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Infrastructure Financing in Nigeria: Engagement with MDBs and Recommendations on how Lending Processes could be Improved

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1. Introduction

Similar to most sub-Saharan African (SSA) countries, Nigeria has a huge infrastructure deficit which considerably limits efforts towards achieving inclusive growth, sustainable development, and poverty reduction. With infrastructure stock estimated at 20-25 per cent of Gross Domestic Product (GDP), Nigeria's infrastructure stock is still significantly lower than the recommended international benchmark of 70 per cent of GDP[1]. The 2014 National Integrated Infrastructure Master Plan (NIMP) estimates that a total of US$ 3 trillion of investments, or US$100 billion annually, is required over the next 30 years to bridge Nigeria's infrastructure gap. In particular, the Plan estimates that Nigeria will have to spend an annual average of US$ 33 billion infrastructure investments for the period 2014 -2018[2]. This means that Nigeria will have to more than double its spending on infrastructure from the current 2-3 per cent of GDP to around 7 per cent to make appreciable progress in infrastructure development over the next three decades. In view of this, the Nigerian government has rapidly increased the use of infrastructure finance from additional sources including Multilateral Development Banks (MDBs), bilateral creditors, and Public-Private Partnerships (PPPs), particularly since the return to civilian rule in 1999. Yet, the scale and size of these lines of credit have largely been unable to markedly reduce Nigeria's huge infrastructure financing gap.

In spite of the progress made in the above-mentioned alternative infrastructure financing sources, infrastructure development in Nigeria is still mainly financed by government revenue and domestic debt, with external debt financing playing a relatively limited role. Between 2000 and 2015 for instance, data from the Central Bank of Nigeria (CBN) showed that on average government revenue was used to fund about 70 per cent of the national budget, including capital expenditure, whereas debt, especially domestic debt, was used to funding the remaining 30 per cent. With Nigeria earning significantly less revenue given the fall in crude oil prices since mid-2014, there is no gainsaying the fact that it cannot sustainably step-up investments in critical infrastructure in the next few years without actively engaging with MDBs, bilateral creditors, and the private sector.

Overcoming Nigeria's huge infrastructure challenge by meeting pressing investment needs across various infrastructure sectors such as energy, water and sanitation, and transportation, will determine the extent to which the country can progress in implementing the post-2015 development agenda, and the 2030 Sustainable Development Goals (SDGs) in particular. Therefore, this study examines Nigeria's borrowing experience with MDBs, especially African Development Bank (AfDB), in the past decade with the view to identifying the key factors constraining the country's use of thier lending windows, even when it is qualified to access such finance. The study hopes to provide useful recommendations on how MDBs can improve their engagement and lending processes for financing infrastructural development in Nigeria.

2. Overview of Nigeria's Infrastructure Landscape

2.1 Government Priorities

According to the National Integrated Infrastructure Master Plan (NIIMP) covering 2014 to 20143, the priorities of the Nigerian government for infrastructure development are largely centred on two critical sectors. Particularly, the Energy and Transport sectors which account for 33 percent and 25

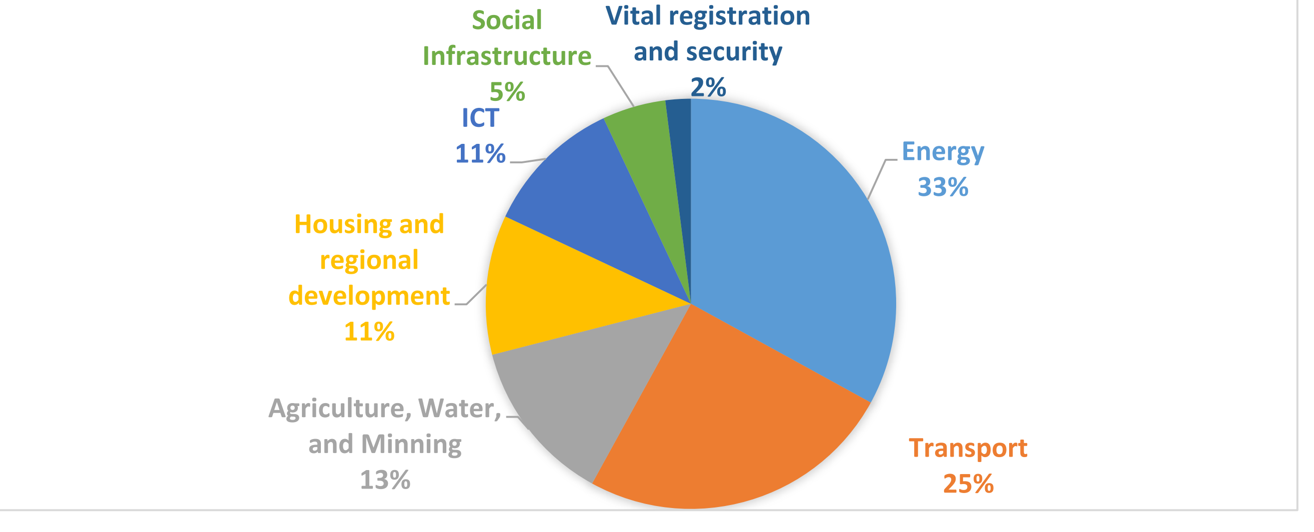
[1] National Planning Commission, 2014
[2] Nigerian Integrated Infrastructure Master Plan, 2014

