Money isn’t the Problem

What then is the problem: shortage of bankable projects

Despite good PPP framework South Africa lagging behind

South African municipal infrastructure requirements & financing

Municipal PPP still to take off

South Africa’s municipal PPP’s: lessons for the future

The impact of policy and risk on utility scale projects

Conclusion
MONEY ISN’T THE PROBLEM
SOCIAL & MACRO INDICATORS

- Sovereign rating – Baa3 (Moody’s; stable outlook)
- Sovereign debt/GDP ratio – circa 60%
- SA Population – 58,78m (2019 mid-year estimates)
- GDP – USD 370bn
- GDP growth forecast (Moody’s) –
  - 2019 – 0,7%
  - 2020 – 1,5%
- Unemployment rate – 29%
- CPI – 4,0%
- Central bank rate – 6,5%
- 10-year Government bond – 8,09%
- USD: ZAR – 14,5560
- Euro: ZAR – 16,1295
- Sterling: ZAR – 18,0444
South Africa’s well developed financial services sector can finance bankable PPPs and then some..

- Banks well capitalised with excess liquidity
- Strong institutional market with diversified products & tenors
- Tradeable securities markets
- Well regulated PPP sector
- Project finance has been the cornerstone of the REIPPP
WHAT THEN IS THE PROBLEM: SHORTAGE OF BANKABLE PROJECTS MEETING STAKEHOLDER REQUIREMENTS
BANKABILITY DEPENDS ON NATURE OF PROJECT

The General Project Finance Feasibility Matrix

- Energy, Water & Sanitation, Transport projects’ economics different
- Government support very important – regulations, financial support,
- Market economics – market growth, competitive landscape
- Project economics – service/product price, capital costs, O & M costs, cashflows
- Contract structure – all parties protected?
- Security package – are lenders protected?
- Sponsor support – how deep are sponsor’s pockets in case of delay, lower market demand or higher cost?
MEETING STAKEHOLDER REQUIREMENTS

- Public sector requirements:
  - Risk Transfer –
    - On time & within budget completion
    - Performance to highest minimum operating standards
    - Failure results in private sector bearing the excess costs including penalties
  - Affordability – can the procuring institution pay for PPP within its budget
  - Value for money – cost of own provision v/s provision through PPP

Source: National Treasury 2018 Budget Review
STAKEHOLDERS REQUIREMENTS CONTINUED

- **Private sector requirements:**
  - ✔ Less complex & cumbersome legislation
  - ✔ Transparency in procurement
  - ✔ International procurement framework
  - ✔ Bankable projects
  - ✔ Creditworthy municipalities/other organs of state/ as off-takers
  - ✔ Cashflows – grants flows, municipal/government contribution, project cashflows
  - ✔ Fair return on investment commensurate with risk

- **Community requirements:**
  - ✔ Impact on employees – minimise unemployment
  - ✔ Adequate consultation
  - ✔ Transparency in procurement
  - ✔ Absence of corruption
  - ✔ Elimination of fronting in BBBEE transactions
POLICY REQUIREMENTS FOR SUCCESSFUL PPPS (SA PASSES WITH FLYING COLOURS)

• Detailed legislative framework
  ✓ Public Finance Management Act
  ✓ Municipal Finance Management Act
  ✓ Municipal Systems Act
  ✓ Municipal Structures Act
  ✓ Municipal PPP regulations

• An enabling PPP framework
  ✓ PPP Manual
  ✓ Standardized PPP provisions
  ✓ Municipal Service Delivery and PPP guidelines

• A well functioning & independent judicial system
• A capable PPP civil service
• Private Sector interest
POLICY REQUIREMENTS FOR SUCCESSFUL PPPS
(CONTENTS OF NATIONAL TREASURY PPP MANUAL)

