



DISCUSSION PAPER

Financing Infrastructure in Developing Countries Through Public-Private Partnerships

Recommendations for Critical Advocacy

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Foreword

Since the world's governments adopted the 2030 Agenda and its 17 Sustainable Development Goals (SDGs), they declare that a massive increase of investment, including in public infrastructure, would be required to realize the economic, social and environmental goals. Normally, governments pay for their long-term investments in infrastructure and other public services by first borrowing the necessary funds and then repaying them over the life of the investment out of their fiscal revenues. Developing countries may borrow from development institutions like the World Bank and other development banks or by issuing bonds that are purchased mainly by pension funds and other institutional investors. However, concerns about unsustainable debt levels of many developing countries, on one side, and concerns about low returns on bonds owing to the low-interest rate environment internationally, on the other, have turned government attention to alternate means for organizing and financing infrastructure investment. The key question is whether mechanisms might be available that would yield more revenue for creditors while guiding more private funds into public-interest investment.

Public-private partnerships (PPPs) are such a mechanism and are now favoured internationally for infrastructure investment. PPPs have been used for decades in developed and developing countries to organize public-interest investment, albeit with mixed results. PPPs involve a government contracting with a for-profit enterprise to build and operate a unit of infrastructure, such as a toll road or an urban clean water system. Management is usually left to the private partner, although with some government oversight. A mixture of public and private financing is arranged with sufficient profit prospects to engage the interest of the private partner.

However, private investors are often unwilling to risk their capital in illiquid, long-term investments out of fear that those investments may fail without a way for the investor to exit beforehand to avoid huge losses. Therefore, strategies have been designed by governments and international institutions like the World Bank and other development banks to address those problems, such as national government guarantees and World Bank co-financing. Indeed, the Group of 20 (the annual meeting of the major economies of the world) has encouraged governments and the international development banks to promote PPPs as part of a strategy for increasing development finance across the world.

However, the nations of the world also agreed in their 2015 International Conference on Financing for Devel-

opment in Addis Ababa that while private capital can be a major source of finance for public investment, it was also necessary to “share risks and reward fairly, include clear accountability mechanisms and meet social and environmental standards” (Addis Ababa Action Agenda, paragraph 48). The emphasis on fair risk-sharing and accountability is a response to the concerns of governments as well as many civil society organizations (CSOs) regarding excessive public costs and risks associated with engaging with the private partners, as well as fear of potentially massive human rights violations if standards for project screening are relaxed.

Now, it is time to develop capacity and national sustainable development strategies to properly and fully assess PPPs to ensure that they generate the intended public benefits and facilitate sustainable and socially responsible investments. Governments should involve civil society stakeholders in the design of those strategies, which can then guide policy on public-private partnerships.

As a step to assist civil society, in particular, to develop its own PPP assessment capacity, this paper considers PPPs in terms of the commitments made in the Addis Ababa Action Agenda. We present this discussion paper as a starting point for civil society and governments to engage in thinking about how to design public-private partnerships in a way that can best serve society and the environment. This notwithstanding, the views and opinions expressed herein are those of the authors and do not necessarily reflect the views of Bread for the World (Brot für die Welt).

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Introduction

Why Should Civil Society Assess PPPs?

The 2015 Addis Ababa Action Agenda (AAAA) endeavors to provide a global framework for financing development projects in accordance with the Sustainable Development Goals. It seeks to “end poverty and hunger, and to achieve sustainable development in its three dimensions through promoting inclusive economic growth, protecting the environment and promoting social inclusion” (AAAA 2015, 1). However, the AAAA notes that public financial resources by themselves are insufficient to achieve all of the envisioned development goals. The projected need for additional investment is staggering – the AAAA identifies an annual infrastructure investment gap of USD 1 trillion to USD 1.5 trillion in developing countries, and the Report of the Intergovernmental Committee of Experts on Sustainable Development Financing estimates the need for financing for investment by small- and medium-sized enterprises (SMEs) to be \$2.5 trillion annually (UN 2014). Financial resources of such a magnitude are unavailable to most developing country governments and international development institutions alike. Instead, the AAAA has embraced innovative finance as the key to development success. This strategy emphasizes the promotion of policies that mobilize domestic financial resources, international development aid, and foreign private investment.