percent of proposed investment shares, respectively. The Energy sector which consists of oil and gas, as well as power sub-sectors is the foremost priority of the Nigerian government. The focus of the government for investment in energy infrastructure is geared towards: increasing privatization and upgrade of power assets, investing in key pipeline infrastructure projects, increasing hydropower generation and transmission capacity, and increasing oil refining capacity to the point of fully meeting national demand. For the transport sector which consists of road, rail, aviation and maritme (ports) sub-sector, the main focus of the government in the Transport sector is largely channelled towards the road sub-sector. The areas for transport infrastructural development that have been identified by the government for the immediate attention include: the expansion, refurbishment and rehabilitation of major cross-national road and rail transport links; Improvement of cross-modal connectivity links; Improvement of urban transportation; Upgrade and renovation of major airports; and Upgrade of inland ports (NPC, 2014)[3].

The priorities of the Nigerian government in the Energy and Transport sectors is unsurprising given the deplorable state of both sectors. Access to energy services in Nigeria remains very low despite the country's endowment with abundant energy resources (fossil fuels, hydro, solar, tidal, geothermal and biomass). It is estimated that more than 100 million people of an overall population of about 180million Nigerians, have no access to electricity at all and only a third of demand for power is supplied from the National Grid (and those that are connected face frequent power cuts)[4]. It is further estimated that USD 1 trillion (USD 600 billion for power and USD 400 billion for oil and gas) is required for the development of the energy sector over the next three decades (USD 20.6 billion per annum)[5]. In a similar vein, transport infrastructures across the country are in extremely dilapidated conditions, especially road networks. While aviation infrastructure remain substandard, rail and maritime infrastructures are in worse conditions.

Other major priorities of the government for infrastructural development in Nigeria include: Agriculture Water and Mining (13 percent), ICT (11 percent), and Housing and Regional Development (11 percent). *See figure 1.*

Figure 1: Proposed Investment Share across Critical Sectors in Nigeria



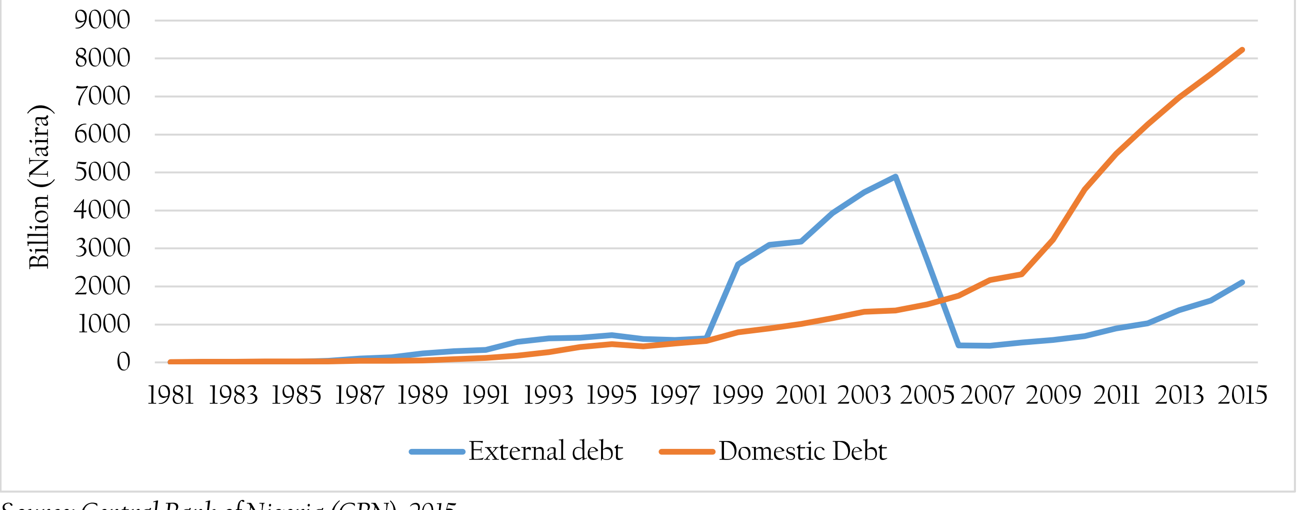
[3] See Annex for priority infrastructure projects outlined in the 2016 National Budget.
[4] National Planning Commission (2014), " National Integrated Infrastructure Master Plan (NIIMP) Draft Report
[5] Ibid.,

Source: National Integrated Infrastructure Master Plan (NIIMP), 2014-2043

2.2 Borrowing Pattern

Nigeria has incurred substantial amounts of domestic and external debts. Particularly, Nigeria's domestic debt has been on a steady rise since the 80s; rising from below N500 billion to over N8 trillion in 2015[6] *(figure 2 and 3)*. On the other hand, Nigeria's external debt, typically owed to foreign creditors such as MDBs and Eurobonds, has been higher than domestic debt prior to 2006. Nigeria's external debt took a 83 percent dip between 2005 and 2006 following the Paris Club debt cancelation in 2006, and has remained lower than domestic debts incurred by the Nigerian government *(figure 2)*.

