PUBLIC-PRIVATE PARTNERSHIPS

Janet Heckman
Managing Director for the Southern and Eastern Mediterranean Region

Paris, 29 June 2018

European Bank
for Reconstruction and Development

Introduction

European Bank
for Reconstruction and Development

- General policy issues
- Policy and finance are inextricably entangled in PPPs
- Drivers for public-sector decisions are also often quite unclear

What is a PPP

1. **Procurement** model
2. Involves **long-term contract** with private sector involvement
3. Which requires initial significant **capital investment**
4. Not necessarily includes **private sector financing** but most likely
5. With **payments over the life** of the contract from the public party or users of the infrastructure
6. **Ownership** of the asset with the government at least at the end of the contract

What is a <u>not</u> PPP

- Projects without any major new capital investment or upgrade
- Outsourcing: no significant investment in soft infrastructure
- A JV investment between the public and private sector unless it involves a PPP contract
- Franchise, Affermage, Service Concessions
- Private sector acquisitions of regulated infrastructure (BOO)
- Design-Bid-Build (DBB) + Management Contract

PPPs – Pros and Cons

European Bank
for Reconstruction and Development

Pros:

- Budgetary Benefit – “off-balance sheet”
- Additionality – acceleration of investments
- Risk Transfer vs VfM
- Whole-live cost
- Less chances of cost overruns
- Economies of scale
- Access to private sector skills
- Single-Point responsibility
- Transparency and accountability
- Others depending on the structure

Cons:

- Larger impact on the public-sector budget
- Financing Cost
- Need of a highly skilled authority
- Reality of risk transfer
- Need of sizable and complex projects
- Discouragement of smaller contractors
- Limited Competition
- Complexity
- Lack of Flexibility
- Transparency in the contract

PPP pre-requisites

Government must enable conditions to attract investment and ensure long-term commitment to PPP among stakeholder

- Political and economic stability
- Create a competent PPP Unit and Independent Regulation
- Appropriate legislation
- Understanding the costs of public sector activity
- Understanding which risks are not transferred and hidden liabilities
- Ability to produce output-based specifications
- Ability to negotiate and handle private sector companies in a sophisticated and thoughtful way

Legal Framework

European Bank
for Reconstruction and Development

Typical legal obstacles without the proper legal framework

- the requirement to conduct separate tenders for construction and long-term operation;
- prohibition for public entities to outsource;
- prohibition of deferred payments for public works;
- limitations on transfer of control of public-sector infrastructure; or
- lenders’ security requirements.

It is key properly address in the Legal Framework the following:

- to provide clarity on procurement procedures;
- to set out the basis on which a Government may provide support for various project risks, e.g. revenue guarantees;
- to provide clarity on investors’ rights if the PPP Contract is terminated early;
- to give lenders the ability to take security over the PPP Contract, as well as ‘Step-In’ rights; and
- if appropriate, to allow for provision of investment incentives such as special tax treatment, etc.

Budgetary Benefit

- The primary reason: PPPs do not require public-sector funding today
- Free of short-term constraints on investment in public infrastructure
- Constrains: insufficient tax revenues and limits on public-sector borrowing
- ‘Off-balance sheet’ for the public sector
- Service Fees are a future annual cost, and thus do have an eventual impact on the public-sector budget
- While there are some instances in which PPPs can increase the fiscal space available for infrastructure, in practice these are limited
- Stream of availability payments under a PPP is not very different from the repayment schedule of a debt-financed public procurement scheme
- Eventually worsen the original constraints, which is a particular danger where relatively small countries
- At best, this can create budgeting issues; at worst, it can enable governments to use PPP to bypass their own prudent public borrowing and budget limits

Risk Transfer

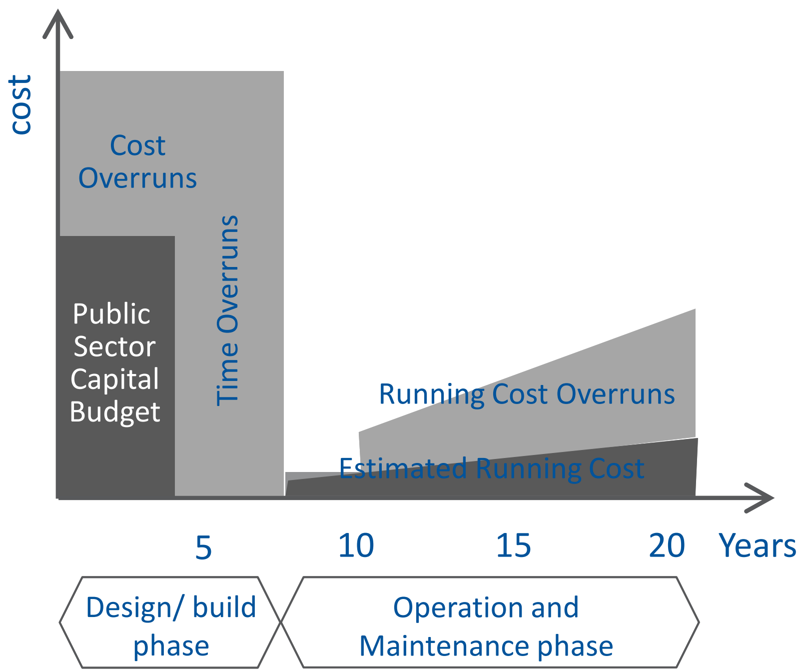
European Bank
for Reconstruction and Development

