



INTERNATIONAL FINANCE CORPORATION  
WORLD BANK GROUP

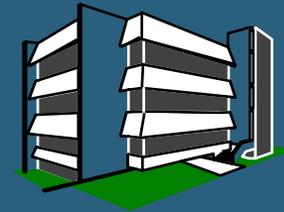
# Public Private Partnerships IFC's Global Experience

Martin Spicer  
Principal Investment Officer  
Municipal Fund  
International Finance Corporation  
Moscow, February 10, 2005

# Presentation Outline

- Introduction to IFC
- Public Private Partnerships
- History of Private Investment in Infrastructure Projects
- IFC Case Studies
- Lessons

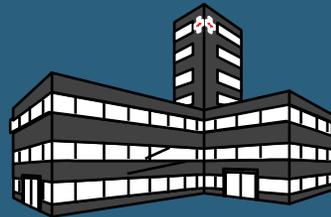
# Introduction to IFC



Multilateral Investment Guarantee Agency  
Established in 1988



International Development Association  
Established in 1960



International Finance Corporation  
Established in 1956



International Bank for Reconstruction and Development  
Established in 1945

# Introduction to IFC

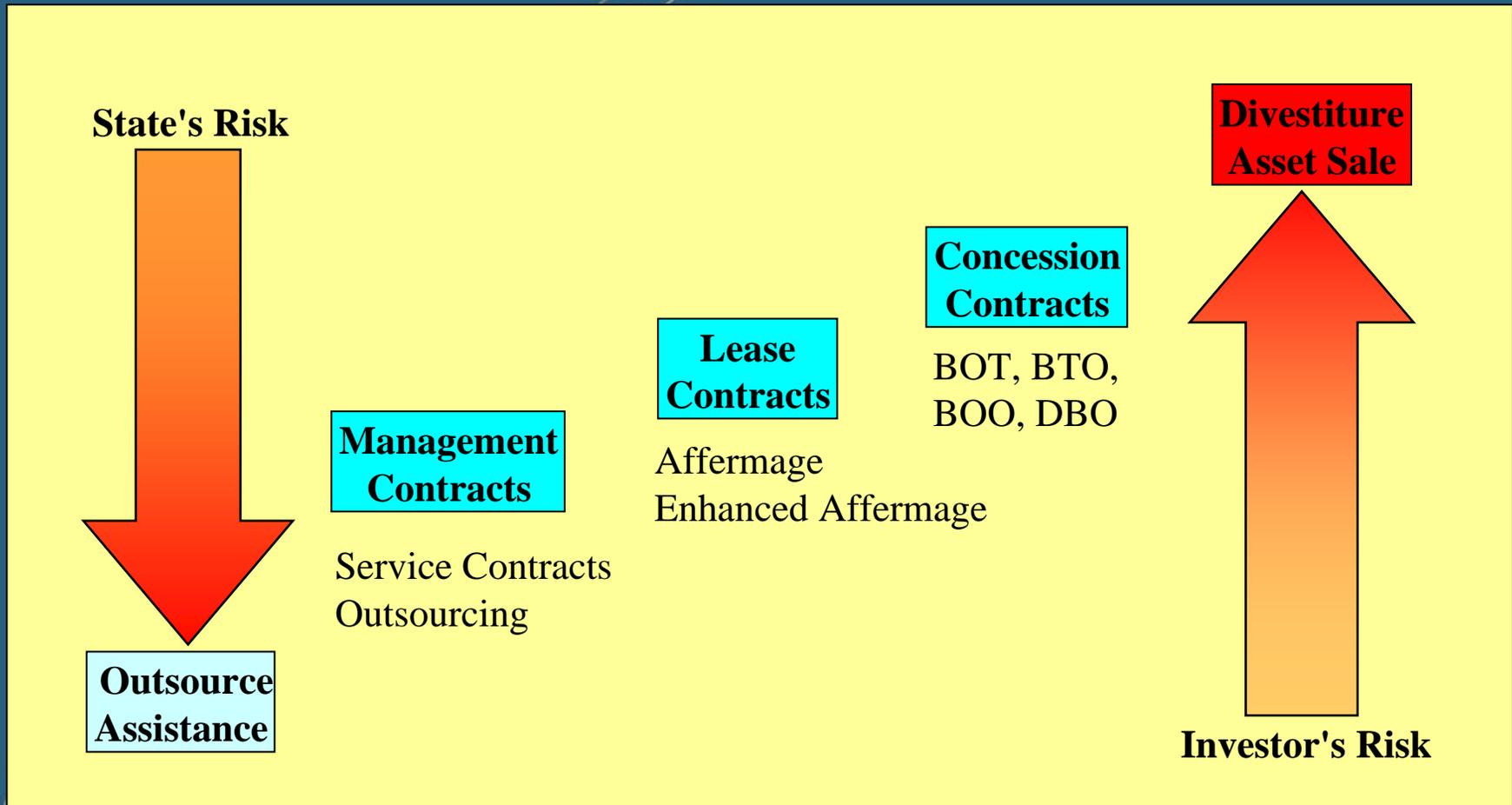
- Largest multilateral source of loan and equity financing for private sector projects in the developing world
- Highly capitalized – Authorized Capital of US\$2.45 billion, Total Capital of US\$7.8 billion as of June 30, 2004.
- In FY04, Operating Income US\$982 million and Total Commitments of US\$4.8 billion
- Total IFC Committed Portfolio is US\$17.9 billion as of June 30, 2004
- US\$3.9 billion infrastructure related (transportation, utilities, telecom) portfolio as of June 30, 2004
  - A significant portion of this investment is in projects with Public-Private Partnerships
- IFC's Advisory Services group has implemented approximately 90 PPP Advisory mandates

