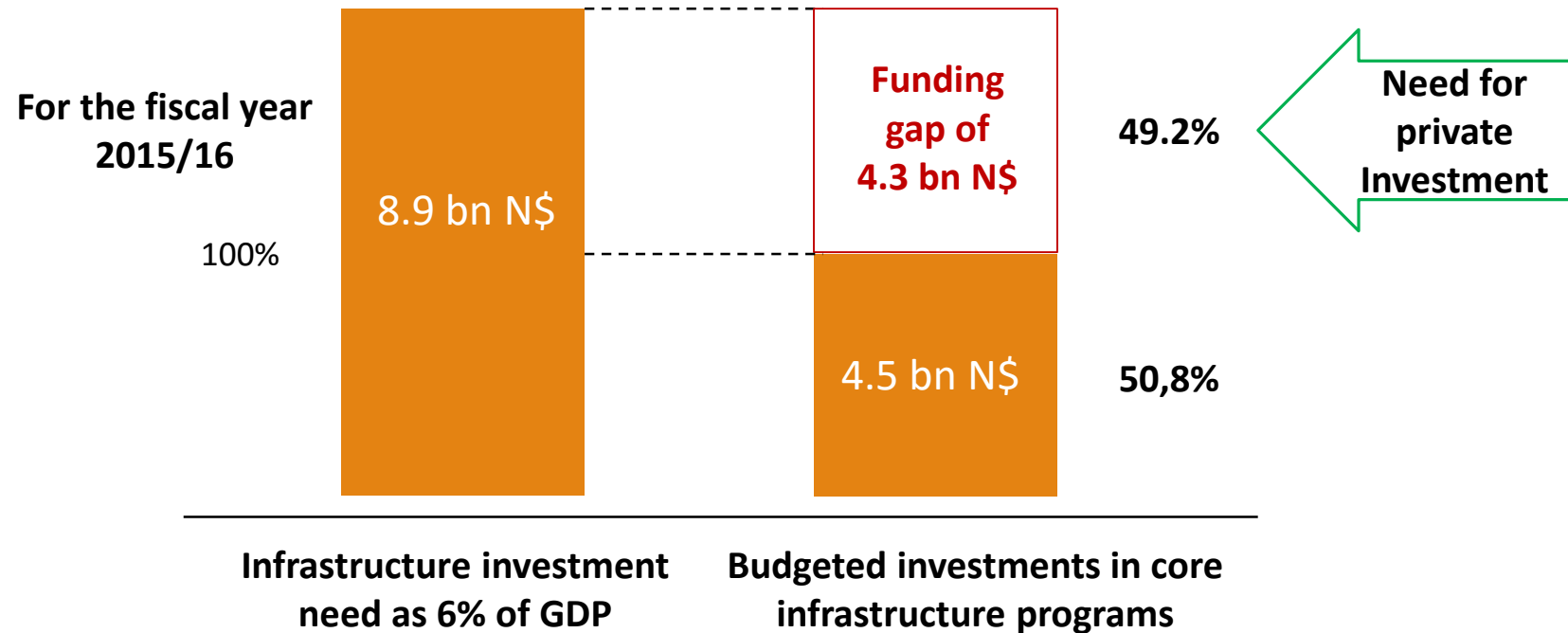
In principle, PPPs can be cost effective (provide value for money) by:

 - Incentivizing on-time and within-budget delivery
 - Optimizing the life cycle costs
 - Providing an opportunity to innovate
 - Optimizing risk allocation

- **Secondary benefit: More opportunities for the private sector to generate efficiencies, expertise and enhance their business**