- Private finance materialise the risk transfer in PPPs
- Private-sector finance costs more than if the project were procured in the public sector and financed with public-sector borrowing
- Project's risks do not disappear just because the public sector is funding it

PPP vs. DBB cash flows

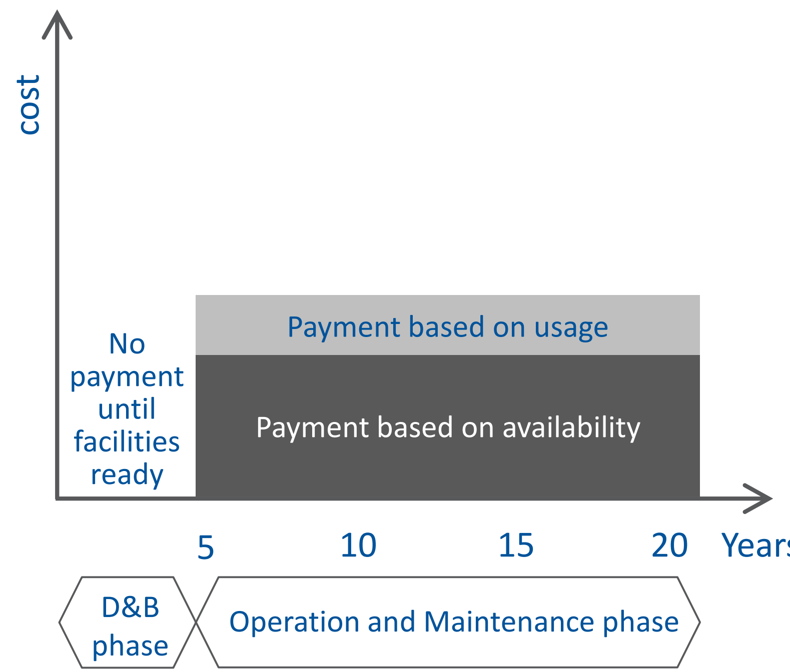
Traditional Cashflow

Payment profile for the public-sector

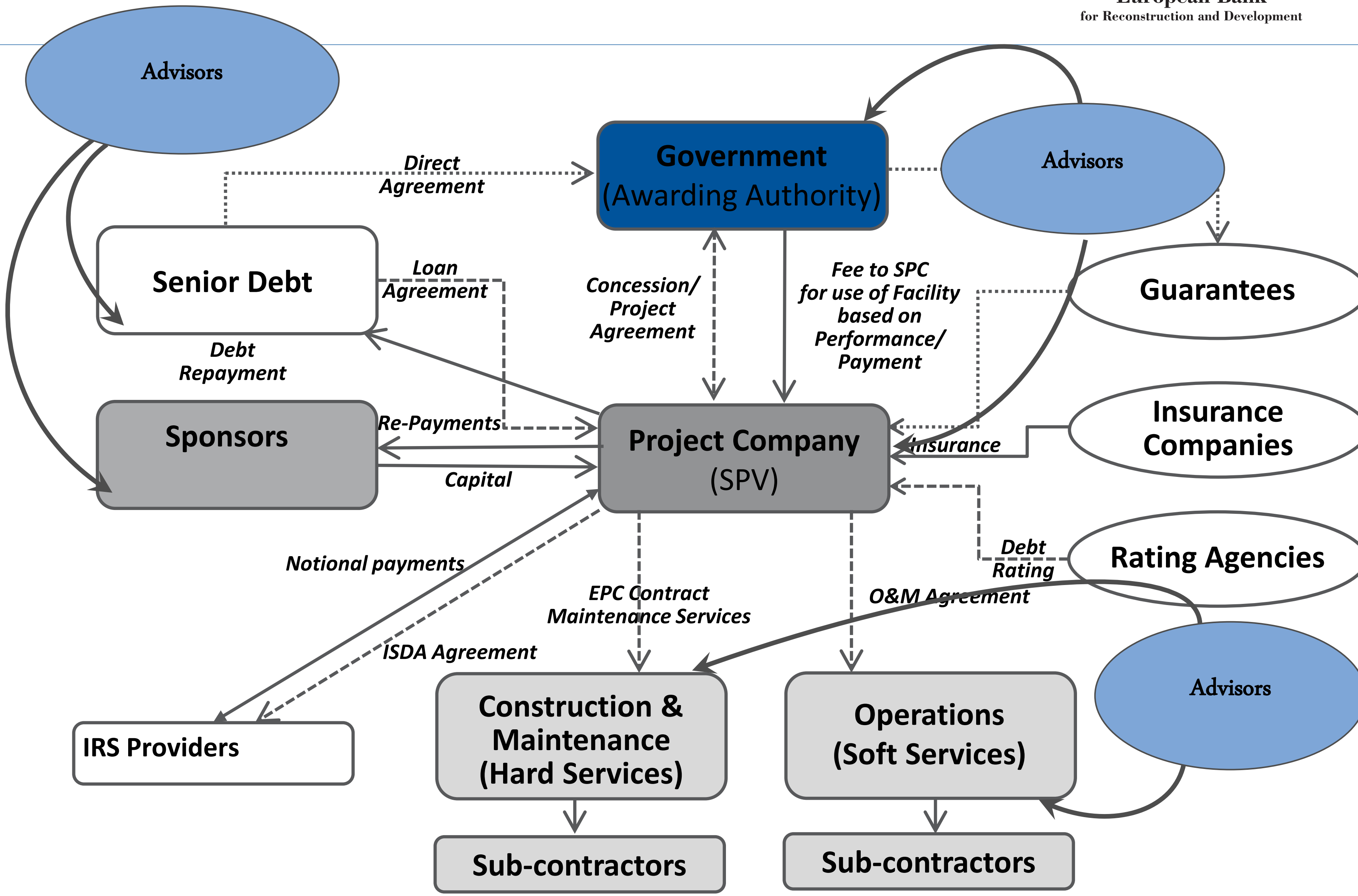


PPP Cashflow

Payment profile for the public-sector



Legal and Cash flow Typical Structure



Key Important Risks (1/2)

European Bank
for Reconstruction and Development

Phase	Risk Category	Nature	Typical Allocation
General	Political	Political opposition to project	Public-sector
		Change in law	Public-sector
	Macroeconomic	Interest rates	Contractor
		Inflation	Public-sector
		GDP	Public-sector
		Exchange Rate	Shared
Construction Phase	Site	Site acquisition	Public-sector
		Ground condition	Shared
		Permits	Shared
		Environmental permits & risks	Shared
		Archaeology and fossils	Public-sector
		Access, rights of way & easements	Public-sector
		Connections to the site	Public-sector
		Protesters	Public-sector
	Construction	Construction Subcontract	Subcontractor
		Price adjustments	Subcontractor
		Changes by the Public Authority	Public-sector
		Revenue during construction	Contractor

Key Important Risks (2/2)

European Bank
for Reconstruction and Development

Phase	Risk Category	Nature	Typical Allocation
Construction Phase	Completion	Delay by Construction Subcontractor	Subcontractor
		Other causes of delay	Public-sector
