US GOES DOWN THE BELTWAY ROAD

WHAT THE NEW US INTERNATIONAL DEVELOPMENT FINANCE CORPORATION MEANS FOR PROJECT FINANCE IN AFRICA. BY WITNEY SCHNEIDMAN AND KIMBERLY STIETZ, COVINGTON & BURLING LLP.

In October 2018, as the US Senate was locked in partisan warfare over the confirmation of Judge Brett Kavanaugh to the US Supreme Court, an important piece of legislation for the project finance world passed both chambers of Congress with strong bipartisan support.[1]

The legislation, known as the Better Utilization of Investment Leading to Development (Build) Act, was signed into law by President Trump on October 5 2018.[2]

This article discusses why the Build Act is likely to make the US commercially competitive in some of the world's most challenging markets – in Africa and beyond – in a way that it has never been before.

We also address one of the primary motivations behind the Build Act – fairly viewed as a surprising initiative from an administration that came into office promising to eliminate the Overseas Private Investment Corporation (OPIC) and cut development assistance by 30%. That motivation, in one word, is China.[3]

Finally, we offer our assessment of what the Build Act means for Africa.

US Development Finance Corporation

The Build Act aims to "facilitate the participation of private sector capital and skills in the economic development of countries with low-or lower-middle-income economies."[4]

Harnessing the power of the private sector through development finance – sometimes referred to as commercial diplomacy – is an increasingly popular complement to traditional foreign aid around the world.[5]

OPIC has served as the US development finance institution since 1971, investing in more than 160 countries and realising an annual net return for US taxpayers.[6]

This is the ultimate goal of development finance: make money while promoting sustainable economic development around the world and advancing national security priorities.[7]

The Build Act is critical to the creation of a modernised OPIC. To this end, the Act creates a new institution – the US International Development Finance Corporation (USIDFC) – which will merge OPIC and several USAID facilities, including the Development Credit Authority (DCA), the Office of Private Capital and Microenterprise (OPCM), and enterprise funds.[8] With US$60bn dedicated to USIDFC, the new entity will have twice the amount of money to invest compared with OPIC's current lending cap of US$29bn.[9]

The Build Act also incorporates several other important changes that will empower USIDFC to function more competitively in the 21st century. For example:

- Where OPIC could only provide debt financing for projects in emerging markets, USIDFC will allow minority equity investments of up to 30% of total equity in any given project. USIDFC is limited to 35% equity of the agency's total investments.[10]
- The OPIC requirement that there be US participation in a project of at least 25% of the project's value has been changed to a preference, offering more flexibility for investments;[11]
- The new agency will be able to offer technical assistance on projects, which is often essential to a sustainable project;[12]
- Products can be denominated and repayable in foreign currencies, rather than just the US dollar.[13]

An interagency process is under way to work through a number of issues prior to the launch of the USIDFC in September 2019. Specifically, the USIDFC must establish the criteria it will use to invest in projects where no US businesses are participating. Equally important, it must determine the basis on which it will make loans and investments in local currencies.

China

The prevailing view in Washington is that the strong bipartisan support for the Build Act, and President Trump's swift signing of the bill into law, was in large part motivated by the consensus that the US needs to increase its commercial diplomacy to compete with China around the world, and particularly in Africa.[14]

In fact, OPIC's president and chief executive was explicit about this motivation, stating that USIDFC will be "a financially sound alternative to the state-directed initiatives pursued by China that have left many countries deep in debt."[15]

> The Build Act is critical to the creation of a modernised OPIC. To this end, the Act creates a new institution - the US International Development Finance Corporation

Other US officials have argued that China is "pursuing a neo-mercantilist vision" in Africa to "secure an economic foothold, from which it is attempting to secure political, diplomatic, and in some cases military access…."[16]

Another critique of China's approach to development centres on its practice of tying its aid to the use of Chinese labour and companies. Critics argue this promotes Chinese interests to the detriment of job creation and skill development among the local population in countries where Chinese development aid is being implemented.

In 2015, the US and China signed a memorandum of understanding identifying development sectors for enhanced collaboration between the two countries.[17]

The era of cooperation between the two superpowers when it comes to development appears to be over, at least for now. In addition to critiquing China's approach to development, the Trump administration heightened its rhetoric against China and waged a trade war, among other policy changes reflecting increased tension between the two countries.[18]

According to AidData based at the College of William & Mary, the amount of aid given by China and the US is now about equal. As of 2017, it was estimated that China gave or lent US$354.4bn from 2009 to 2014, compared with US$394.6bn in US aid during same time period.[19]

It is estimated that China leverages US$40bn through its varied development finance institutions, monies implemented with no political conditionalities attached under the umbrella of China's One Belt One Road initiative.[20]

In Africa specifically, China has now far exceeded the US in total trade with the continent: in 2010, China conducted over US$92bn in trade with Africa and the US conducted over US$80bn; by 2017, Chinese trade with the continent exceeded US$165bn and US trade with Africa dropped to less than US$37bn.[21]

While debates about China's aid model and how the US can most effectively respond to it will continue, it is without a doubt that the Build Act will make the US more competitive with other development finance corporations in Europe and Asia – and USIDFC gives the US an opportunity to assert itself as a leader in development finance on the African continent.

USIDFC and Africa

Sound arguments are being made for the USIDFC to play a leadership role in streamlining the impact of development finance institutions in Africa.[22]

According to the Washington-based Atlantic Council, between 2012 and 2016, projects in Sub-Saharan Africa accounted for the largest share of commitments (US$14.2bn) of all DFI portfolios, followed by East and South Asia (US$10.5bn) and Latin America (US$10.2bn).[23]

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Nevertheless, African private equity funds continue to struggle, raising only US$1bn in 2017, less than 0.2% of the US$435bn total raised globally.[24]

In 2017, sub-Saharan Africa accounted for 27% of OPIC's portfolio.[25] As of 2018, OPIC's Africa portfolio included 128 projects and an investment of US$6.1bn.[26]

Expectations are that the percentage of the USIDFC's investment in Africa will increase – much of that potentially in the project finance space. For example, Africa's need for investments in roads, ports, railways and other vital infrastructure was estimated in 2018 to be in the US$130bn to US$170bn range by the African Development Bank.[27]

OPIC already responds to Africa' infrastructure needs in a number of ways, for example it provided a US$50m loan guarantee to the Meridiam Infrastructure Africa Fund in 2015.[28]

The Fund is to invest in infrastructure projects in the energy, transportation, environment, and social and telecommunications services sectors.[29] The USIDFC will be able to expand these types of investments.

Power generation is another area of critical investment, as it is estimated that 14% of the global population lacks reliable electricity, with 95% of those living without electricity in Africa and Asia.[30]

OPIC is invested in a number of power generation projects in Kenya, Senegal, Ghana, Guinea and more. For example, OPIC is one of the lead financiers of the 50MW Greenfield Thermal Power Plan in Conarkry, Guinea.[31]

OPIC is providing US$89m of debt financing and a further US$30m of political insurance risk for this project,[32] which will help meet critical power needs where the power supply is lowest among the 140 countries tracked by the World Economic Forum.[33]

In July 2018, OPIC announced the US$1bn Connect Africa Initiative, which will focus on investments in infrastructure, technology and value chains.[34] USIDFC should enhance and expand such initiatives.■

Footnotes

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