• National Treasury PPP manual
  ✓ Module 1: South African Regulations of PPP
  ✓ Module 2: Code of Black Economic Empowerment in PPPs
  ✓ Module 3: PPP Inception
  ✓ Module 4: PPP Feasibility Study
  ✓ Module 5: PPP Procurement
  ✓ Module 6: Managing PPP Agreement
  ✓ Module 7: Auditing PPP
  ✓ Module 8: Accounting treatment PPP
  ✓ Module 9: Introduction to project finance
DESPITE GOOD PPP FRAMEWORK SOUTH AFRICA LAGGING BEHIND EMERGING MARKETS AND DEVELOPING ECONOMIES
• Public Infrastructure investment spend 6% of GDP

• SOC’s account for 44% of Public Expenditure

• Local government 22% of spend (MTEF: USD 12.64bn)

• PPP’s 2% of total public spend (MTEF: USD 1.27bn)

• Water sector 14% of total spend (MTEF: USD 8.1bn)

• Municipal water PPP’s 0.36% of all PPP’s

Source: National Treasury 2018 Budget Review DBSA calculations

- Average South African spending on PPP’s less than 0.1% of GDP
- Emerging Markets & Developing Economies spending grew from 0.1% in 1991 to 1.1% in 1997
- Post 1997, global PPP’s fell to 0.2% before rising again to peak at 0.6%
EMDE PPP INVESTMENTS (2006 – 2015)

- At 2% of Public Sector Infrastructure Spend, South African PPP’s less than even Low Income Countries (0.2% of GDP)
- Between 1991 & 2015, Top 5 Emerging Markets, including three BRICS countries, account for US$909bn (60%) of PPP’s investment
- US$1.5tr invested in 5000 PPP’s in 121 low-to-middle income countries

Source: PPI Database. World Bank, as of November 2015.
INVESTMENT REQUIREMENTS PER SECTOR

<table>
<thead>
<tr>
<th>Service</th>
<th>10 Yr capital investment (US bn) – 2016F</th>
<th>10 Yr Capital investment % contribution (USD bn) – 2016F</th>
<th>Ave annual capital investment % contribution (USD bn) – 2016F</th>
</tr>
</thead>
<tbody>
<tr>
<td>Water</td>
<td>19.6</td>
<td>27.0</td>
<td>Water 1.96</td>
</tr>
<tr>
<td>Sanitation</td>
<td>12.9</td>
<td>43.0</td>
<td>Sanitation 1.29</td>
</tr>
<tr>
<td>Electricity</td>
<td>12.0</td>
<td>29.0</td>
<td>Electricity 1.20</td>
</tr>
<tr>
<td>Solid waste</td>
<td>0.6</td>
<td>1.0</td>
<td>Solid waste 0.06</td>
</tr>
<tr>
<td>Total</td>
<td>45.2</td>
<td>1.0</td>
<td>Total 4.52</td>
</tr>
</tbody>
</table>

Source: Ian Palmer & Others

**Infrastructure required to address backlogs**

<table>
<thead>
<tr>
<th>Service</th>
<th>Backlogs</th>
<th>Growth</th>
<th>Rehabilitation</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Water</td>
<td>9%</td>
<td>57%</td>
<td>34%</td>
<td>100%</td>
</tr>
<tr>
<td>Sanitation</td>
<td>13%</td>
<td>54%</td>
<td>33%</td>
<td>100%</td>
</tr>
<tr>
<td>Electricity</td>
<td>15%</td>
<td>42%</td>
<td>43%</td>
<td>100%</td>
</tr>
<tr>
<td>Solid waste</td>
<td>1%</td>
<td>75%</td>
<td>24%</td>
<td>100%</td>
</tr>
</tbody>
</table>

Source: Ian Palmer & Others; USD:ZAR – 14.556
## CAPITAL EXPENDITURE, NEW BORROWING AND OUTSTANDING DEBT