		Design	Subcontractor
		Performance	Subcontractor
Operation Phase	Operation	Usage/demand risk	Public-sector
		Network	Public-sector
		Revenue payment and tariff	Public-sector
		Availability and service	Contractor
		Operation cost	Subcontractor
		Maintenance	Subcontractor
	Termination	Project Company default	Contractor (*)
		Termination by the Public Authority	Public-sector
		Force Majeure	Public-sector
		Residual value	Contractor

Source: Adapted from Public–Private Partnerships, Principles of Policy and Finance, E. R. Yescombe

Whole-Life Costing and Maintenance

European Bank
for Reconstruction and Development

- Perhaps the most important element in favour
- Investors will be responsible both for the construction of the Facility and for its operation and service delivery, they are incentivised
- Whereas a typical public-sector procurement approach is to go for the lowest initial capital cost
- Bundling' construction and long-term services together is weaker in relation to Soft FM services
- Long-term contractual nature of a PPP forces the public-sector to make provision for maintenance
- However, a Public Authority could enter into a long-term contract covering design, construction and maintenance which could produce the same result

Private Sector Skills

European Bank
for Reconstruction and Development

- Project Selection
- Project Management
- Single-Point Responsibility
- Efficiency
- Innovation
- Third-Party Due Diligence

Public Sector Reform

European Bank
for Reconstruction and Development

PPP are a change in mind for the public-sector:

