Nigeria Economic and Power Sector Reform Programme (EPSRP)[1]

Overview

This operation is an ADF loan of UA 100 million with a first tranche of UA 67 million and a second tranche of UA 33 million. It was approved by the AfDB Board on 1st October 2009. It was originally anticipated that first tranche disbursement would take place in March 2010 and the second tranche in September 2010. It represents both the first Bank PBO in Nigeria, and the first Bank PBO in the energy sector. It is the largest sectoral PBO that the Bank has approved over the evaluation period.

The origin of the operation was a proposed power sector project which AfDB wished to take forward within a context (as discussed in a meeting of the Bank's Nigeria Management Country Team Meeting focusing on Implementation of the Bank Group Strategy in 2008-9) of the unwillingness of the Nigerian authorities to undertake non-concessionary borrowing, and a consequent decline in the Bank's portfolio in Nigeria, and the need identified by the Bank to restructure Nigeria's borrowing on AfDB terms to finance private sector projects in infrastructure. AfDB originally envisaged (as recommended by the Mid Term Review of the Nigeria CSP in March 2008) a Power Project as an ADF Loan of UA 73 million (from Nigeria's 2007-2010 ADF allocation) with additional possible cofinancing from the Bank's Private Sector window as part of a Public Private Partnership arrangement.

An identification mission took place in November 2008 which aimed to identify potential energy sector projects and to assess the progress of sector reforms and advise on any complementary studies prior to project preparation and appraisal by the Bank. The Mission identified six potential operations for ADF funding:

- Reinforcement of Transmission system in Abuja (USD 156 million)
- Technical Assistance and Studies for Small Hydropower Development (USD 57.8 million)
- Solar Energy Projects (USD 8.3 million)
- Small Hydropower Projects (USD 2.2 million and USD 0.8 million)
- Rehabilitation of Transmission and Distribution Networks at Rano/Kibya and Karaye in Kano State (USD 8.3 million)
- Construction of a 15MW Hydrostation at Shia Falls in Nasarawa State (cost USD 28.7 million).

In addition, the following possible projects were identified for potential funding from the Bank's Private Sector Window:

- Increase in Hydro Generation Capacity (USD 32.9 million).
- Construction of Small Hydropower Stations and Water Bottling Plant (USD 30 million).
- Construction of a 450 MW Gas Fired Power Station in Kano State (USD 500 – 700 million).
- 30 MW Wind Farm Project (USD 65 million).

[1] This note was prepared based on a review of project documentation and interviews with Bank staff.

It was recognised in the Bank that there was a large potential for private sector involvement in infrastructure, but that major technical, organisational, institutional, regulatory and policy challenges would need to be addressed, though it was also noted that Infrastructure Concession Regulation Commission (ICRC) which was established in November 2008 was intended to play a leadership role in closing the infrastructure gap and in accelerating market development for PPPs.

The Bank requested a priority list of projects to be financed by ADF loan from the Federal Ministry of Finance. An operation in support of the Abuja Transmission Line Project was envisaged, and that a prequalification process was undertaken by the Nigerian authorities to recruit consultants to work on project preparation in March 2009.

However, during the Bank's 2009 Annual Meeting, confirmed in a letter from the Federal Minister of Finance (18th May 2009), the Nigerian authorities instead requested a quick disbursing loan of UA 118 million to "support Nigeria's efforts aimed at mitigating the adverse impact of the global financial and economic crisis". The Bank replied (from Vice President Ordu, 8th June 2009) to say that Bank was considering extending a fast-disbursing policy-based loan through an Energy Sector Economic Reform Program which would use the remaining balance of Nigeria's ADF-XI country allocation.[2] The Bank stated that:

> "Consistent with the Government development agenda and the Bank's strategy in Nigeria, the program will aim at addressing key reforms to be implemented in the short-run, in order to create an enabling environment for massive private sector investments in the power sector. Towards this end, an updated review of the energy sector reforms on key strategic, policy, institutional and regulatory constraints is necessary. This review will provide a sound basis for the planned program."

It was agreed within the Bank that OINF3 would assume the leadership of the operation, with guidance and technical inputs from other Bank relevant departments (ORWA, OSGE, OPSM). A field mission took place during June 2009 to design the operation, followed by an appraisal mission in August 2009. The "Economic and Power Sector Reform Program" (EPSERP) was prepared as an ADF loan of UA 100 million. It was originally intended to disburse the first tranche of loan (UA 67 million) in late October or early November 2009. The Letter of Development Policy from the Federal Minister of Finance of Nigeria stated the objective of the budget support was to "finance strategic interventions and development priorities in the context of the 2009 budget that would help address power sector bottlenecks, sustain non-oil real GDP growth rate, reduce unemployment and alleviate poverty."

The Appraisal document notes that the focus on the power sector reflected analysis in the joint AfDB and World Bank Investment Climate Assessment Report that power is the most binding constraint on doing business in Nigeria. The Appraisal Report also noted that:

> "The structuring of the proposed budget support as the EPSERP is an opportunity for knowledge building within OINF which normally uses investment loans to intervene in RMCs. Important lessons can be drawn from the EPSERP on how budget support can be leveraged to improve infrastructure installations and institutions."

