FUNDING OF POWER PROJECTS: THE ROLE OF THE CENTRAL BANK OF NIGERIA (CBN)

Paper Presented By
Mallam Sanusi Lamido Sanusi
The Governor, Central Bank of Nigeria

Represented By
Dr. Kingsley Chiedu Moghalu
Deputy Governor (Financial System Stability)
Central Bank of Nigeria

At the
“Gas To Power: Prospects and Challenges” Conference
Organised by
The National Association of Energy Correspondents (NAEC)
at
Eko Hotels & Suites
Victoria Island, Lagos.

Thursday August 19, 2010
1.0 Introduction

I am highly delighted to be invited to deliver a paper at this important forum that seeks to critically examine the prospects and challenges of Nigeria’s power sector.

Nigeria is the most populous country in Africa, the 8th largest oil producer and has the 6th largest deposit of natural gas in the world. Other resources that abound in the country are the large expanse of arable land, vast solid minerals deposits and abundant manpower. Yet in the midst of all these, the development of Nigeria’s energy resources has stagnated over the years.

Economists have long established that energy development, interpreted broadly to mean increased provision and use of energy services, is an integral part of economic development. This is generally measured by either energy unit per capita or energy unit per unit of output. It is in this wise that the United States Central Intelligence Agency World Fact-Book reports on per capita electricity consumption in kilo-watt hours (kWh) for 2009 which ranks Nigeria 178th with 106.21 kWh per head, far behind South Africa (4,921.26), Libya (3,281.87), Iraq (1,377.75), Gabon (900.00), Ghana (283.65), Cameroon) (176.01) and Kenya (124.68). This is indeed very disturbing.

Little wonder that the key operators in the country’s real sector represented by the Manufacturers Association of Nigeria (MAN) and the National Association of Small Scale Industries have estimated that
their members spend an average of N1.8 billion on power generation weekly and that the major problem facing the manufacturing sector in Nigeria was the lack of power. At the individual level, it is estimated that about 60 million Nigerians now own power generating sets for their electricity, while the same number of people spend a staggering N1.56 trillion ($13.35bn) to fuel them annually.

The above indices are not appealing. Forums of this nature provide an opportunity for us to periodically examine the nation’s development priorities, where we are, where we want to be, and who’s doing what so as to chart systematic ways of achieving our desired goal of economic development. This presentation is strictly limited to what the Central Bank of Nigeria is doing, from the standpoint of finance and as an economic adviser to the Government, to ensure that our citizens get critical services from the energy sector.

2.0 The Energy Challenge

Electricity generation in Nigeria in 2008 was 7,011.6 MW, consisting of 72.9% of thermal power and 27.1 % of hydro-power. The Power Holding Company of Nigeria (PHCN) accounted for 85.3% of total generation while Independent Power Projects (IPPs) accounted for 14.7%. Total electricity consumption was 2,108 mega-watts per hour (Mw/h), which showed a drop of 6 per cent from the 2007 figures of 2245.5 mega-watts per hour (Mw/h). The oil and gas industry actually declined by 4.76 per cent and had a negative contribution to GDP of -0.93 per cent in 2008 (CBN Annual Report, 2008).

Other notable challenges of power supply in Nigeria are the transmission and distribution networks which are poorly maintained
and inefficiently operated making it difficult to move power from
generation sites to consumption points. The low tariffs coupled with
high level of losses in the system points to the fact that the sector is not
financially viable.

This brings us finally to the question: Where, in all of this, is the role of
the central bank?

3.0 The Role of CBN in Mobilizing Investments in Energy

The Bank’s interest in the energy sector is derived from the desire to
use monetary policy to fast-track economic growth and create jobs. In
other words, to ensure that Nigeria has an electricity supply industry
that can meet the needs of its citizens and power our economy into the
20 top economies of the world by the year 2020.

This is in tandem with the goals and objectives of the National Electric
Power Policy (NEPP) which includes, among others, to:

- Improve the efficiency and affordability of power supply;
- Encourage private sector participation and competition;
- Attract investment; and
- Provide a conducive environment for long term development of
  the sector.

3.1 The Development Finance Role of the CBN

Statutorily, the Central Bank of Nigeria (CBN) was established to
promote monetary and price stability, a sound financial system, and
perform the core functions of currency management. Due to
peculiarities of Nigeria as a developing nation, the CBN Act (2007) (sections 31, 32(i) and 42) has also given the Bank developmental functions through various intervention programmes to improve access to finance for real sector development. The interventions take the form of collaborative programmes, schemes, institutions and policies with the government, development partners and other private sector players. For the Bank to effectively perform this important task, there exists a full fledged Department, known as Development Finance Department to handle all development finance matters. In addition the Infrastructure Finance Office was established and commenced operation on March 01, 2010. Its mandate is to, among others, evolve a sustainable financing framework to stimulate long term financing for infrastructure development of the country.

