By: Cherry Reynard

A New Start for African Infrastructure Development?

Earlier this year, Allianz Global Investors (AGI) committed nearly $120 million, structured as a 12-year loan to the Emerging Africa Infrastructure Fund (EAIF). In doing so, it became the first insurance investor in the EAIF. To what extent does this also mark a turning point for infrastructure investment across the African continent?

Africa's wealth of natural resources has seldom translated into wealth for its citizens. While the reasons for this are myriad, a lack of viable infrastructure has been a clear barrier to the long-term development of African economies. Africa's annual infrastructure gap – the difference between what it has and what it needs – is now estimated at around $170 billion.

Research by the World Bank states that per capital GDP growth could increase by 1.7 percentage points per year if Africa could find ways to bring its infrastructure in line with the median of the developing world.

To date, the way African infrastructure investment has been funded has often been unsatisfactory. On the one hand, few African governments have sufficient cash resources to fund infrastructure investment themselves. This leaves them reliant on either loans from large wealthy countries – such as China – or on private companies willing to take the development risk.

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Both options have clear side-effects. China is estimated to have lent around $95.5 billion between 2000 and 2015. There are real concerns over whether impoverished African countries can pay this back. China has also been accused of “predatory loan practices,” of not using local labour or developing local skills, and even focusing on infrastructure to suit its own ends rather than those of the domestic population.

Private capital has been seen as a route to infrastructure development, but this too comes with its problems. The region is considered high risk, with political and economic instability rife. The risk premium demanded by investors may be considered too high by cash-strapped governments. There are other, practical, considerations. Infrastructure investors risk taking a significant currency risk. African countries often have no developed yield curve and currency hedging is impossible. This is a vital consideration where investors are trying to build long-term, reliable income streams.

Jurie Swart, chief executive officer of African Infrastructure Investment Managers (AIIM), says: “There are a lot of statistics around African infrastructure – that the power generation is the same as Spain, or that 50% of roads are unpaved. And it is true that a lot of projects are not commercially feasible for the private sector...That said, we are seeing an increasing interest in Africa.” He believes that for some time U.S. and European investors have been able to get high rates on private equity investment so haven’t seen the need to invest in high risk areas such as Africa, but this is likely to change as the returns on their domestic assets fall.

Swart admits that some of the risks associated with Africa are real, but in general, he says, governments honour their commitments: “It is not like some developed countries that have reneged on feed-in tariffs for renewables.” He says African governments have generally been more inclined to let go of ‘non-core’ infrastructure development – mobile phone towers, for example – than strategically important areas such as power generation, but this too is happening, albeit slowly. According to the World Bank, power generation would make the most significant difference to long-term economic growth in the region.

New models are emerging. The EAIF is part of the Private Infrastructure Development Group (PIDG). This aims to draw financing to the poorest countries and to develop ways to help manage the risks for private investors, such as through the use of local currency guarantees.

Claus Fintzen, head of infrastructure debt at Allianz Global Investors, says that the EAIF had the right protections in place to ensure the assets were suitable for inclusion in their portfolios and met their fiduciary responsibilities. He says scale remains a problem when investing in Africa: “There is nowhere near the scale to get a meaningful amount of money into the region. We have a big team, but don’t have a local presence. It means we need to rely on the right local knowledge and team up with the right local partners.” While this deters some investors, it is possible, he says.

In all these models, responsible investment is key. Investors encourage local buy-in, recognize the importance of using local labour and helping build local skills. As Swart says, “we have been around for a long time, and if the local community isn’t convinced, we won’t proceed.”

Fintzen adds: “I wouldn’t be surprised if other asset managers move in. It is one of the big topics for agencies such as the OECD and World Bank. It is an important source of diversification for investors.” Encouraging domestic pension fund investment is the next frontier. The AGI move is pioneering. It may not change the landscape on its own, but it could be the start of something far bigger.

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