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital expenditure</td>
<td>2.1</td>
<td>2.3</td>
<td>2.9</td>
<td>3.3</td>
<td>3.7</td>
<td>3.8</td>
<td>3.7</td>
<td>4.0</td>
<td>5.0</td>
</tr>
<tr>
<td>New borrowing</td>
<td>0.44</td>
<td>0.43</td>
<td>0.45</td>
<td>0.52</td>
<td>0.64</td>
<td>0.63</td>
<td>0.53</td>
<td>0.60</td>
<td>0.8</td>
</tr>
<tr>
<td>New borrowing as a % of CAPEX</td>
<td>21%</td>
<td>19%</td>
<td>16%</td>
<td>16%</td>
<td>18%</td>
<td>17%</td>
<td>15%</td>
<td>15%</td>
<td>17%</td>
</tr>
<tr>
<td>Outstanding debt</td>
<td>3.0</td>
<td>3.1</td>
<td>3.3</td>
<td>3.5</td>
<td>3.7</td>
<td>4.2</td>
<td>4.3</td>
<td>4.3</td>
<td>4.6</td>
</tr>
</tbody>
</table>

Source: NT Municipal Borrowing Bulletin; USD:ZAR – 14.556
### SA MUNICIPAL LONG TERM DEBT LANDSCAPE

<table>
<thead>
<tr>
<th>Muni category</th>
<th>Metros</th>
<th>Total Debt Q3 2018/19 USD bn</th>
<th>Share of total debt</th>
<th>Actual revenue 2018/19* USD bn</th>
<th>Debt to revenue ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>BUF</td>
<td></td>
<td>0,29</td>
<td>1%</td>
<td>0,45</td>
<td>6%</td>
</tr>
<tr>
<td>NMA</td>
<td></td>
<td>0,80</td>
<td>2%</td>
<td>0,71</td>
<td>11%</td>
</tr>
<tr>
<td>MAN</td>
<td></td>
<td>0,70</td>
<td>2%</td>
<td>0,45</td>
<td>15%</td>
</tr>
<tr>
<td>EKU</td>
<td></td>
<td>0,38</td>
<td>9%</td>
<td>2,49</td>
<td>15%</td>
</tr>
<tr>
<td>JHB</td>
<td></td>
<td>1,34</td>
<td>31%</td>
<td>3,59</td>
<td>37%</td>
</tr>
<tr>
<td>TSH</td>
<td></td>
<td>0,71</td>
<td>17%</td>
<td>2,35</td>
<td>31%</td>
</tr>
<tr>
<td>ETH</td>
<td></td>
<td>0,58</td>
<td>14%</td>
<td>2,43</td>
<td>24%</td>
</tr>
<tr>
<td>CPT</td>
<td></td>
<td>0,46</td>
<td>11%</td>
<td>2,78</td>
<td>17%</td>
</tr>
<tr>
<td><strong>Total Metros</strong></td>
<td></td>
<td>3,65</td>
<td>86%</td>
<td>15,17</td>
<td>24%</td>
</tr>
<tr>
<td><strong>B</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other Muni’s</td>
<td></td>
<td>0,57</td>
<td>13%</td>
<td>12,01</td>
<td>5%</td>
</tr>
<tr>
<td><strong>C</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Districts</td>
<td></td>
<td>0,45</td>
<td>1%</td>
<td>1,47</td>
<td>3%</td>
</tr>
<tr>
<td><strong>Total all muni’s</strong></td>
<td></td>
<td>4,3</td>
<td>1%</td>
<td>28,65</td>
<td>15%</td>
</tr>
</tbody>
</table>

Source: NT Municipal Borrowing Bulletin
- Excluding capital transfers
- USD:ZAR – 14,556
SA MUNICIPAL PPP’S STILL TO TAKE OFF
MUNICIPAL WATER PPP PROJECTS

<table>
<thead>
<tr>
<th>Project name</th>
<th>Government institution</th>
<th>Type</th>
<th>Date of close</th>
<th>Duration</th>
<th>Financing structure</th>
<th>Project value USD m</th>
<th>Form of payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Water and sanitation</td>
<td>Kwa-Dukuza Local Municipality</td>
<td>DFBOT</td>
<td>Jan-1999</td>
<td>30 years</td>
<td>Debt: 21% Equity: 18% Govt: 61%</td>
<td>8.93</td>
<td>User charges</td>
</tr>
<tr>
<td>Dolphin Coast water and sanitation concession</td>
<td>Mbombela Local Municipality</td>
<td>DFBOT</td>
<td>Dec-1999</td>
<td>30 years</td>
<td>Debt: 40% Equity: 31% Govt: 29%</td>
<td>12.98</td>
<td>User charges</td>
</tr>
</tbody>
</table>