The programme was conceived as having two main components:

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[2] Along with a capacity building project to support PPP and railway sector management of UA 8.4 million.

1. Improving the electricity system in a sustainable manner and the business environment, to support the Government to reach its targets in terms of power generation, transmission and distribution and also support the Government's efforts to improve the business environment by 2011 which is the time horizon for the private sector to enhance its participation in the development of the power sector.

2. Sustaining growth through sound macroeconomic policies and budget priorities. This component was noted as being consistent with the second pillar of the World Bank Development Policy Operation aimed at sustaining growth through sound macroeconomic policies and budget priorities. The rationale was to maintain a donor coordinated dialogue with the FGN on sustaining ongoing Public Financial Management and fiduciary reforms which were identified as critical for the achievement of the development outcomes of the EPSERP, particularly in the context of the global crisis.

The programme was envisaged as providing finance as an input along with eight areas of action in support of the overall improvement in the performance of the power sector:

(i) Refurbishment of existing power plants.

(ii) Refurbishment and reinforcement of transmission and distribution infrastructure.

(iii) Completion of the National Integrated Power Projects (NIPP) programme.

(iv) Approval of transitional management boards for PHCN successor companies.

(v) Building of gas processing and supply infrastructure.

(vi) Adopting of a new gas pricing structure.

(vii) Adoption and initiation of a coal to power policy framework.

(viii) Implementation of the Renewable Energy Master Plan.

Loan negotiations took place in October 2009 and the loan was approved by the ADF Board on 28th October 2009. The preferred dates for loan disbursements for the Nigerian authorities were 31st March 2010 and 30th September 2010. The conditions precedent to First Tranche Disbursement were the following:

(i) Opening of a special account in foreign currency at the Central Bank of Nigeria dedicated to receiving the loan proceeds.

(ii) Establishment of a formal technical coordinating committee composed of representatives of from the Federal Ministry of Finance (FMF), the Federal Ministry of Power (FMP), the Power Holding Company of Nigeria (PHCN), and the Bureau of Public Enterprise (BPE).

(iii) Cumulative release of at least 75% of 2009 budget appropriation to the power sector.

(iv) Achievement of available power generation capacity of 4.500 MW.

(v) Establishment of Management Boards for PHCN successor companies.

The second tranche conditions were:

(i) Cumulative release of 100% of 2009 budget appropriations to the power sector

(ii) Achievement of available power generation capacity of 6,000 MW.

The appraisal document identified five main risks: the affect of the global downturn (including lower oil prices) on FGN revenues, failure by the NNPC to deliver gas processing and supply infrastructure to enable gas supply to be continued, unrest in the Niger Delta affecting gas supply, non-resolution of labour disputes, and unavailability or late disbursement of funds to continue or complete works. Ongoing processes of dialogue with Niger Delta activities and labour representatives were identified as mitigation measures, along with the "revamped commitment of the FGN to accelerating reforms", and progress in completing three new gas processing facilities.

However, effectiveness of the loan was delayed as it required approval by the Nigerian Legislature. This was not secured until December 2010. In August 2010, President Jonathan (who had assumed the Presidency in May having been Acting President over the previous year) had set out a Roadmap for Power Sector Reform envisaging the development of a national electricity grid using public and private financing, and the privatisation of electricity generation and distribution.[3] President Jonathan had made improvements in power supply one of his key objectives as President ahead of his re-election bid in 2011.

Issues

It had originally been intended to take forward the Bank's support for the power sector in Nigeria through a series of investment projects. The change to a PBO was the result of the Nigerian government's desire for quick disbursing support in the context of the impact of the international financial crisis and in particular fears that the oil price falls would substantially impact on government revenues. The amount of support provided was determined by the level of resources remaining unused under Nigeria's ADF allocation.

There was a clear rationale in this context for the Bank's proposal in response to this request that there should be a power sector PBO because of the identification of the poor performance of the power sector as a critical constraint on growth outside the oil sector and for suggesting that support should be provided in this form rather than through the investment projects that were in the process of being identified and developed. It also provided an opportunity for closer involvement by the Bank in the wider sectoral reform process.

However, political uncertainty in Nigeria and a smaller than feared impact of the international financial crisis on oil prices meant that first, the loan was not approved on a timeframe that would have allowed it to meet the liquidity needs that prompted the initial Nigerian request for quick disbursing support, and second that the loan was in the event not required for the macroeconomic reasons that had originally been envisaged.

Since the loan has only recently been approved by the Nigerian legislature, it remains to be seen whether it will prove to be an effective instrument to support the high profile initiative for power sector reform that the Nigerian government is taking forward, given that it was designed principally to provide short-term fiscal stabilisation, with loan conditions focused on

[3] See Vetiva Research Flash Note, 31st August 2010.

ensuring that the budget for the power sector was protected during 2009, rather than on the longer-term structural reform measures that form part of the wider power sector reform roadmap. In this context, the position of the Bank's support will need to be determined within the overall financing required for the Power Sector Roadmap reform process that was announced in August 2010. It also remains to be determined how the Bank can most effectively engage with the renewed reform effort in terms both of advisory support and further investment projects.