# Public Private Partnerships – A Definition

- “A Public Private Partnership is an arrangement between a government entity (central or sub-national) and a private entity established for the purpose of providing an essential service or facility to the public. The goal of this arrangement is to provide the service or facility more efficiently and at a lower cost to the end user than either entity could provide the service on its own. The arrangement will try to allocate the risks of the venture fairly between the private and government entities, based on each entity’s ability to manage these risks and to provide rewards to each party based on the risks they have assumed.”

# Public Private Partnerships

## Fundamental Challenge: Choice of Contract for a Balanced Risk Allocation

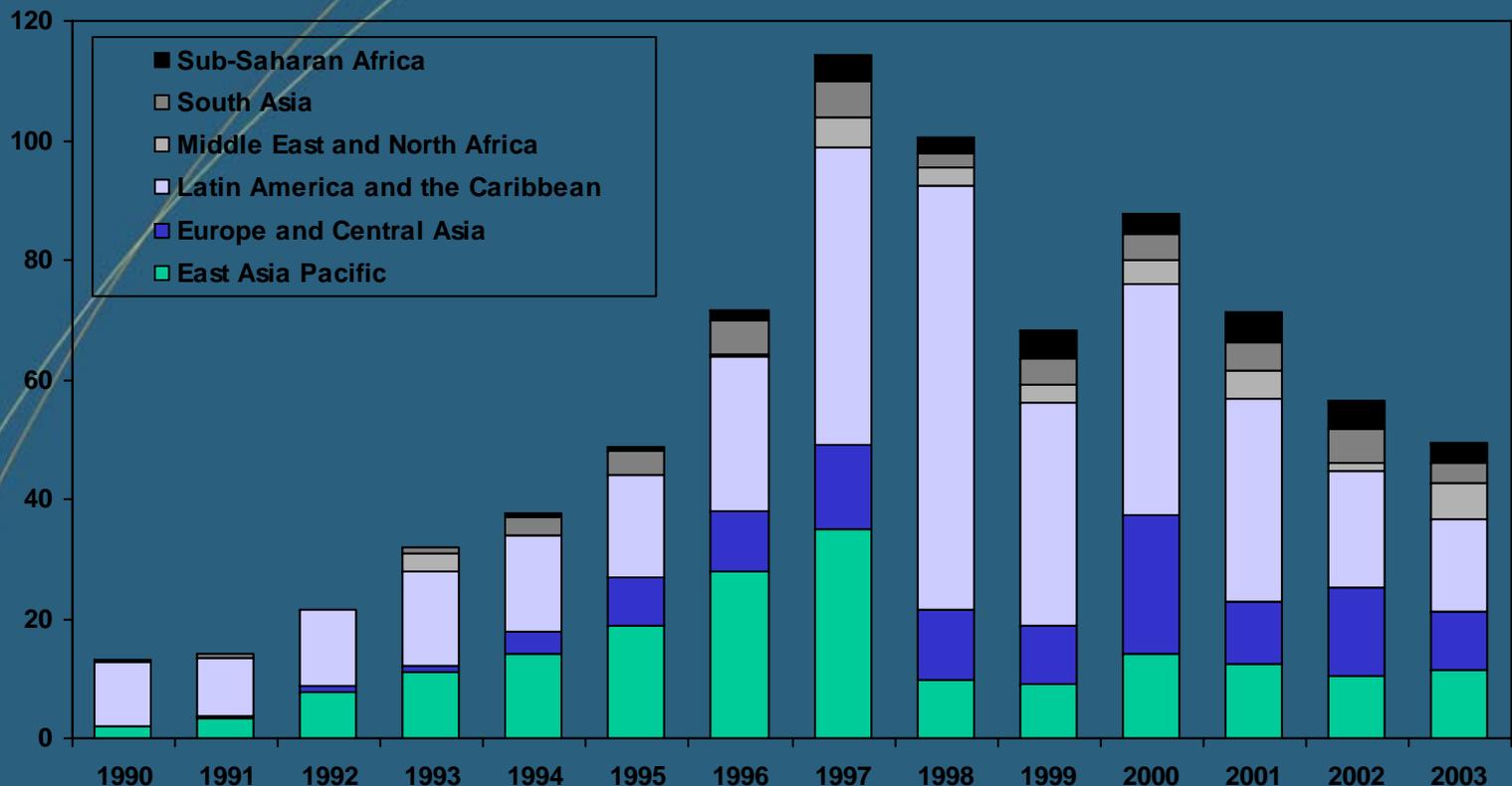


