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2024 MTBPS

PUBLIC-SECTOR INFRASTRUCTURE

national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

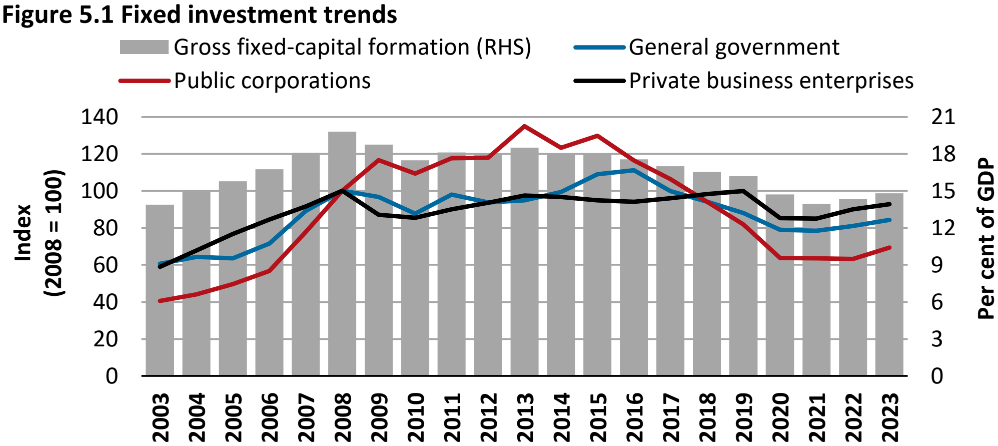
In brief

- Higher investment and more effective delivery of infrastructure are needed to grow the economy and create jobs.
- Government is reforming its approach to infrastructure development, focusing on partnerships with the private sector.
- Lessons from other successful programmes will be used to accelerate infrastructure delivery and adapt institutions.
- In addition to scaling up private-sector participation, the proposed reforms are designed to ensure coordinated decision-making and promote climate resilience.

INTRODUCTION

Efficient infrastructure investment contributes to economic growth in two ways. In the short term it boosts demand for workers and materials through construction activities, and over the long term it increases the economy's capacity to produce. Public- and private-sector fixed investment levels are the foundation for inclusive and sustainable growth – yet they stand at about half of the target of 30 per cent of GDP set by the National Development Plan.

Figure 5.1 Fixed investment trends

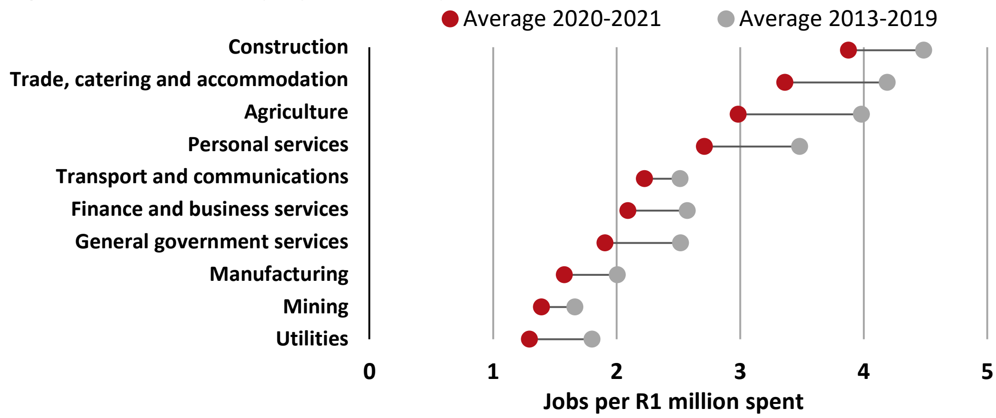


Source: Statistics South Africa

Fixed investment as a percentage of GDP rose steadily through the 2000s but declined between 2016 and 2021, hastened by the COVID-19 pandemic (Figure 5.1). Initially strong investment by public corporations has not translated into effective electricity supply and transport infrastructure, and private investment has been largely flat over the past 15 years.

Reversing this trend is necessary to improve the growth and employment outlook. The construction sector is a major employer that has significant multiplier effects: for every R1 million spent on a construction project, more than three jobs are created for individuals whose highest qualification is a matric certificate. By comparison, a similar investment in mining creates just one job for those whose highest qualification is a matric certificate.