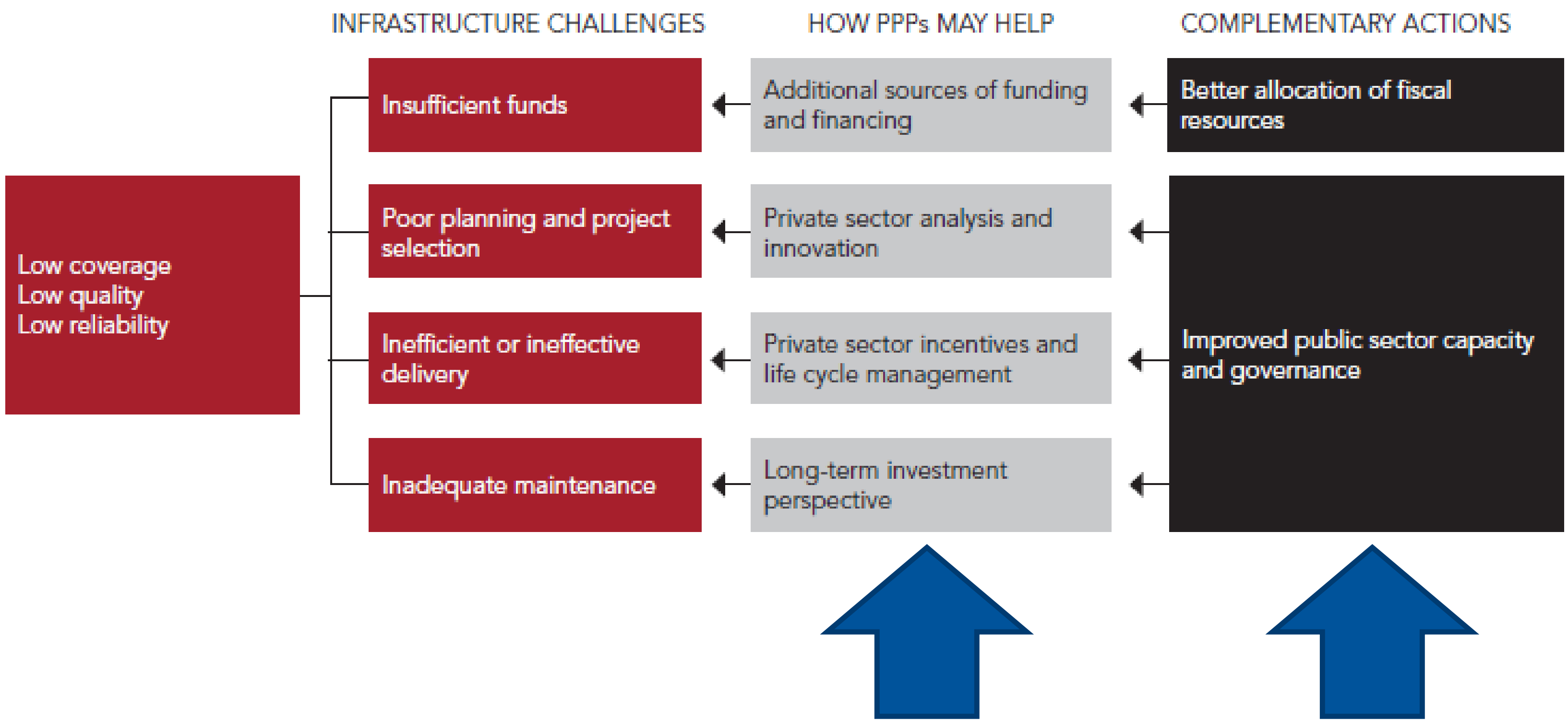
- Governments: purchase infrastructure services vs. operate assets
- Governments: focus on administer contracts vs. assets
- Governments: monitor outputs and quality of service
- Contracting-out public services to the private sector

A PPP programme can serve as a catalyst for wider public-sector reform in a number of different ways:

- Transparency and Accountability
- Develops procurement skills
- Contestability

Where we can provide value

The Challenges with Infrastructure and How PPPs Can Help:



Source: PUBLIC-PRIVATE PARTNERSHIPS. Reference Guide, The PPP Knowledge Lab

EBRD engagement in PPPs

European Bank
for Reconstruction and Development

Transport

- Since 1994: Over 230 transactions and commitment of EUR 16.0 billion
- Total of 24 PPP transactions with over EUR 1.8 billion in finance

Municipal Environmental Infrastructure

- Since 1994: Over 460 transactions and commitment of EUR 7.9 billion.
- Total of 30 PPP transactions with over EUR 1.6 billion in finance

➢ **Supported privatisation, restructuring and better infrastructure service delivery.**

➢ **Promoted policy dialogue with regards to investment climate business environment and policies.**