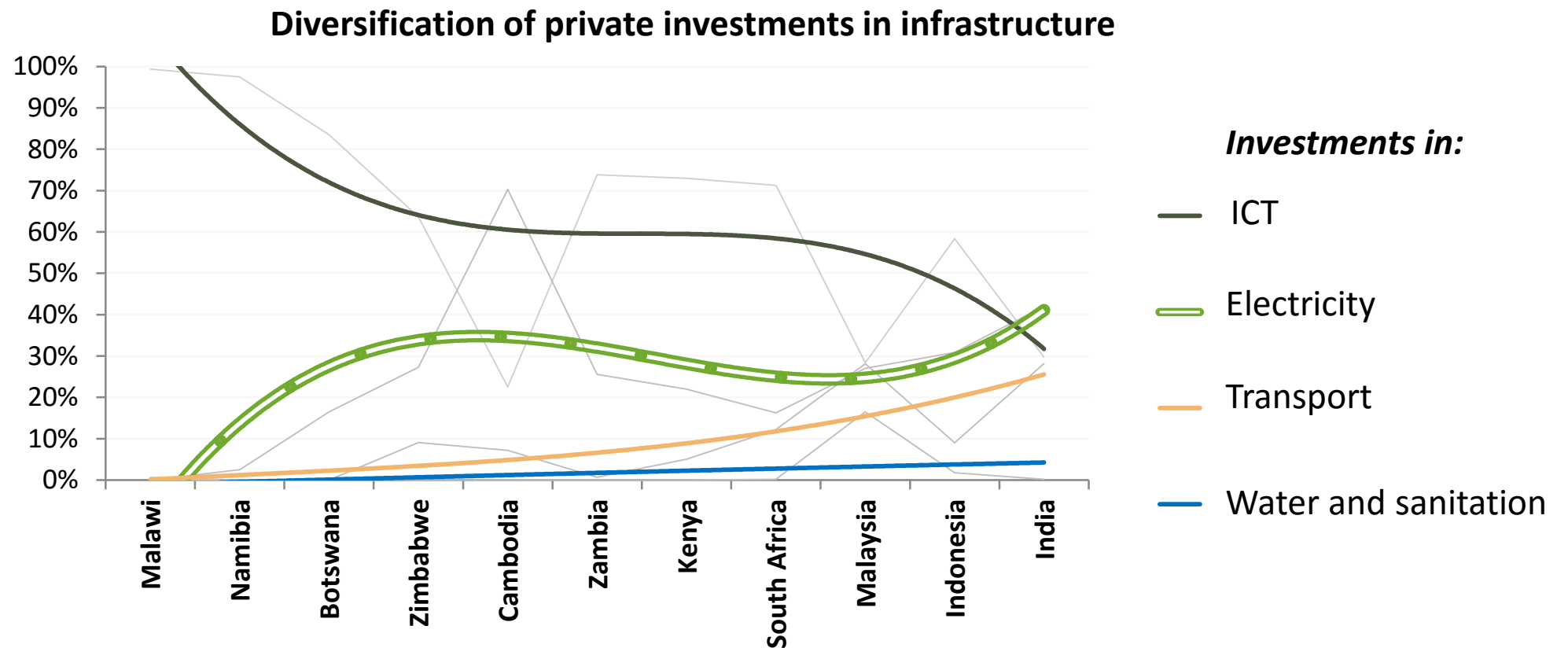
Private investment is not a choice, rather a necessity to ensure adequate infrastructure investments in Namibia

- **Governments are not able to finance all infrastructure development requirements from budgetary resources**
 - For developing countries, annual infrastructure investments equal to 6% of GDP is a conservative estimate or requirement; based on present funding trends in Namibia budgetary resources fund approx. 50%
- **Private investment can help closing the funding gap** and further contribute by enhancing efficiencies in the infrastructure development process



Electricity is usually the infrastructure sector that attracts the first PPP investments

- Demand risk can be easily managed in case of electricity generation projects, relatively easy to structure; Power distribution PPPs however are more nuanced
- Overall substantial investment requirement (normally the infra segment with the highest investment need)



* countries listed by %contribution to world GDP

Source: PPIAF Public Private Infrastructure Advisory Facility (World Bank), database

Developing bankable PPP projects

Private investment in infrastructure cannot be taken for granted

Government's reluctance towards PPPs...

- Infrastructure regarded as vital national asset
- Infra projects have extensive external effects and linkages – govt.'s involved role in planning
- Many Infrastructure developments operate as natural monopolies, risk of abuse of dominant position

Developers may face substantial risks...

- **Demand risk:** less than expected traffic & underutilized capacity
- **Tariff risk:** tight regulation typical for aeronautical revenues - revenue risk
- **Development stage risks:** issues in obtaining statutory approvals
- **Financing risk:** Inability to raise finances / delay in financial closure / increase in financing costs

Key to-dos to make projects bankable & attractive for pvt. Sector

- Adequate project preparation – for high private interest, getting competitive bids
- Sensible risk allocation between government & private developer
- Transparent & balanced framework for tariff setting (including trajectory)
- Viability enhancement measures if required
- Measures to enhance lender comfort

Logical risk allocation is at the heart of PPPs (and bankability)

Risks typically allocated to private sector:

- Design, technology and construction risk
- Demand / traffic risk (PPAs mitigate this in power projs.)
- Operating / performance risk
- Financing risk

Shared risks

- Force majeure
- Demand risk (in some cases)

Binding government to obligations:

- 'Implementation agreements' or 'state support agreements' may be signed in addition to CAs that record committed government responsibilities
- Default on key obligations may trigger compensation or force majeure

Risks typically allocated to government:

- Ensuring land acquisition
- Key statutory approvals
- Ensuring connecting infrastructure
- Change in law / other regulatory risks

Observations on commonly raised issues in context of electricity PPPs

TREATMENT OF RISKS IN CONTRACTS | GOVERNMENT GUARANTEES

Treatment of risks

Force majeure and change in law

- Force majeure and change in law as points of debate in discussions with different stakeholders
- Regarding force majeure and change in law, it is required to look at the risk elements on a disaggregated basis in order to define the relevance/ probability of issues
- These risk elements are not deal-breaker issues but rather finer points - risk elements related to political force majeure and discriminatory change in law concerning the energy sector in Namibia are extremely unlikely



Context of guarantees

World Bank energy sector support program in Kenya

(Select) Risks/Obligations	Contractual Responsibility / additional backstop			Risk Mitigation
	IPP & Lenders (Pvt. Sector)	KPLC (Utility Co.)	Govt. of Kenya	
Plant design	X			
Power Capacity Availability and Output Quality Specifications	X			
Payment of Energy and Capacity, Payments and Fuel charge		X	X	
Force majeure events affecting KPLC		X	X	
Political Event (ongoing obligation)			X*	
Other Force Majeure Events	X			
Termination Payment due to KPLC Default		X		X

* Political Event may include War and Civil Disturbance, Expropriation, Changes in Law, Regulation, Taxes and Licensing Arrangements

Context of guarantees

Govt. support for PPAs in Philippines | Recent examples of MIGA supported projects

- Sovereign backstopping for identified IPP projects in Philippines
 - Context is that electricity tariffs are not cost reflective – this means that the utility (the govt. counterparty to the PPA) anyway structurally depends on treasury support
 - Recognised need therefore that the utility cannot honour PPA payments in case government subsidy payments discontinue
- Representative examples of MIGA support to energy projects (*examples not cherry-picked*)

Country	Project name	Guarantee Value (\$M)	Sovereign rating
Albania	Energji Ashta Shpk	159.4	B1
Pakistan	Star Hydro Power Ltd.	148.5	B3
Uganda	Bujagali Energy Ltd.	115.0	B1
Kenya	OrPower 4, Inc.	99.0	B1
Rwanda	KivuWatt Ltd.	95.4	B+*

Namibia's Sovereign rating (Moody's): Baa3

Moody's Ratings where:

- Aaa – A 3 relate to prime/high and upper medium grades
- **Baa1 – Baa3 relate to lower to medium investment grade**
- Ba1- Ba3 relate to non-Investment grade speculative
- **B1 – B3 relate to highly speculative**
- Caa1 – C relate to substantial risks, extremely speculative, in default

Rounding up discussion on guarantees

- Provision of guarantees need to be a well considered choice, not a default requirement
 - Guarantees are not free – therefore cost trade-offs come in to play
- Guarantees must not have an effect of shifting the burden of appraisal from the project to the guarantor
- Fiscal / contingent liability considerations real and therefore stringent guarantee appraisals are necessary

Missing link - is bringing creditable PPP projects to market

Points of View...

<u>View: Article in The Economist, “Infra Red”</u>	<u>Counterview: (letter to editor published 2 weeks after the article)</u>
<ul style="list-style-type: none">•Ambitious infra development targets – investment requirements•Large proportion to come in as private investments•Pace of infrastructure development has been slow – one reason is low pvt. Investment•There is a need to increase avenues of debt financing available for pvt infra investments•Reduce risk factors that can derail or slow down projects (land acq, govt approvals etc.)	<ul style="list-style-type: none">•It’s a myth that infra investments in developing countries have been hampered by dearth of sufficient funds•No observed example of a ‘bankable’ project that has not been taken up mainly due to lack of equity or debt funds•Poor investment climate / governance issues have hampered investments•Fundamental issue with most projects is lack of dependable revenue model

Graduating from project ideas to attractive PPP project opportunities...