Figure 2: Nigeria's Public Debt Profile



Source: Central Bank of Nigeria (CBN), 2015

Figure 3: Percentage Share of Various Sources of Borrowing in Nigeria

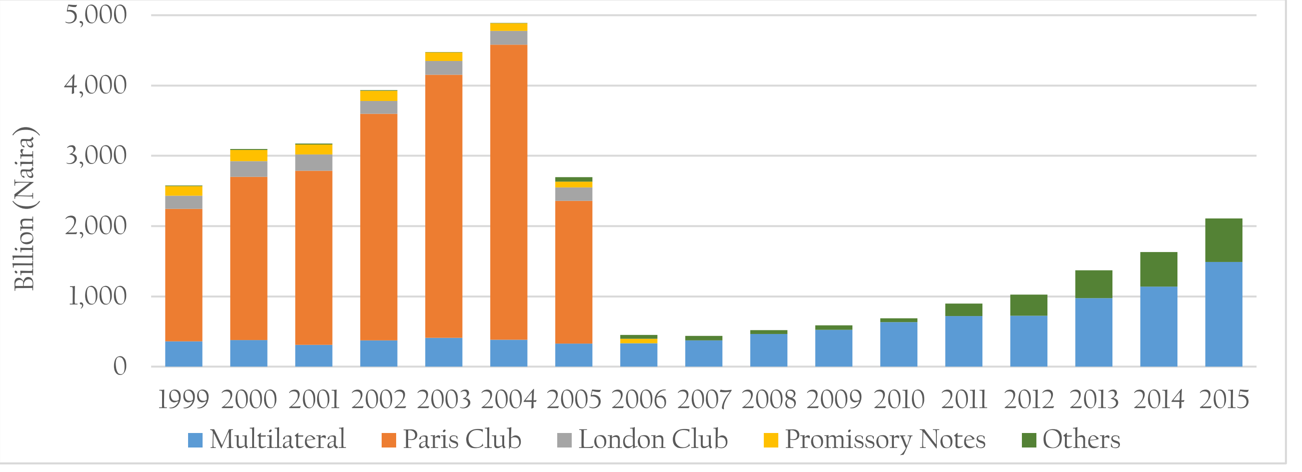
Year	CBN	Deposit Money Banks	Non-Bank Public	Privatization Proceeds	Other Funds
2004-2007	0.0	38.1	49.6	0.0	12.3
2008-2011	0.6	68.3	71.6	0.4	-45.1
2012-2015	12.3	37.0	20.2	1.4	29.1
Average	**4.3**	**47.8**	**47.1**	**0.6**	**-1.3**

Source: Central Bank of Nigeria, 2015
Note: Other funds include: Public, Special and Trust Funds, Treasury Clearance Funds, excess reserves, FG's contribution to the External Creditors' Fund.

Following the Paris club debt cancellation, which constituted a major portion of Nigeria's eternal debt pre-2006, the country's external debt profile has been largely dominated by debts from multilateral creditors since 2005 (*figure 3*). After the dip in 2006, Nigeria's external debts has been rising steadily since 2007, reaching 78 percent of the 2005 level in 2015. Besides multilateral creditors, bilateral and commercial (Eurobonds) creditors "Others, have increasingly played key roles in Nigeria's borrowing patterns since 2011 *(figures 4)*.