IFI Project Preparation Facilities

Global Infrastructure Facility	ADB's Asia-Pacific Project Preparation Facility	IaDB's PPF	AfDB's NEPAD
100m **multi-donor fund, housed in World Bank**	150m **multi-donor fund, housed in ADB**	30m **fund, using internal capital only in start up phase, housed in IADB**	75m **fund, multi-donor fund, housed in AfDB**
Channels PPP funding to regional MDBs for PPP preparation , and provides PPP policy	**Funds PPP preparation, national transaction advisory, and PPP policy**	**Funds PPP preparation, national transaction advisory, and PPP policy**	**Funds PPP preparation, and PPP policy**
Established 2015	**Established** 2016	**Established** 2017	**Established** 2010

EBRD's IPPF structure

European Bank
for Reconstruction and Development

EUR 40m Facility, directly funded by EBRD net income, applicable to all Countries of Operation of EBRD

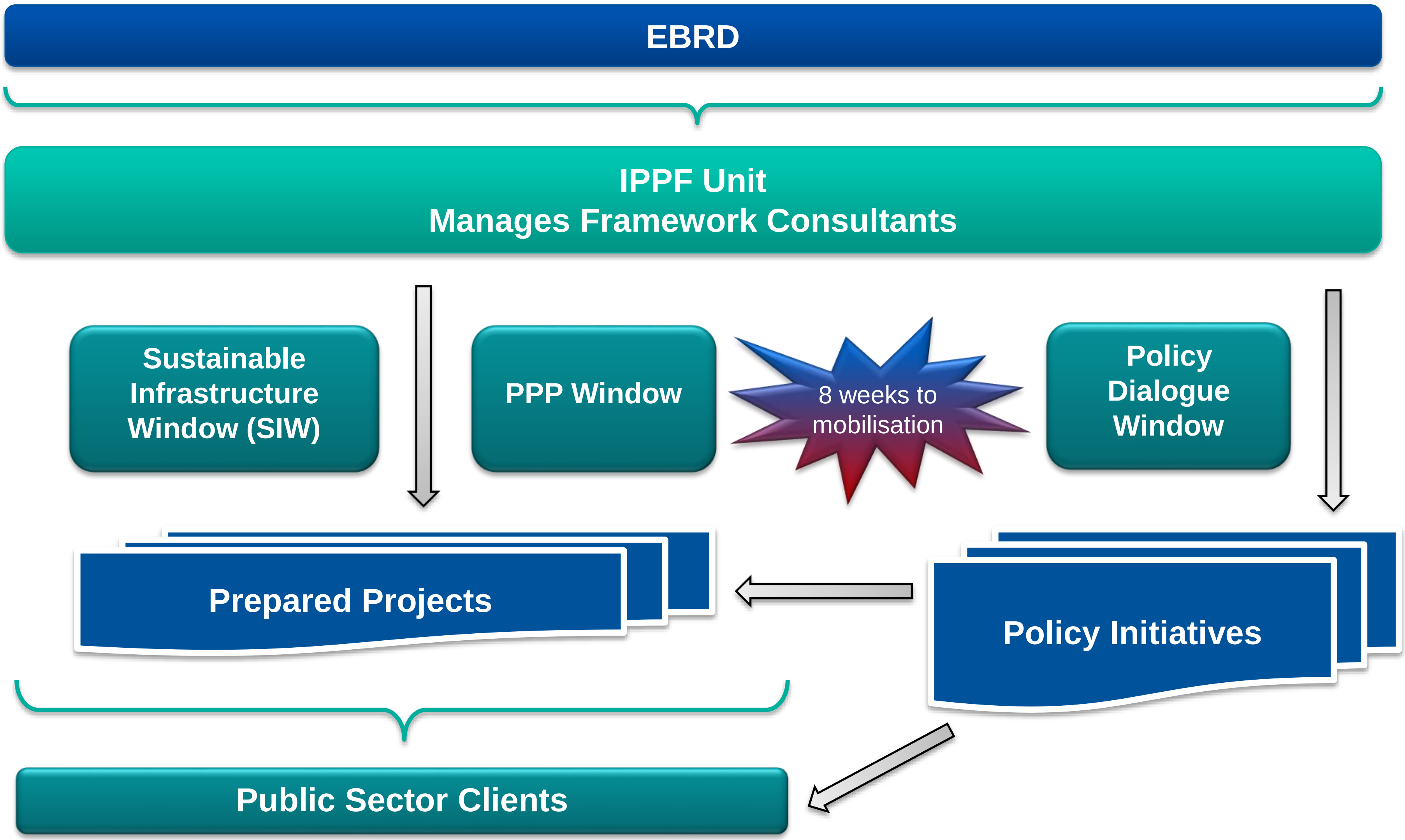
Preparation of bankable PPPs and commercialised public sector projects