# PPP Models, Described

- Technical Assistance – Limited to advice to the government on how to provide more efficient operations
- Management Contracts – Private management, but little or no private sector investment
- Lease Contracts – Private Sector pays for use of system. Public sector pays operations fees.
- Concession Contracts – Usually Significant Private Sector Investment, with a period of ownership, but ultimately assets revert to Public Sector
- Sale of Assets – Public Sector sells system ownership to Private Sector and retains regulatory Authority
- PPP's have been used in the infrastructure sectors more than any others, but are now being considered for hospitals, schools and other essential services.

# History of Private Participation in Infrastructure

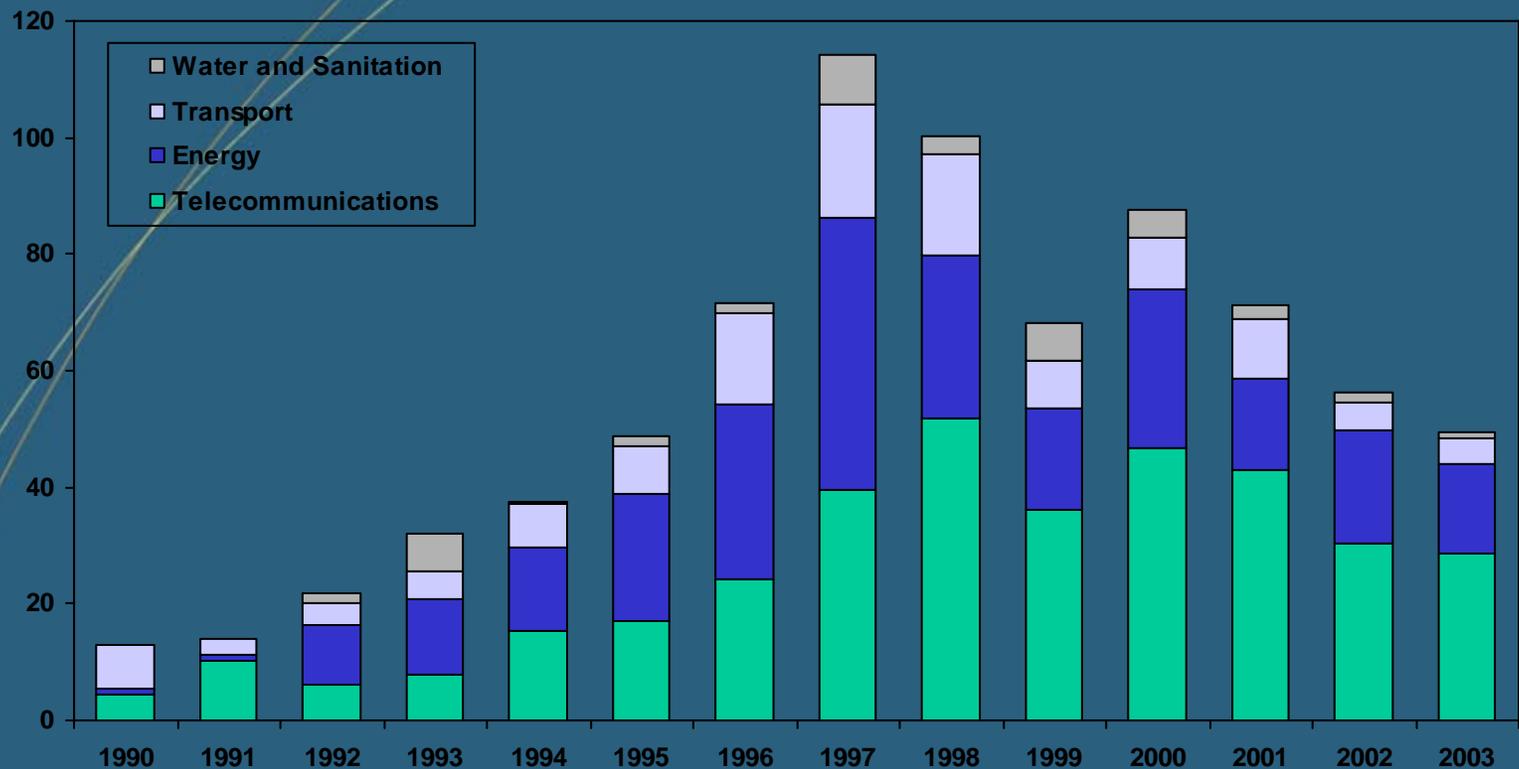
Investment in Infrastructure Projects with Private Participation  
by Region (US\$ billions, nominal)