[6] Central Bank of Nigeria, 2015

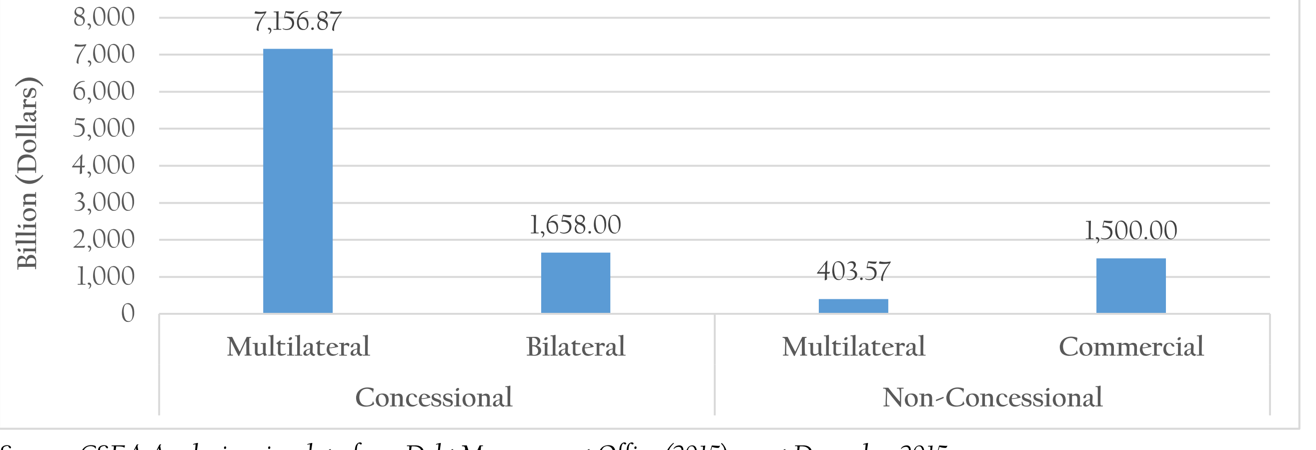
Figure 4: Nigeria's External Debt



Source: CSEA Analysis using data from Debt Management Office (2015)
Note: "Others" include: Bilateral and Commercial (Eurobonds) debts

Despite its MIC status, Nigeria's external debt is still dominated by concessional loans (82.2%) relative to non-concessional loans (13.9%)[7]. This is largely due to Nigeria's debt strategy that places more emphasis on concessionary borrowing.

Figure 5: Concessional and Non-concessional Loan for Nigeria's Infrastructure Financing



Source: CSEA Analysis using data from Debt Management Office (2015), as at December 2015

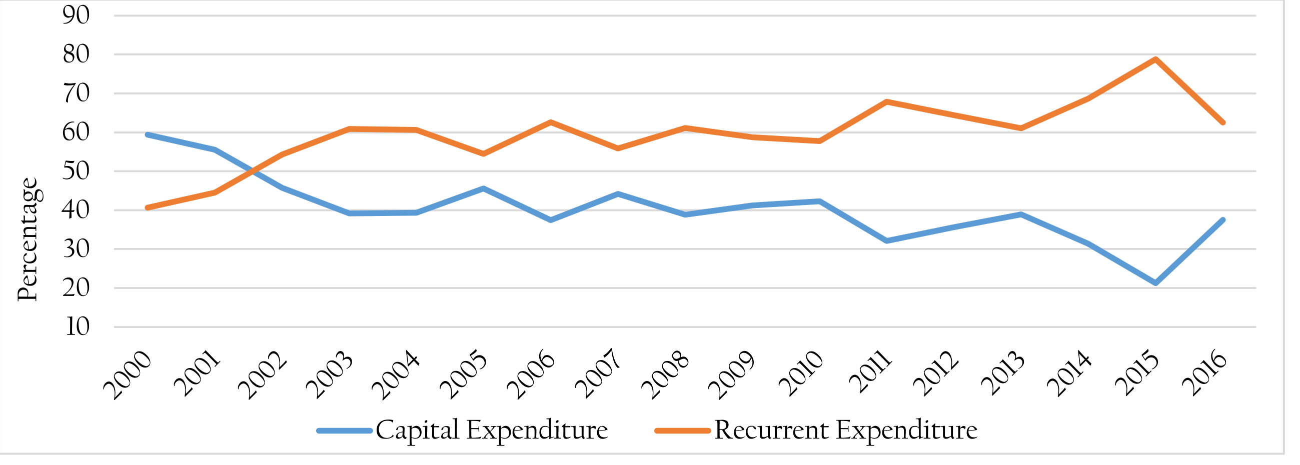
2.3 Infrastructure Trend

The trend in infrastructure investment in Nigeria can be roughly tracked with the trend in capital expenditures, as contained in the annual national budget *(figure 6)*. The size of the capital budget is the total amount of fund budgeted for appropriation in projects and capital assets, and this has a moderating influence on the improvements of existing facilities, and the extent of assets acquisition and maintenance[8,9]. Until recently, capital expenditure in Nigeria was primarily financed using revenue from crude oil exports, with debt and private sector financing playing a limited role. The reliance was largely as a result of high crude oil prices in the international crude oil market, and

[7] Debt Management Office, 2015
[8] Bhattacharya, D., Iqbal, M.A and Khan, T.I (2009). "Delivering on Budget FY 2009-2010: A Set of Implementation Issues". A Centre for Policy Dialogue (CPD), Bangladesh
[9] Kwanashie, M. (2013) "Capital Budget and National Development" Presented at the 43rd Annual Accountants Conference of Institute of Chartered Accountants of Nigeria, Abuja.

Nigeria was a major player. While this boom period was clearly beneficial to Nigeria, the price volatility in the international crude oil market meant that revenue flows were both unpredictable and unstable. In view of this, both national and sub-national budgetary allocations to various critical infrastructural sectors such energy and transportation have fluctuated considerably, proving to be unstainable.