Source: National Treasury 2018 Budget Review

- 257 municipalities in South Africa – 8 Metros; 44 Districts; & 205 local municipalities
- Varied governance & financial management capabilities
- Most municipal water & sanitation projects financed on balance sheet
- Balance sheets of some large metros constrained
- Potential for further balance sheet borrowing in Category B municipalities but…
DOLPHIN COAST: A CASE STUDY

• Dolphin Coast concession was initiated because the municipality had inadequate funds for
  o Rehabilitation, upgrading and expansion of water & sanitation service (WSS) infrastructure
• 30-year (1999) concession requiring private entity to
  o Oversee, manage & implement the provision of WSS within the boundary of Dolphin Coast municipality
  o Population of 45 000 characterised by wealth and poverty
• Positives of the PPP included
  o Investment in CAPEX and O&M by the concessionaire
  o Improved quality of WSS
  o Reduction in water losses in supply area
  o Fewer leaks
  o Fewer faulty water meters
• Unanticipated increases in raw water tariffs leading to
  o contract renegotiation and
  o reduced investment by the concessionaire
• Higher increases in end-user tariffs
  o Level 4 users (water borne sewers) experienced 119% increase in tariffs
  o Level 2 users (VIP) suffered an 80% increase in tariffs
SA MUNICIPAL PPP’S: LESSONS FOR THE FUTURE
LESSONS FROM MUNICIPAL PPP’S

• Protect low income consumers
• Have a capable civil service to negotiate contracts
• Ensure enough revenue for O&M and regular reinvestment
• Greater transparency by concessionaire and the public entity/state regarding tariffs to engender consumer buy-in and trust
• Size matters for economies of scale
• Look out for national policy changes like municipal boundaries
  ○ Could increase costs for municipality & ultimately ratepayers
THE IMPACT OF POLICY AND RISK IN UTILITY-SCALE PROJECTS
POLICY & RISKS FOR PPPS

- Tariffs must reflect economic cost
- Supply chain regulations must protect the state but be attractive to private
- Supply chain practices must engender private sector confidence
- A predictable & supportive state subsidy/grant framework consistent with long term infrastructure financing requirements essential
- Transparent & enforceable legislative framework critical
CONCLUSION
Elements of successful PPP’s include

• Well regulated global PPP environment essential  
  ✓ To attract domestic & foreign capital in a constrained fiscal environment

• Find balance between consumer protection and sustainable investment  
  ✓ Too low a tariff discourages private investment due to risk-return incongruence  
  ✓ Results in under investment in both CAPEX & maintenance  
  ✓ Too high tariffs hurt vulnerable members of society
Elements of successful PPP’s include

• Well regulated global PPP environment essential
  ✓ To attract domestic & foreign capital in a constrained fiscal environment

• Find balance between consumer protection and sustainable investment
  ✓ Too low a tariff discourages private investment due to risk-return incongruence
  ✓ Results in under investment in both CAPEX & maintenance
  ✓ Too high tariffs hurt vulnerable members of society
Elements of successful PPP’s include

• Generate pipeline of bankable projects by tapping into project preparation facilities of continental &
global DFI’s and ODA
  ✓ Invest in feasibility studies to determine viability & determine potential funding sources
• Triple bottom line important in determining project viability (ESG)
  ✓ Profit
  ✓ Planet
  ✓ People
• Strong institutions – well trained civil service with the requisite experience & skills
• A well functioning & independent judicial system
THANK YOU

Tshepo Ntsimane: Head: Metros/Intermediate Cities/ Water Boards
Email: TshepoN@dbsa.org
Office Number: (011) 313 3163