Identified candidate PPP projects in Namibia

Convention & Mixed-Use Centre in Windhoek

Industrial Park at Walvis Bay

Trade Hub in Congo

Agri Produce Hub-Windhoek

Ndjieskoppe Green Scheme Project

Windhoek – Hosea Kutako International Airport
Freeway

Walvis Bay North Bulk Terminal

Windhoek-Rehoboth Rail Commuter Services

Ship Repair Facility

Rundu Town Development

Marina at Walvis Bay

Affordable Housing Initiative

Technical

Commercial

**Regulatory/
legal**

... feasibility

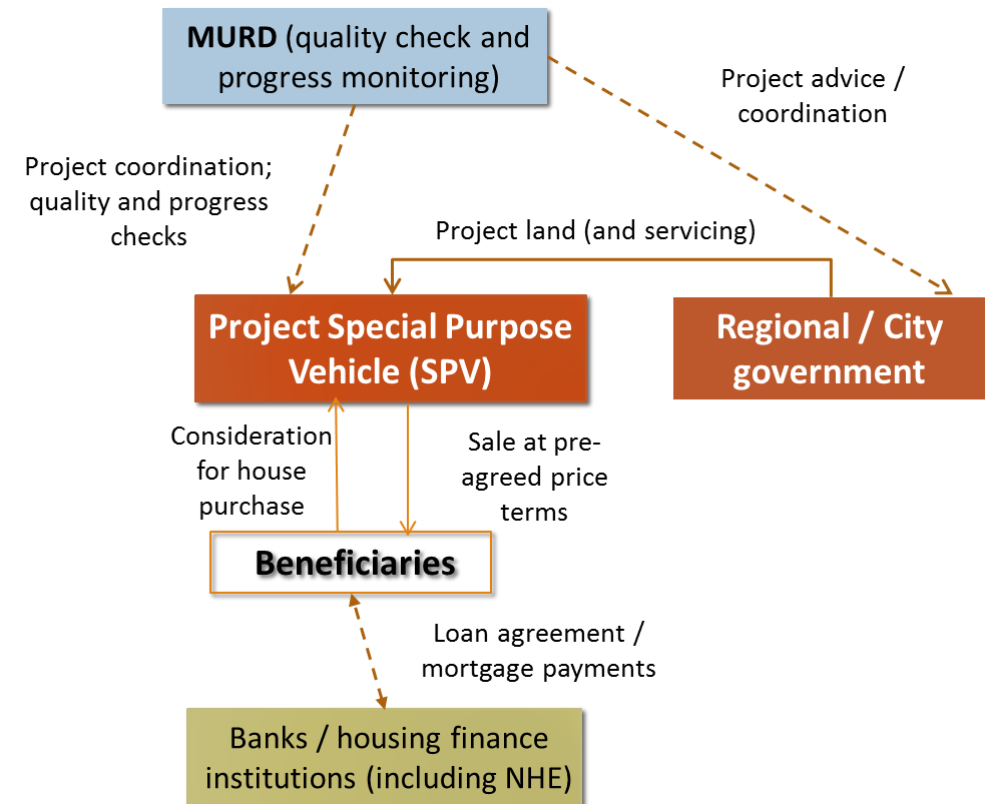
Other hurdles

Promising PPP projects require:

- A legal and regulatory framework that improve the predictability of outcomes
- Robust preparation: Efficient and coordinated PPP processes followed through the project life cycle
- Strong capable public institutions with responsibility for managing PPP contracts

PPP Unit's involvement in developing a PPP concept for affordable housing

- Joint working group formed between teams from Min. of Urban and Rural Development and MoF
- A workable PPP project concept has been prepared for development of affordable housing units
- In the developed project structure the government to completely move away from directly paying for construction of houses
- **Focus on project preparation:**
 - Site selection based on comprehensive criteria (drawn up)
 - Extensive site investigations and documented performance / quality parameters
 - Process for conducting a transparent and well management PPP procurement process to maximize private sector interest – and competitive pressure
 - Financial selection criteria to drive down final selling price of housing units (selection based on lowest committed selling price)
 - Safeguards to deter speculative activity



- Private participation in the electricity sector in Namibia is not a choice but a necessity
- Missing ingredient: a flow of credible, well-prepared PPP projects that we get to the market
- Identification and rigorous preparation for candidate PPP projects is essential for success
- **PPP Unit at the Ministry of Finance** can provide hands-on support

**PPP Unit
NAMIBIA
MINISTRY OF FINANCE**

Thank You

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