Figure 6: Nigeria's Capital and Recurrent Expenditures

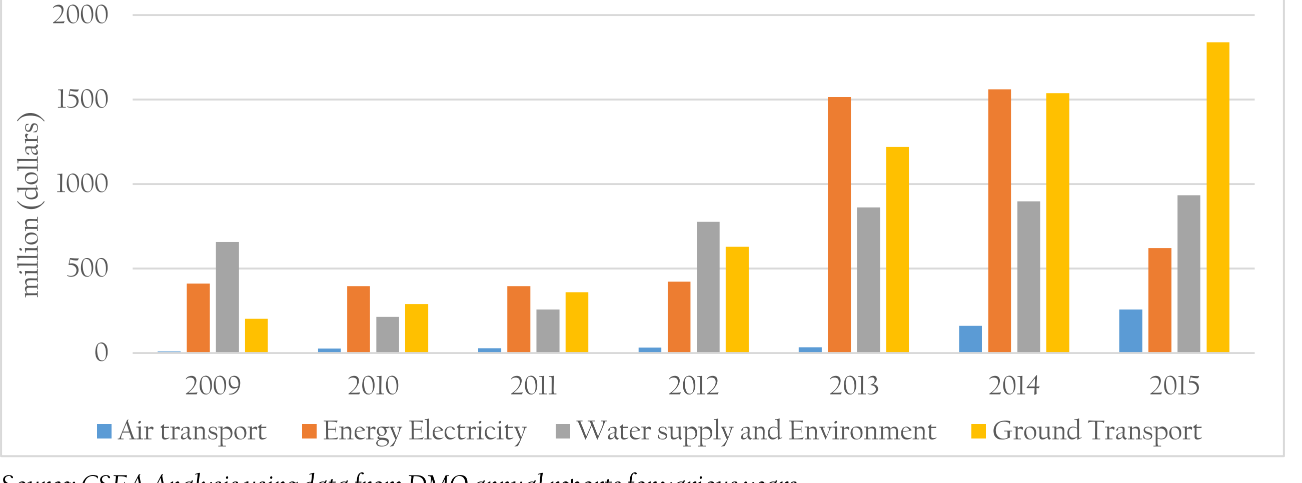


Source: CBN, 2016

Note: These figures are budgeted/planned expenditures and does not reflect actual spending.

Given that the extent to which the capital budget can be fully implemented is severely constrained by (oil) revenue shortfalls, the Nigerian government typically rely on debts from domestic and external creditors to finance investment in priority sectors. Domestic, and especially external, debts have mainly been allocated to sectors that line up with the objectives and priorities of government, especially since 2013 *(figure 7)*. This is such that external debts have been tied to projects on the basis of them featuring in national budget. In 2015, highest allocations of external debt were targeted to Multi-sector project spending (26.80 percent) and health and Social welfare (12.20 percent in 2015). Allocations were also made to air transport (2.40 percent), electricity (5.81 percent), ground transport (3.90 percent), rail transport (6.86 percent), road transport (6.42 percent), water supply (5.82 percent) and environment (2.89 percent)[10].

Figure 7: Sectorial Allocation of External Debt in Nigeria



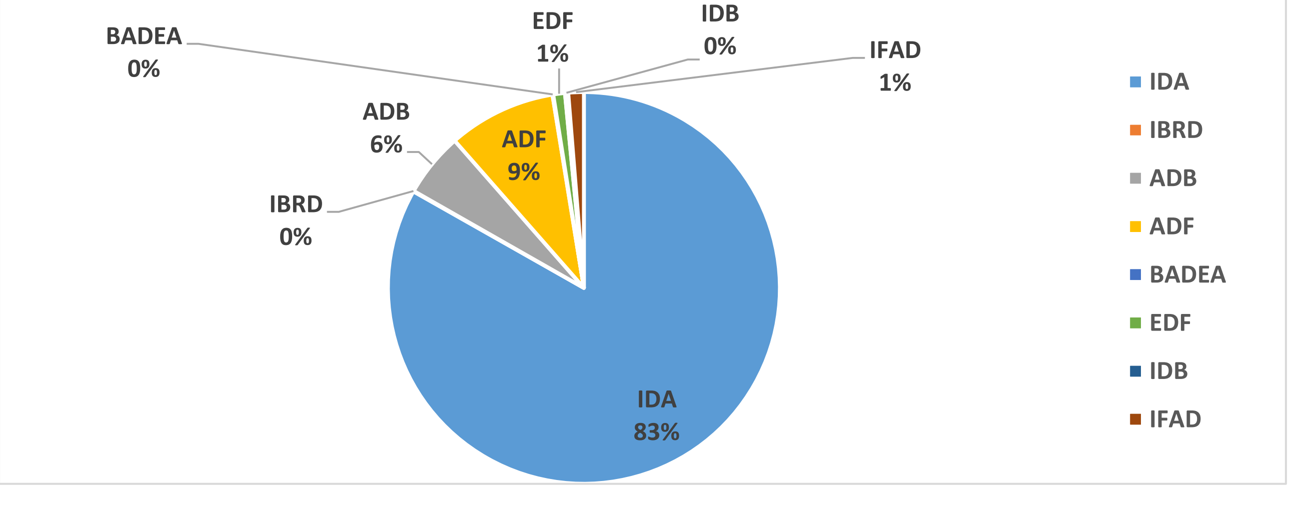
Source: CSEA Analysis using data from DMO annual reports for various years