Figure 5.2 Sectoral employment multipliers*



**Based on Social Accounting Matrices between 2013 and 2021. Employment multipliers indicate the relationship between output and employment*
Source: National Treasury and Statistics South Africa

Over the medium term, government is transforming its approach to public-sector infrastructure by creating the conditions to attract private-sector participation. The changes focus on improving project preparation, strengthening partnerships and exploring alternative financing mechanisms. Beginning in 2025/26, the National Treasury will combine project preparation support, transaction advice for public-private partnership (PPP) projects and ringfenced financing from government borrowing in a single structure.

This unified approach will bring together the PPP office and Capital Projects Appraisal Unit in the Government Technical Advisory Centre and the capabilities in the Infrastructure Fund located in the Development Bank of Southern Africa. The consolidation of project preparation and financial structuring functions will strengthen planning and preparation, helping large-scale projects and programmes to reach financial close faster.

In addition, the National Treasury will make greater use of financial instruments such as dedicated bilateral loans, concessional financing and infrastructure bonds to fund large infrastructure projects. Engagements with the private sector, including by sourcing technical skills and facilitating contracting arrangements, will underpin delivery.

SCALING UP PRIVATE-SECTOR PARTICIPATION

A series of reforms under way is expected to catalyse greater private-sector participation in public infrastructure projects.

Credit enhancements to mobilise private finance

Through the successful experience of the Renewable Energy Independent Power Producer Procurement Programme (REIPPPP), government and investors gained a deep understanding of the risks involved in specific types of public-sector infrastructure investment. In this regard, government is developing a blended financing risk-sharing platform that will build on the REIPPPP experience. It will include a credit guarantee vehicle to help de-risk public-sector projects – starting with the energy sector – for private-sector developers and lenders, while reducing government's contingent liabilities.

The initial focus will be on independent transmission projects to bridge the energy transmission deficit, with options to include other sectors over the medium term. The vehicle is expected to be operational by the end of 2025.

Increasing private participation in transactions

The REIPPPP has unlocked private-sector participation in infrastructure investments and helped develop a credible project pipeline. Various institutions across government are strengthening partnerships to apply the lessons of the REIPPPP in different sectors.

The Department of Water and Sanitation's Water Partnerships Office has two priority programmes for non-revenue water (the revenue lost from leaking water infrastructure) and recycling wastewater for different uses. The private sector can participate through performance-based contracts and PPPs. Performance-based contracts for the non-revenue water programme are being fast-tracked in the eThekwini, Tshwane, Nelson Mandela Bay, Buffalo City and Mangaung metros.

To support the objectives of the freight logistics roadmap and improve passenger rail services, Transnet and the Passenger Rail Agency of South Africa are finalising a list of priority projects. Transaction advisors will then be appointed to structure the transactions and prepare requests for proposal, which will be issued to the market in 2025/26.

Implementing the PPP review recommendations

PPPs, such as the Gautrain and the toll road concessions, are a tried and tested mechanism to deliver infrastructure. A PPP is a contract between government and a private party for the development and management of a public asset in which the private party bears substantive responsibility for risk, provides a significant portion of the finance, and is compensated based on the performance and use of the asset.

The 2024 Budget outlined reforms to the PPP regulations to accelerate infrastructure delivery. The new regulations will reduce procedural complexity in PPP implementation and close regulatory gaps. Regulations relating to unsolicited proposals will make it easier for a private company to make a proposal to the public sector for an investment opportunity. Risk governance will be strengthened through the introduction of fiscal commitments and contingent liabilities reporting requirements.

Together, these reforms will re-energise the development of a bankable pipeline of transactions, providing opportunities for better private capital mobilisation within a transparent regulated framework.

Since the 2024 Budget, government has finalised amendments to National Treasury Regulation 16 and Municipal Regulation 309 – both of which govern PPPs – that incorporate comments received from the public and private sector. Government will release the final amended regulations for entities governed by the Public Finance Management Act (1999) before the end of November 2024.

Grant reforms to support sustainable urban development

Electricity, water, sanitation and waste management services are in long-term decline due to underinvestment in maintenance, rehabilitation and expansion at the municipal level.

In large cities, these services are supplied through trading services, which have experienced significant financial decline. Detailed reforms are being rolled out, including a requirement for municipalities to produce separate financial statements for each trading service and to make the financial relationship between the service and the municipality explicit. In 2025/26, government will create a performance-based conditional grant to trigger these changes. The results are expected to improve the functioning of trading services, which over time will allow for increased investment to supplement grants.

SUSTAINABLE INFRASTRUCTURE FINANCING

Government is considering new long-term financing mechanisms to support infrastructure investment as a standalone asset class. These include the creation of a long-term financing instrument without the current market obligation to value assets on a daily basis. Also under consideration are changes to the Securitisation Regulations issued under the Banks Act (1990) to allow infrastructure loans to be pooled and traded as asset-backed securities – and for the creation of infrastructure investment trusts, which would derive returns from income-generating infrastructure.