Efficient mobilisation using pre-selected 'framework consultant' approach

Dedicated EBRD IPPF team, operational since September 2015

IPPF’s architecture drives business and policy

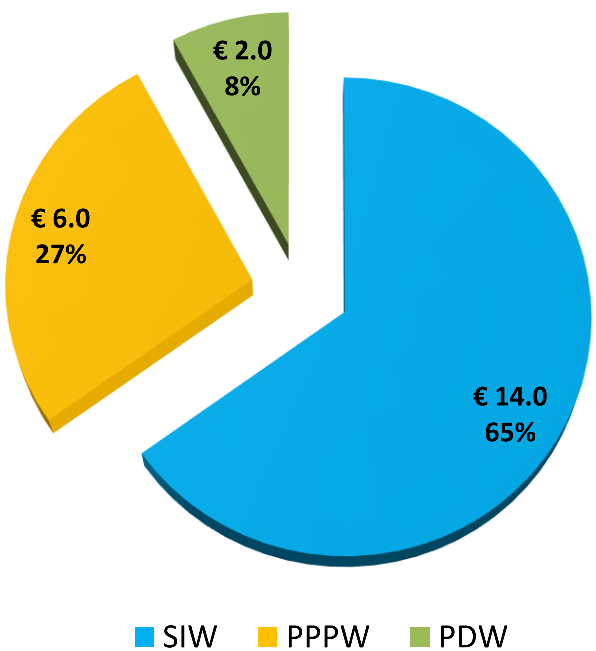
European Bank
for Reconstruction and Development

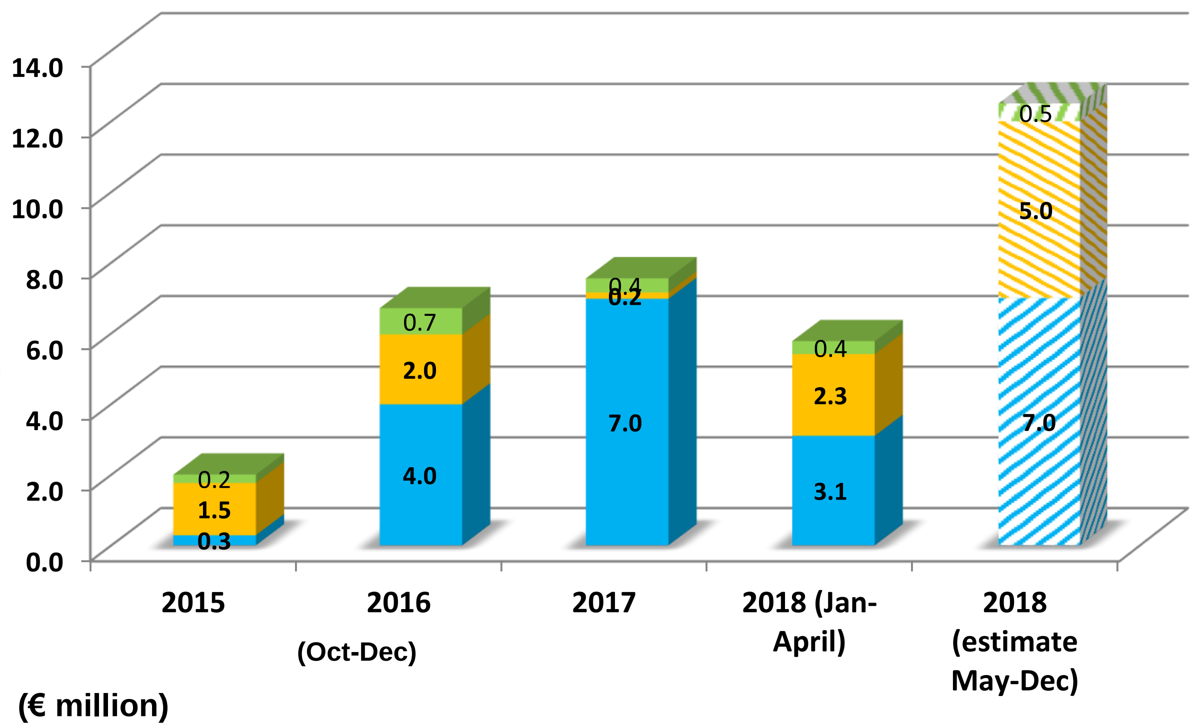


IPPF Usage Overview: Strong demand through 2018

European Bank
for Reconstruction and Development

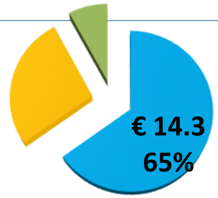
- To date, IPPF has delivered consultancy assignments worth **€22** million through its three Windows: Sustainable Infrastructure Window; PPP Window; Policy Dialogue Window
- On pace to commit **€35**m by year end **2018**