[10] Debt Management Office, 2015

3. Nigeria's Cooperation with MDBs

3.1 Engagement and Experience with Key MDBs

Engagement with MDBs is a key part of Nigeria's external financing sources. Multilateral creditors including the World Bank Group (International Development Association; IDA, and the International Bank for Reconstruction and Development; IBRD), the African Bank Group (African Development Bank; ADB, and the African Development Fund; ADF), the European Development Bank (EDF), Arab Bank for Economic Development in Africa (BADEA), International Fund for Agricultural Development (IFAD), and Islamic Development Bank (IDB) have been the main source of external debt financing for Nigeria *(figure 8)*. Although there has been increased borrowing from the multilateral window, its proportion as a percentage of total external debt outstanding, their share however reduced from 80.63 percent in 2011 to 70.54 per cent in 2015. Stand alone, the IDA accounted for 58.69 per cent (USD 6.29 billion) of Nigeria's external debt, while borrowings from the AfDB group was about 10 per cent (about USD 1.07 billion)[11]. Considering the fact that the AfDB is meant to be a specialized bank for Africa and by extension Nigeria, as well as the fact that Nigeria has blended access to concessional and non-concessional loans from AfDB, the proportion of external debt secured from the AfDB appear relatively low. This may not be unrelated to certain business practices and financial policies which have been identified to constrain lending from the AfDB. Specifically, some of these constraining practices and policies bother on the bureaucracy involved in accessing loans from the AfDB before and after loan extension, pricing and size of AfDB loans, perceived weak technical and knowledge services offered by the AfDB, lending and credit rating policies etc[12]. On the other hand, Nigeria is the sixth biggest borrower from the IDA in 2015, which accounts for the bulk of Nigeria's external debts[13]. The underlying reason for this is not unrelated to the scale, level of concession, and the various highly specialized technical, knowledge and policy design services that accompany IDA lending. The IDA carries out analytical studies in loan recipient countries to help build the knowledgebase that allows for intelligent design of policies. Also it has developed a system of financing which is based on countries' risk of debt distress, a design that helps countries ensure sustainability of debt obligations.



[11] International Development Association, 2016. Retrieved: http://ida.worldbank.org/financing/ida-financing

[12] Humphrey, Christopher (2014) "The African Development Bank: Ready to face the challenges of a changing Africa?" Stockholm: Expertgruppen för biståndsanalys (EBA)

[13] ibid

Figure 8: Multilateral Sources of Financing for Nigeria

Source: CSEA Analysis using data from Debt Management Office (2015), as at December 2015

Going forward, the Nigerian government's aims to further increase the composition of the public debt portfolio in favour of external debt; from 16% as at 2015 to 40% for the 2016-2019 period, as contained in its Debt Management Strategy[14]. The recent emphasis on external financing is largely driven by the rising cost 0f domestic debt, especially high market interest rate, and the need to use more long-term external financing, with relatively lower interest.

3.2 Key Constraints and Challenges

Two key issues in MDBs' business practices have been identified so far as constraints to Nigeria's engagement with MDBs, especially with AfDB. First, MDBs are characterized by excessive bureaucracy in loan approval process and lengthy procurement process which offsets their attractive financial terms. According to the World Bank (2013), it takes an average of 28 months for IBRD and IDA to move a project from the initial identification phase to the first disbursement of funds. Other MDBs have similar long waiting periods. For instance, it took AfDB and AsDB an average of 13 and 11 months respectively, between project initial identification and board approval of loans. Like other countries, Nigeria also face multiple processes and requirements when applying for MDB loans. These include: lengthy internal review, rigorous safeguards for social and environmental concerns, and strict rules on the use of funds by borrower. AfDB has even a more complex process, with fully 20 formal review and approval steps required between the initial request for financing and board approval[15]. Borrowing countries like Nigeria face further delays and hurdles in conforming to the procurement requirements of MDBs, further delaying project implementation[16] on the nature of infrastructure project being financed, this process can take up to another year. While this rigorous business practices is aimed at improving project quality, available evidence suggests that they are a major deterrent to external financing for borrowing countries, like Nigeria[17], in sharp contrast to domestic and private financing.