3.1.1 The N300 billion Power Intervention Fund

The 213th Monetary Policy Committee (MPC) meeting in Abuja on March 1-2, 2010 underlined the need to catalyze financing of the real sector of the Nigerian economy such as power and other economic infrastructure, to attract much needed private sector investment and thereby promote employment generating growth in the country. The MPC accordingly decided, among other measures, to continue with the quantitative easing policy by providing a N500 billion facility for investment in debentures issued by the Bank of Industry (BOI) in accordance with Section 31 of the CBN Act 2007, for investment in emergency power projects dedicated to industrial clusters.
The fund is to be channeled through the Bank of Industry for on-lending to the Deposit Money Banks (DMB) at a maximum interest rate of 1.0 per cent for disbursement to power projects with a tenor of 10 – 15 years at concessionary interest rate of not more than 7.0 per cent. The Africa Finance Corporation (AFC) was appointed to serve as Technical Adviser (TA) on the power projects.

The objectives of the Fund are to:

i. Fast-track the development of the electric power projects, especially in the identified industrial clusters in the country;

ii. Serve as credit enhancement instrument to improve the financial position of the Deposit Money Banks;

iii. Catalyze the removal of regulatory and institutional constraints in the Nigerian electricity sector;

iv. Improve power supply, generate employment, and enhance the living standard of the citizens through consistent power supply; and

v. Provide leverage for additional private sector investments in the power sector.

The MPC also approved in-principle the extension of the Facility to DMB’s for the purpose of refinancing/restructuring their existing portfolios to manufacturers. The aviation sector (Airline operators) was also allowed to partake in the Fund when it became obvious that most
of them were heavily indebted to the deposit money banks in the country.

In order to ensure systematic intervention, the CBN constituted a Technical Committee on Power to work out the modalities for the Power Sector initiative. The membership of committee comprised of various key industry stakeholders including banks, regulators, federal government representatives, technical experts, industry operators and private financiers. The Committee has since completed its assignment and its report would form the basis of the operational guidelines for accessing the Fund. The Governor of the Central Bank is also a member of the President’s Advisory Committee on the power sector.

3.1.2 Highlights of the Project Selection Criteria for the CBN Power Intervention Funding

Eligible power projects to be financed could be promoted by private or public sector sponsors (or a combination of both) and may be structured either as profit-oriented business or a public service, provided that contracted cash-flows or financing support exists to ensure repayment of principal and interest, as well as long term viability. Prospective beneficiaries could be companies already existing and in operation, in design/development, under construction, or existing but operationally inactive.

Two main eligibility criteria are being considered. These are Project-based and Impact-based eligibility criteria. Under the Project-based eligibility criteria, the power promoters wishing to access financing under the Program will need to demonstrate firstly to their commercial bank lenders, and ultimately to the CBN (under the recommendation of
its Technical Adviser) that they are capable of timely principal and interest payments as contracted with lenders and other obligors, and that they are able to effectively deliver their product or service within the Nigerian electricity industry value chain.

The Impact-based eligibility criteria on the other hand, will rate projects on their relative ability to make a substantial impact on the electric power supply deficit in Nigeria. Under the programme, power project promoters will need to demonstrate that they are capable of contributing significantly to the provision of electricity to end-users in Nigeria, in as short a time frame as possible, and in a manner that is sustainable over a long term period, will be given priority.

For the Programme to function effectively, a proper governance structure is being put in place to approve projects which qualify for the facility. In line with best practice, an Approving Committee should be appointed to give the final approval for the utilization of the facility by projects. The Approving Committee shall comprise relevant participants and stakeholders in the program.


This presentation would be incomplete without briefly mentioning the collaborative efforts of the Bank with other government agencies and development partners to improve infrastructure financing in the country. Under the Nigeria Public Private Partnerships (PPP) Project, The World Bank, has in 2008, agreed in principle, to provide a PPP project finance facility of US$315.5 million to the Federal Government of Nigeria [FGN] through the Infrastructure Concession and Regulatory
Commission (ICRC). The facility was structured into two (2) components: Capacity Building and Transaction Support facility of US$115.5 million and the Financial Intermediary Loan [FIL] facility of US$200 million. The capacity building component was meant to support PPP institutional, legal and regulatory capacity building to develop Nigeria’s long term market for infrastructure financing.