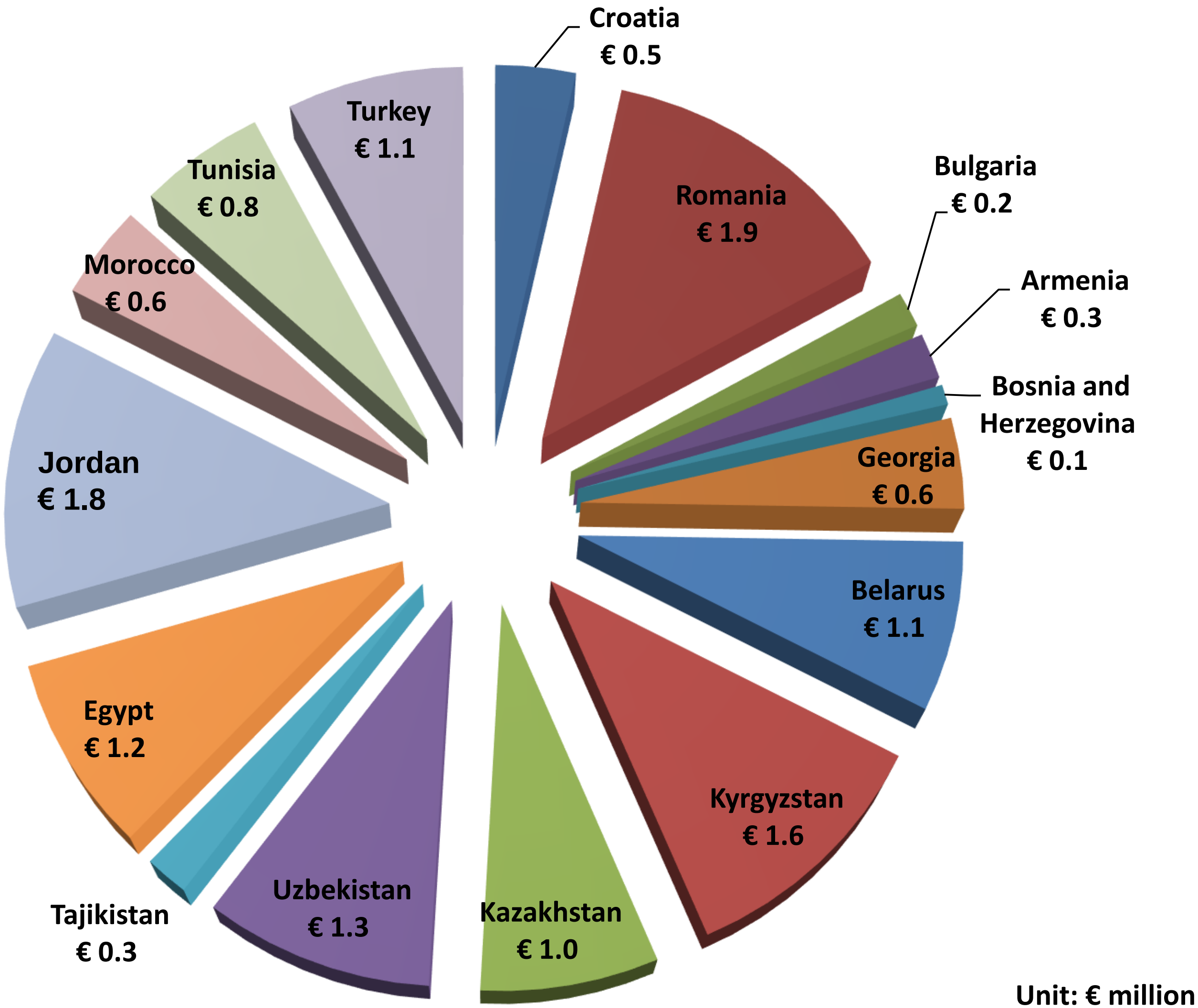




Sustainable Infrastructure Window: Balanced geographic distribution

European Bank for Reconstruction and Development





37 assignments for a total of €14.3 million

€400,000 average/project

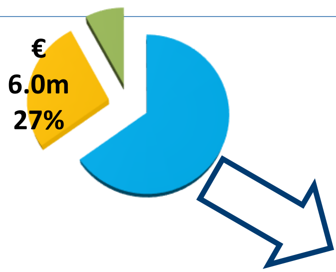
SEE/EE/ Caucasus: 33%

Central Asia: 29%

SEMED & Turkey: 38%

PPP Window:
Promoting Pioneering Efforts in New Markets

European Bank
for Reconstruction and Development

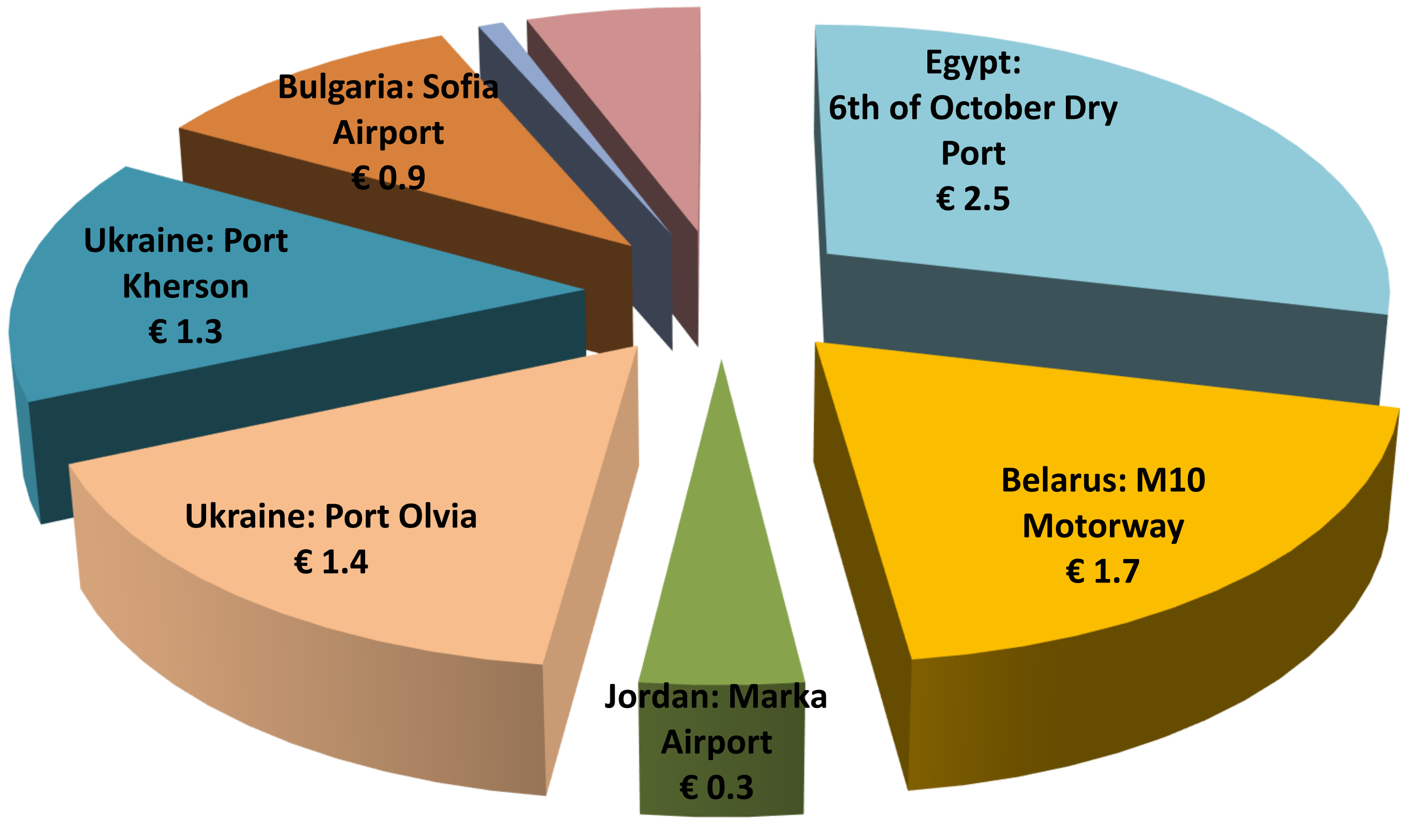


Strong partnerships:

IPPF = € 5.7m

Global Infrastructure Facility = € 1.8m
(for contributions to Sofia Airport; Egypt Dry Port; Ukraine Ports; Jordan Airport)

IFC Advisory = € 1.2m
(for contributions to Sofia Airport; Ukraine Ports)



in € million

IPPF Case Study: PPP Window - 6th of October Dry Port PPP

- A dry port is an intermodal terminal that is connected by rail, road and/or inland waterways to a seaport
- This Project southeast of Cairo is the 1st dry port in Egypt., and will be connected by rail to the Greater Port of Alexandria (GPA).
- GALDP (dry port authority) is the project promotor.
- The project has an estimated capital expenditure of USD 100m
- IPPF contracts: €1.9m
- Tender launched, Pre-qualification phase May '18; contract award targeted by year-end 2018

Rail (or road) freight ⟷ **Dry Port** ⟷ Direct connection ⟷ **Sea Port** ⟷ maritime freight

Conclusions

European Bank
for Reconstruction and Development

- PPPs are a very efficient procurement model for delivery infrastructure projects, but complex and expensive

- Government honest motivation for reducing whole-life cost and risk transfer are key for success

- If government motivation is budget constrains or public deficit, the programme might result unaffordable

- Strong political commitment and Policy Frameworks is key for success