Second, weaknesses in knowledge services and policy advice is identified one of the major shortfalls in engagement with MDBs. One of the expected comparative advantages in borrowing from MDBs is the knowledge transfers and technical assistance related to specific infrastructure projects that developing countries get. While the World Bank Group (WBG) is known for its top-level knowledge services to clients, AfDB is perceived to be weak in providing such services. This weakness has clearly been one of the factors limiting the demand for AfDB services by countries.

Beyond the business practices of MDBs, it is important to note that country-specific factors such as foreign exchange crisis and risks, play a role in a Nigeria's decision to borrow externally. On this basis, the Nigerian government, for instance, largely substituted external financing with domestic financing, after the Paris Club debt relief in 2005. However, with the rising cost of servicing and refinancing domestic debt as well as their short maturity period, the Nigerian government is currently increasingly placing emphasis on increasing external financing.

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[14] Debt Management Office, 2015

[15] Humphrey, Christopher (2014) "The African Development Bank: Ready to face the challenges of a changing Africa?" Stockholm: Expertgruppen för biståndsanalys (EBA)

[16] World Bank Corporate Scorecard, 2013.

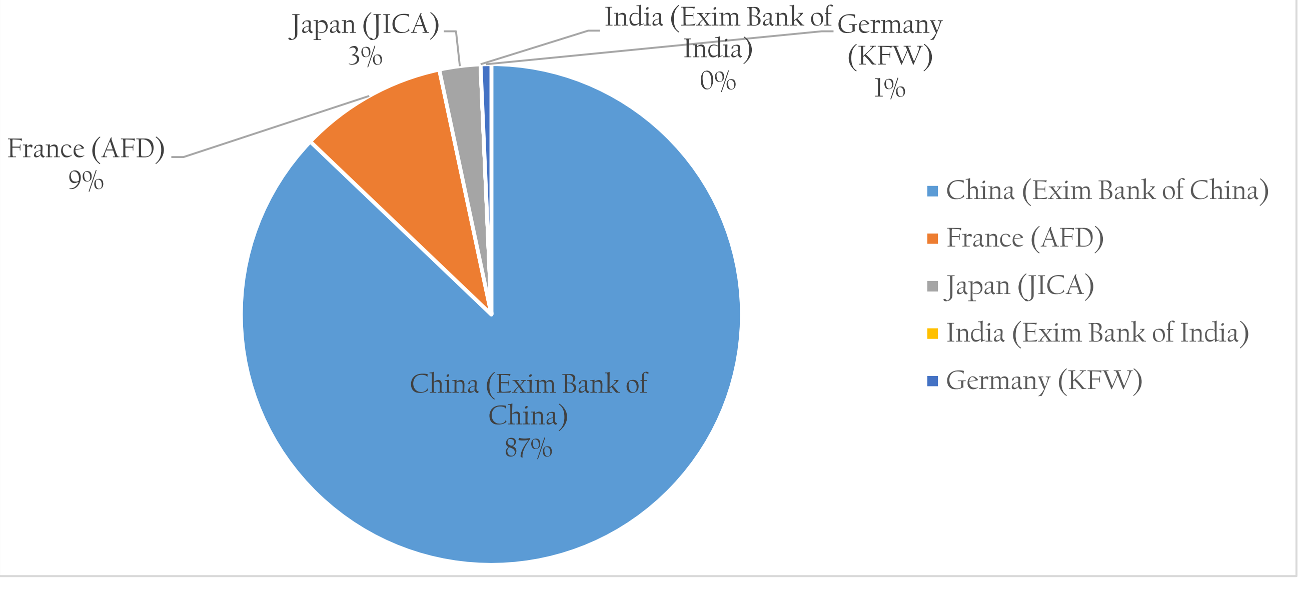
[17] Romilly Greenhill, Annalisa Prizzon and Andrew Rogerson (2016) "The Age of Choice for Development Finance: Evidence from Country Case Studies" London: Overseas Development Institute

4. Alternative Infrastructure Financing Sources

The Nigerian government is increasingly exploring alternative sources of finance outside the MDBs, for infrastructure development. Major alternative sources include: bilateral donors, private finance, and official development finance (ODA).

Lending from bilateral creditors have increased as a proportion of total external debt outstanding from 8.01 per cent in 2011 to 15.47 per cent in 2015, with borrowing from China accounting for the bulk of bilateral debt outstanding of 87.13 per cent (13.48 per cent of total external debt USD 1.4billion). This is followed by France through the Agence Francaise de Developpement (AFD) which accounts for 1.47 per cent (USD 157.95 million) of total external borrowings[18]. The trend in the past decade at increased "Chinese financing" for projects is evident all over Africa, with the China Exim bank having pledged USD 1 trillion for financing in Africa.[19] Another perceived underlying factor for the resort to "Chinese financing" would be the concessionality of the loans advanced the China Exim bank. Some being in the form of commodity swaps with African countries; including Nigeria and also the technical assistance that accompanies such loans particularly for infrastructure projected financing loans. The significance of the concession involved as being a factor in determining financing decision for the government in Nigeria is particularly highlighted by the fact that as at the end of December 2015, concessional creditors and non-concessional creditors accounted for 82.2 per cent and 17.8 per cent of external loans respectively. The bulk of the non-concessional loans was in the form of Eurobonds (78.8 per cent of total non-concessional debts). Even then, although commercial debt (Eurobonds) outstanding increased as a proportion of external debt outstanding from the past five years, there has however been no new borrowing from this window between 2011 and 2015. Particularly, Eurobond debts outstanding of USD1.5 billion accounted for 13.99 per cent of total external debts outstanding in 2015, the same amount at 8.82 per cent in 2011(DMO, 2015).