Source: World Bank's PPI Database

# Across All Sectors: Power, Telecoms, Transport and Water

Investment in Infrastructure Projects with Private Participation  
in Developing Countries by Sector (US\$ billion, nominal)



Source: World Bank's PPI Database

# Private Investment has been Concentrated in Certain Sectors

- Projects that generate ready cash flows and where user fees can be imposed on wholesale users (*telecommunications, ports, airports, captive power plants, freight railways and natural gas pipelines*) continue to attract the bulk of what private investment is available.
- Power, roads, urban transport, water supply and sanitation receive little private capital.

# Why are PPPs taking front stage?

- Availability of public capital remains constrained due to deficits and/or prudent fiscal management
- Availability of private capital also constrained: investors generally more risk-aware than previously and less willing to take risks in emerging markets
- Yet huge capital needs remain in infrastructure, education and health care, for development and for competitiveness
- Efficiency gains from private sector involvement are believed to be considerable.

# Public Support Key to Sustainability

- Visible and appreciable improvements in service delivery and customer relationship
- Tariff affordability and acceptability
- Transparency and clear communication
- Avoidance of unintended downsides (community disruption, resettlement, etc...)
- Subsidies where appropriate, to:
  - Avoid 'rate shocks' for consumers
  - Share financial risk with investors
  - Kick start major projects in difficult investor environment

# Public Private Partnerships IFC Case Studies

# PPP Case Study: Pamir Energy (Tajikistan) Description

- A US\$26m project to finance, purchase and upgrade formerly government owned power assets in Gorno Badakhshan
  - Pamir Energy Corporation, owned 70% by Aga Khan Fund for Economic Development, a for profit entity took over the assets
  - Private company took over and operates all existing electricity generation (40MW), transmission and distribution facilities in Gorno (serving 200,000 people) under a 25-year concession agreement;
  - Expansion of the partially completed Soviet-era Pamir 1 hydro-power Plant from 14MW to 28MW and construct a river regulating structure at the upstream Yashikul lake to ensure adequate flow in winter and
  - Rehabilitation of other assets including substations, transmission and distribution lines.
  - Financing done and a 55/45 debt to equity basis.

# PPP Case Study: Pamir Energy (Tajikistan)

## Challenges and Mitigants

- Many customers poor and unable to afford commercial tariff – Close to 80% of residents of Gorno live in poverty. The government wanted Pamir Energy to continue to provide power to all customers, but the company could not expect to be paid an adequate tariff by the poorer customers
  - World Bank/IDA provided US\$10m loan to the government, who lends funds to Pamir Energy – difference in IDA interest rate and interest rate from government to GBAO used to support a lifeline tariff to poor customers
  - Government of Switzerland providing a grant to top-up lifeline tariff fund.
  - Private company receives lifeline tariff payment from fund if it delivers electricity and is paid by user. This is a form of output based aid (OBA).