Under the FIL component, the World Bank is to provide funding to eligible participating financial intermediaries [FIs] for on-lending to final borrowers. The Africa Finance Corporation [AFC] was identified as the lead FI. The World Bank mission identified the CBN to act as the apex for Infrastructure PPP FIL component.

The roles of the CBN under the proposed functions of Apex are to perform independent review of subproject (sub-loan) applications form eligible participating financial intermediaries to ensure that they fully meet all criteria that have been stipulated for sub-loans that can be financed under the project.

There is also an agency relationship with the Government where the Bank is to receive funds from the government that have sourced from the IDA loan, using procedures and a mechanism approved by the World Bank, and on-lend to PFIs at the agreed interest rate, and under terms and conditions agreed with the FI. Other functions relates to making loan commitments to PFIs for eligible projects, making disbursements to the client project, collecting interest, principal repayments and commitment fees from the PFIs; etc on behalf of the world Bank.

3.2 Review of the Prudential Guidelines to recognize the peculiarities of long term financing.
As part of measures by the CBN to further encourage banks to lend to the real sector of the economy, in particular SMEs, infrastructure and agriculture, the Board of Directors of the CBN approved the amendment of the prudential guidelines on loan loss provisioning. The objective is to take cognizance of the current dynamics in the industry and provide guidance on the recognition and measurement of loans, establishment of loan loss allowances, credit risk disclosure and related matters.

The reviewed Prudential Guidelines recognizes the use of a time-based approach for specialized loans. The time based approach establishes longer time lines for measuring asset quality, based on the gestation periods for projects in the target sectors.

The new prudential guidelines provide a supportive lending framework for the financing of infrastructure projects, including power projects, because they recognize the longer gestation periods inherent in these kinds of ventures and remove a major stumbling block to access to financing – the fear of lending and borrowing by banks and industry operators who want to reduce or avoid bad loans when time lines for measuring asset quality are too short.

### 3.3 Review of the Universal Banking Model

The CBN is in constant consultation with other stakeholders to review the universal banking model in favour of monoline and specialized banking so as to encourage innovation and specialization among banks.
Again this major plank of banking reform will facilitate infrastructure project finance.

3.4 Policy Advocacy

Another important role of the CBN in the funding of the power sector is that of policy advocacy – utilizing the Central Bank’s statutory role as an economic adviser to the Government of Nigeria. In this context, the CBN has remained consistent in its view that what the power sector needs most is not just money. Even more important is the urgent need for the Federal Government of Nigeria to implement reforms that will create an enabling environment for the private sector and other investors to invest in translating our natural gas resources into power. Establishing an appropriate, incentive-based pricing regime for gas-to-power products is the key that will unlock private sector investment.

This policy advocacy role is driven by our conviction that (a) we cannot achieve real development without real sector growth in manufacturing, which can only be powered by appropriate levels of electric power, and (b) the reforms in the banking sector will be incomplete without revamping the power sector because banks need to be able to finance power infrastructure and other areas of the real economy if they are to avoid asset bubbles that can lead to banking crisis.

4.0 Conclusion

There is no doubt that inadequate energy and poor infrastructure have contributed significantly to the economic woes of our country.
The CBN Power Intervention Fund was conceived to provide the much needed long term financing to investors in the power sector. The refinancing window will enable power industry operators whose projects have almost become moribund owing to lack of finance to restructure or refinance them and still have additional resources to bring the project to fruition. It will also ensure that some of the non-performing power industry-related loans that have bedevilled the books of our deposit money banks are refinanced to improve the balance sheets of the banks.

Besides the foregoing measures, the CBN has also pursued several initiatives to provide the enabling environment for investments in the energy sector. These include the maintenance of general price level stability especially the constant fight against domestic inflation and the maintenance of exchange rate stability, both of which are essential for planning. It should be noted that one of the goals of the on-going reforms in the banking sector is to ensure that we have strong and reliable banks that can genuinely and effectively fund the real sector and other development priorities of the government.

The initiatives taken by the Central Bank of Nigeria are only temporary interventions meant to catalyse the economy and open up avenues to attract long term funds that are critically needed for infrastructure development in Nigeria, but which are currently lacking. The most sustainable source of financing long term projects, including the power and energy sector, is to develop the corporate bond market and further liberalise the financial and capital markets to ensure depth, stability and transparency.
As stakeholders in the Nigerian economy, the members of this respected association should acknowledge and propagate the positive elements of financial sector reforms and project the state of the nation’s energy sector in the best form so as to attract prospective power investors from both within and outside the country. The collective goal is to have sufficient and steady power supply, without which Nigeria’s economy cannot experience sustainable growth.

Thank you.