Figure 7: Bilateral Sources of Financing for Nigeria



[18] see Annex for Nigeria's External debt profile as at 31st December 2015

[19] South China Morning Post 2013 http://www.scmp.com/business/banking-finance/article/1358902/china-provide-africa-us1tr-financing

Source: CSEA Analysis using data from Debt Management Office (2015)

Another notable feature of most government's projects and programmes over the time, has been the promotion of private sector investment/participation in infrastructure development. This was driven by the prolonged dismal performance of public enterprises in infrastructure financing and service delivery. Some level of success has been recorded in the years following the various policies of government aimed at incentivizing private investment in infrastructure development in Nigeria. Drawing from the World Bank PPI database, over the last fifteen years, Nigeria has attracted a total of $39.362 billion dollars in private investment in infrastructure for 51 projects cut across 7 economic infrastructure sectors (Airports 0.51 per cent, Electricity 6.37 per cent, ICT backbone 72.2 per cent, Natural Gas 1.72 per cent, Ports 18.22 per cent, Railways 0.015 per cent, Roads 9.71 per cent) with the highest investment being in ICT infrastructure (72.2 per cent)[20]. At the sub-national level, each state government is responsible for developing its policies with regards to infrastructure development and PPPs. Some states such as Lagos state have been active in promoting the use of private finance for infrastructure. For instance, the Lagos State Roads, Bridges, and Infrastructure Development Board Laws of 2005 and 2007 established a framework for the use of PPPs in roads. The State also created an Office of PPPs in 2008 to provide technical support to facilitate the implementation of PPPs. Since then, in 2011 the Lagos State PPP law was implemented which gave the Office of PPPs the authority to operate across all sectors and not just roads. However, current private financing and investment patterns have not satisfactorily delivered expected results. For instance, while the Nigerian government have implemented PPP frameworks and mechanisms, weak political will and capacity limitations have constrained the impact of PPPs on the Nigerian economy[21]. PPPs in Nigeria face major challenges such as non-availability of long term financing (10-15 years) with attractive interest rates for the investment opportunities in the sector, as well as global credit and financial crisis limiting foreign private investment.

ODA has also been instrumental in providing alternative sources of infrastructure finance for Nigeria. However, ODA is insufficient to meet the huge funding requirements for development across all developing countries: an estimated $4.5 trillion is required to finance critical sectors in developing countries between over 15 years, which is far greater than available ODA funding, which reached an all-time high of $135 billion in 2013 (WEF, 2015). The dearth of ODA suggest the need to deepen and improve engagement with other sources for financing infrastructural development in Nigeria.

[20] World Bank PPI database http://ppi.worldbank.org/snapshots/country/nigeria

[21] 3rd ICRC PPP Stakeholders Forum, 18th July 2012.

5. Conclusions and Recommendations

Nigeria has huge infrastructure gap that cannot but solely financed with government (oil) revenue. For the period 2014-2043, Nigeria's infrastructure plan is to finance the following sectors in order of priority: Energy, Transportation, and Agriculture and Water and Mining. Nigeria's public debt portfolio is largely dominated by domestic debt (84: 16), but government's preferred debt management strategy (2016-2019) is to increase external financing. Despite its MIC status, Nigeria's external debt is still dominated by concessional loans (82.2%) relative to non-concessional loans (13.9%). This is largely due to Nigeria's debt strategy when places more emphasis on concessionary borrowing. While factors such as excessive bureaucracy and procurement requirement has played a significant role in limiting Nigeria's external borrowing, Nigeria still engages with MDBs. However, high foreign exchange risks seem to be the most important factor limiting use of external financing, especially since 2005.

Lastly, there is a prevailing need for the Nigerian government to increase its engagement with MDBs, especially given its current Debt Management Strategy for the 2016-2019 period which emphasizes increasing external financing. Much more, there is an urgent need for MDBs, especially the AfDB, to significantly streamline their business practices with the aim of, for instance, reducing the number of months it takes borrowing countries to receive loan disbursements. It is expected that this reform will considerably incentivize countries, including Nigeria, to raise long-term infrastructure financing through its lending windows. The insufficiency of ODA and the volatile nature of other alternative sources of finance support the need to strengthen MDBs' engagement with developing countries like Nigeria.