# PPP Case Study: Pamir Energy (Tajikistan)

## Challenges and Mitigants

- Government's inexperience and mistrust of private sector – The Government of Tajikistan did not have much experience with privatizations and was cautious about involvement of the private sector.
  - World Bank role in later stages contributed to government's increased level of comfort with supporting private investors
  - IFC involvement in form of a \$3.5m equity investment (30%) also important.
- Power market and off-take risk. Initially, the project was conceived as an IPP in which Pamir Energy would sell its power to Barki Tajik, the national power company. But Barki Tajik was not perceived as a creditworthy off-taker.
  - Project was restructured to allow Pamir Energy to operate as a full utility in the Gorno Badakhshan region, with direct access to the customers.

# PPP Case Study: Powerlinks (India)

## Description

- A US\$265 million project to build, own, operate and transfer (BOOT) five 400kV and one 220kV double-circuit transmission lines of about 1,200km from West Bengal to Delhi, with a capacity of about 3,000MW.
  - Powerlinks Transmission Ltd., a joint-venture between the private utility Tata Power Company Ltd. (51%) and the 100% central government-owned Power Grid Corp. of India Ltd. (49%), will implement the project. Power Grid is the GoI's sole investment vehicle and operating agency for inter-state power transmission.
  - Tata Power won the international tender conducted by Power Grid for the 51% stake in Powerlinks
  - BOOT is for 30 years, during which time Powerlinks will make available its entire capacity to Power Grid.
  - Financed 30% equity and 70% debt. All debt in local currency.
  - IFC's loan is in Rupees and equivalent to US\$75 million
- Project is the first private investment in power transmission in India.

# PPP Case Study: Powerlinks (India)

## Challenges and Mitigants

- First Private Power Transmission Investment – Power Grid realized it needed to attract other investors to build essential transmission capacity. Interest from private companies was limited, though, to two bidders for the 51% stake.
  - Gov gave strong support to process. Regulator increased normal RoE expectations in tariff to attract private investors. Power Grid publishes data on itself on the internet, promoting transparency in its operations.
- Off-take risk – Many of the State Electricity Boards have poor payment record and Powerlinks was unwilling to take SEB risk directly.
  - Transmission Services Agreement calls for Powerlinks to maintain the transmission lines, ensuring a minimum availability and 100% of capacity for Power Grid. Tariff based on a cost-plus formula including an RoE component. Power Grid has highest possible rating by two local rating agencies.

# PPP Case Study: Powerlinks (India)

## Challenges and Mitigants

- Delays in Consents and Approvals – Government approvals difficult to obtain generally, more so for first privately controlled transmission company.
  - Powerlinks relies on its government-owned shareholder, Power Grid, to lead it through the consents and approval process
- Construction Cost Overruns – Lenders viewed multiple contractors as a risk and asked the shareholders to help mitigate this risk.
  - Response was a project support agreement from Tata Power that would cover any potential overruns.
- Corporate Governance – With a 49%/51% shareholding structure, how to ensure both shareholders were able to have their fair voice?
  - Management positions in Powerlinks are to be nominated by different shareholders based on their strengths. Board of Directors to have five members appointed by Tata Power and four by Power Grid, with two additional to be appointed by the lenders.

# Case Study: Mexico Toll Roads Experience (1989-1994)

## Description

- In 1989, Mexico embarked on a private toll road program which more than doubled the national toll road network – from 4,500km to 9,900km in 1994.
  - 53 concessions were awarded to private investors who constructed and then operated the toll roads under BOT schemes receiving revenues directly from users of the roads
  - Approximately US\$13 billion was invested between 1989–94 and was sourced from local commercial banks (52%), concessionaire equity (29%) and federal and state government grants and equity contributions (19%)
- However, gross miscalculation of investment costs and operating income led to an unsustainable set of operating conditions. Mexican currency crisis of December 1994 further undermined financial equilibrium of projects.
- Local banks were saddled with non-performing loans and concessionaires had to write off significant portions of their investments. IFC also invested in one project – Toluca Toll Road.
- Solution involved either Government bail-out (partial) or very high tariffs.
- Mexico is embarking on a new pilot program to accelerate investment in the toll road sector trying to take into account the