In its coordinating and harmonizing effort, the Addis Agenda has the opportunity to be an important catalyst for such financing efforts, and is rightly at the center attention of CSOs. It is important to keep in mind that, rather than a policy paradigm shift, the AAAA is the formalization of financial processes developed in the previous two decades. This, however, provides a good opportunity to evaluate the measures proposed to improve the financial framework over a longer historical trajectory. This paper will do just that for one aspect that is a central component promoted by the AAAA: public-private partnerships (PPPs). PPPs had their origin in the developed world and were initially envisioned as a way to offload costly social and infrastructure expenditures from public budgets. Encouraged by donor countries – and by the Group of 20 in particular in recent years – PPPs have been promoted over the last three decades by the international development banks, with the World Bank and the European Investment Bank (EIB) serving as the main proponents in this movement. However, as a policy tool, PPPs have also found support from the regional development banks, such as the Inter-American Development Bank (IDB), Asian Development Bank (ADB),

and even national development banks (NDBs). PPPs are now a highly promoted part of the tool kit for the promotion of development finance across the world.

The ascendancy of PPPs both in terms of the rhetoric as well as in the volume of announced deals are of little surprise, as PPPs serve many interests. For governments, both in developing countries as well as in donor countries, PPPs are a convenient means to increase the provision of infrastructure and services without directly increasing government spending. International development agencies, on the other hand, can increase the leverage of their funds when they join in financing PPPs. They can also simultaneously facilitate numerous PPPs without providing any of their own financial resources or assuming any financial risk. Domestic development banks are similarly enthusiastic because of the increased amount of financial resources that often flows through their channels. For their part, private investors have more investment opportunities and can seek political assurances for them. PPPs allow the investors to combine profits with reduced risk. While not all of these goals are mutually compatible, they form a sufficiently coherent mix of aligned interests such to explain the strong growth of PPPs.

In fact, the last two decades witnessed a substantial rise in the quantity and aggregate amount of PPPs. A first wave occurred in the early 1990s until stopped by the 1997/1998 Asian Crisis (World Bank Group 2016a). This was followed by a second wave of PPP investments from 2004 to 2012 (Romero 2015). Although the growth of PPP investments slowed during the Great Financial Crisis in 2007/2008, it resumed its pre-crisis pace shortly thereafter. Investments jumped from USD 22.7 billion in 2004 to USD 134.2 billion in 2012, mainly driven by the demand for infrastructure development in rapidly growing developing countries. However, developed country firms were also supportive of participating in PPPs because of the prospect of lower risk assumption and higher returns on investment, especially when compared to the decreasing opportunities in the slower-growth advanced economies. Investments shrunk to USD 84.4 billion in 2013, mainly reflecting lower investment in Brazil and India, but have since fluctuated at roughly similar levels (Romero 2015). Today, PPPs are employed in more than 134 developing countries, where they account for about 15-20 percent of infrastructure investment (World Bank Group 2015a). While the total number of projects increased, there is signifi-

cant variation in the size and locations of these PPPs. For instance, the average size of projects has increased substantially, from USD 182 million in 2003 to USD 410 million in 2010 and USD 322 million in 2013. Regionally, Latin America and the Caribbean, as well as South Asia, were the main sources of the aggregate expansion, experiencing a steady growth in investments until 2009 for the former and 2010 for the latter. While Latin America and the Caribbean posted positive growth in PPPs shortly after, albeit experiencing a renewed shortfall in 2013, PPP investments in South Asia continued to decrease (see Figure 1).

More generally, it was Brazil, China, India, Mexico, and Turkey (the “Big 5” in Figure 2), that had the most growth of PPPs (World Bank Group 2016a) compared to the rest of emerging markets and developing economies (EMDE).