A consultation paper discussing the design of these instruments will be published before the 2025 Budget.

Reforming government borrowing for infrastructure

Government borrowing for infrastructure programmes and capital budgets funded through the budget will be shown as a defined category of the broader borrowing programme. The scope for borrowing will be extended to include infrastructure bonds, bilateral loan financing and concessional funding from international financial institutions, including multilateral development banks. Where possible, partners in the Just Energy Transition Investment Plan will be approached for concessional loans for projects with demonstrable climate change co-benefits. In addition to funding, multilateral development banks and other international financial institutions can provide technical assistance with project preparation and implementation.

A request for proposals will be issued before end-November 2024 with details for selected projects and programmes that can be financed by interested lenders.

RECONFIGURING PROJECT APPRAISAL AND FINANCING

Since its introduction in 2016, the Budget Facility for Infrastructure (BFI) has developed a standardised appraisal methodology for large infrastructure projects in line with global best practice. Building on earlier successes, the BFI will evolve into a unified public investment system, or centralised gateway, for all large infrastructure projects.

Project submissions will be evaluated quarterly rather than annually, as is currently the case. The same appraisal methodology will be used, but financing decisions will be separated from the budget process to determine the most effective mechanism for each project. This could include government guarantees, appropriations, PPPs or other fiscal tools. This is expected to improve efficiency and the allocation of fiscal and project risk.

New appraisal and financing system to take shape over medium term

The BFI employs bid windows through which public institutions – including national departments, provinces, municipalities and public entities – request funding for part of the cost of a project. The eighth bid window for the 2025 Budget process is piloting the reconfigured system of appraisal and financing described above.

The introduction of project-based loans may result in a marginally higher borrowing requirement at the time of the 2025 Budget. However, it is expected that the borrowing costs will be more favourable and investors will be able to directly link their investment decisions to specific infrastructure projects or a portfolio of projects.

The following projects have been approved for execution using the new appraisal and financing system from 2025/26:

- Transnet: Cape Town Container Terminal Expansion Phase 2B to expand landside capacity at the terminal. It includes rehabilitating and upgrading the container stacking pavement, expanding the truck staging area and building new rail sidings.
- City of Johannesburg: Alternative Wastewater Treatment Technology PPP to convert 500 000 tonnes of solid waste per year to energy.
- eThekwini: Non-Revenue Water Project for infrastructure upgrades to reduce leaks.
- South African Nuclear Energy Corporation: Replace the SAFARI-1 research reactor.
- Department of Water and Sanitation: Olifants Management Model Programme Phase 2D and 2F for bulk distribution water infrastructure, including pipelines, reservoirs and reticulation.
- Department of Health: Siloam District Hospital to build a new 224-bed hospital, refurbish the psychiatric ward and mortuary, and construct facilities for allied services such as audiology, physiotherapy and occupational therapy.
- Department of Higher Education: Student Housing Infrastructure Programme to build six facilities at universities and technical and vocational education and training colleges.
- Western Cape Department of Health: Tygerberg Hospital Redevelopment Health Technology PPP to procure health technology.
- Transnet: Ukuvuselela Gauteng-Eastern Cape High-Capacity Rail Corridor to upgrade the South Corridor railway line and expand port infrastructure for automotive handling.

BUILDING CLIMATE RESILIENCE

Climate-related disasters are occurring with increasing frequency and severity, with correspondingly larger effects on lives and livelihoods. Methods previously developed by the public and private sectors to manage disaster response and recovery are becoming unrealistic in terms of their costs.

The financing of disaster relief depends heavily on budget allocations through funding mechanisms for unforeseeable and unavoidable events. Government is exploring options for purchasing insurance for certain events where such a practice would not undermine budget sustainability.

The National Treasury is reviewing how disaster emergency funding is accessed and disbursed by municipalities. The review will include recommendations on different options for national government to manage risk depending on the frequency and severity of shocks such as fires, floods and drought. It will also examine the rationale for establishing a risk-pool arrangement at the subnational level as a cost-effective way to respond to shocks.

CONCLUSION

The infrastructure investment system is being strengthened in the areas of planning, investment appraisal, contracting, monitoring and evaluation. These reforms are expected to attract significant private-sector investment to augment public-sector resources. Over time, these changes will improve the fiscal position as well as the provision of effective and growth-enhancing infrastructure.