# Case Study: Mexico Roads Experience

## Major Issues and New Ideas

- Underdeveloped institutional capability – The program was ambitious and at the time exceeded the technical and administrative capacity of nearly all of the entities involved – government, financial institutions and investors.
  - In 2003, the Ministry of Finance created a special group to lead a new program – Proyectos para Prestacion de Servicios (PPS), based on the Public Private Partnerships and PFI models originally developed in the U.K. This group has received advice (partially funded by IFC) from Partnerships U.K. (PUK), itself a PPP with government and private ownership, and other private consulting firms with specific experience with the U.K. model.
- Inadequate tendering process and concession design – Prequalification standards were not rigorous (no detailed financing plan was required). Criteria limited the bidder pool to a handful of local construction companies
  - Qualification criteria now are much more rigorous both for technical and financial criteria. Also the bidding criteria are much less restrictive. Bid awards will be based on the lowest net present value of payments required from the government.

# Case Study: Mexico Toll Roads Experience

## Major Issues and New Ideas

- Inadequate financial discipline by banks – Primarily government-owned commercial banks, provided large amounts of non-recourse financing with little or no due diligence. This behavior was guided by an implicit understanding that ultimate recourse was with the national government.
  - Mexican banks have learned from their past mistakes. Also, in the current program of road PPPs, the private party will be responsible for construction, maintenance, security services and availability of the road over a 20 year period. The Ministry of Communications and Transport will make a payment – expected to be 90% based on availability and on performance measures and 10% on the number of vehicles that use the road. Private company will take all risks related to construction and operation of the toll road.
- Underdeveloped local financial markets – Peso-denominated debt featured very short maturities rarely extending beyond five years, with interest rates often 1,000 to 1,500 basis points above government rates.
  - Today in Mexico long term financing is available from both banks and the capital markets on attractive terms, which will enable projects to be funded with local currency on appropriate terms.

# Case Study (Advisory): Bucharest Water (Romania)

## Description

- IFC Advisory was mandated by the City of Bucharest to structure and implement a transaction to achieve
  - EU Level of Services at lowest tariff
  - Create a privatized system which is efficient, financially independent, and sustainable
  - Secure public support
  - Meet the Privatization Timetable
- High losses: unaccounted for water = 50%
- Poor water quality and pressure
- Insufficient financial resources
- Low tariffs (US\$0.17/cu. m)
- Strong labor unions

# Case Study (Advisory): Bucharest Water (Romania) Process and Concerns

- Bidding to be conducted on a single parameter: Lowest Tariff Basis
- No Technical Bids but qualified bidders to be selected through strict pre-qualification
- Contract to be output oriented, i.e., establish levels of service (EU level) without any defined requirement of investment
- Limited desire to increase tariffs,
- Desire to include a number of ongoing investments as obligations
- Need for smooth labor transition

# Case Study (Advisory): Bucharest Water (Romania)

## Structuring Success

Strong public support was key for success:

- Extensive market research
  - focus groups and consumer surveys
  - supported privatization
- Proactive media oversight
  - extensive and favorable press coverage
  - high profile and information level
- Early involvement of municipal council in decision making
- Transparent and open tender process
  - One quantifiable bidding criteria (water tariff)
  - Three strong competitors: IWL; SLDE; and Vivendi

# Lessons - What is important for a successful PPP?

- Focus on the outcome that is desired
- Identify the constraints to achieve this outcome
- Address these constraints by taking
  - what the private sector can provide most effectively and
  - what the public sector can provide most effectively
- Information disclosure, transparency and clarity
- Political and public support
- Targeted subsidies to the poor have a role
- Sound regulatory arrangements and structures
- Well developed local capital markets and banking system

# IFC – A Full Solution Provider

- Advisory assignments to government (central and sub-national) for structuring of PPP arrangements
- Funding source
  - for private entities in PPPs.
  - for private-public joint ventures
  - for sub-national governments



INTERNATIONAL FINANCE CORPORATION  
WORLD BANK GROUP



# Thank You

Martin Spicer  
Municipal Fund  
International Finance Corporation  
+1 202 473-1295  
[mspicer@ifc.org](mailto:mspicer@ifc.org)