It is apparent that PPPs are an increasingly important component of the development toolkit and with the ongoing implementation of policies in support of the AAAA and Sustainable Development Goals, PPPs are likely here to stay. Given this trend, it is imperative for practitioners and observers alike to better understand the operations and impact of PPPs. This can encompass a broad range of questions: Do PPPs achieve their intended goals of advancing sustainable development? What are the pitfalls of this contractual technique between the public and the private? Under which conditions are PPPs likely to generate benefits and under which conditions are they likely to lead to failure? What role in PPP development is being undertaken by the international development banks, which have been a major source of international public financing for infrastructure and other long-term investment in developing

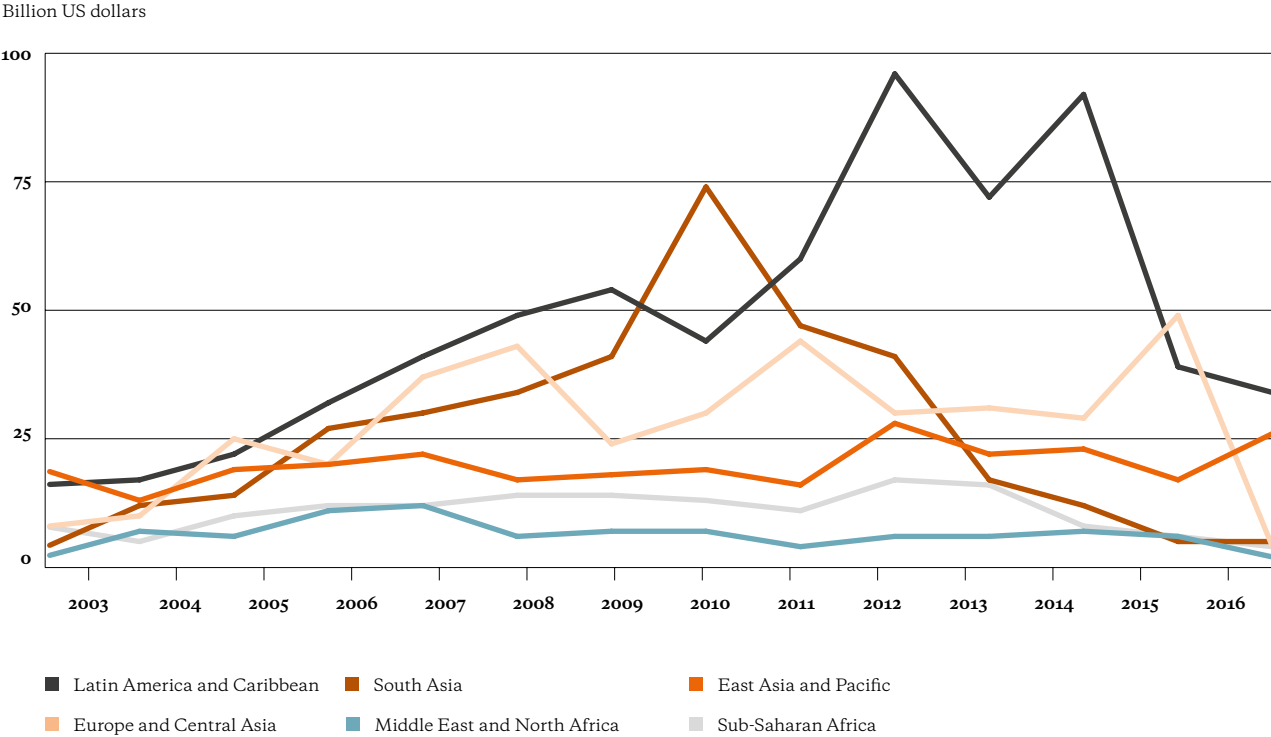


Figure 1: Private investment in PPP infrastructure projects by regions, 2003–2016 (billion US dollars)
 Source: World Bank 2017d

countries since the Second World War? What is the current role of development banks in the planning, implementation, and ownership of PPP projects in developing countries? In what ways have development banks supported the propagation of PPP projects? What are the challenges associated with development bank support. Finally, how can CSOs ensure that PPPs are implemented with the greatest social benefit?

lifecycle - initiation, implementation, and ownership. Lastly, it highlights the critical points which should be in the focus of CSOs seeking to ensure the best possible implementation of the individual PPPs in developing countries.

In order to address these questions, this paper first briefly addresses the gap in infrastructure financing and the potential role for PPPs to mobilize private finance for investment. It then seeks to identify the various types of contractual arrangements subsumed under the heading of PPPs and details both the positive and negative aspects of PPPs. It then documents how development banks of all varieties have guided the development of PPPs, including during the three stages of the PPP

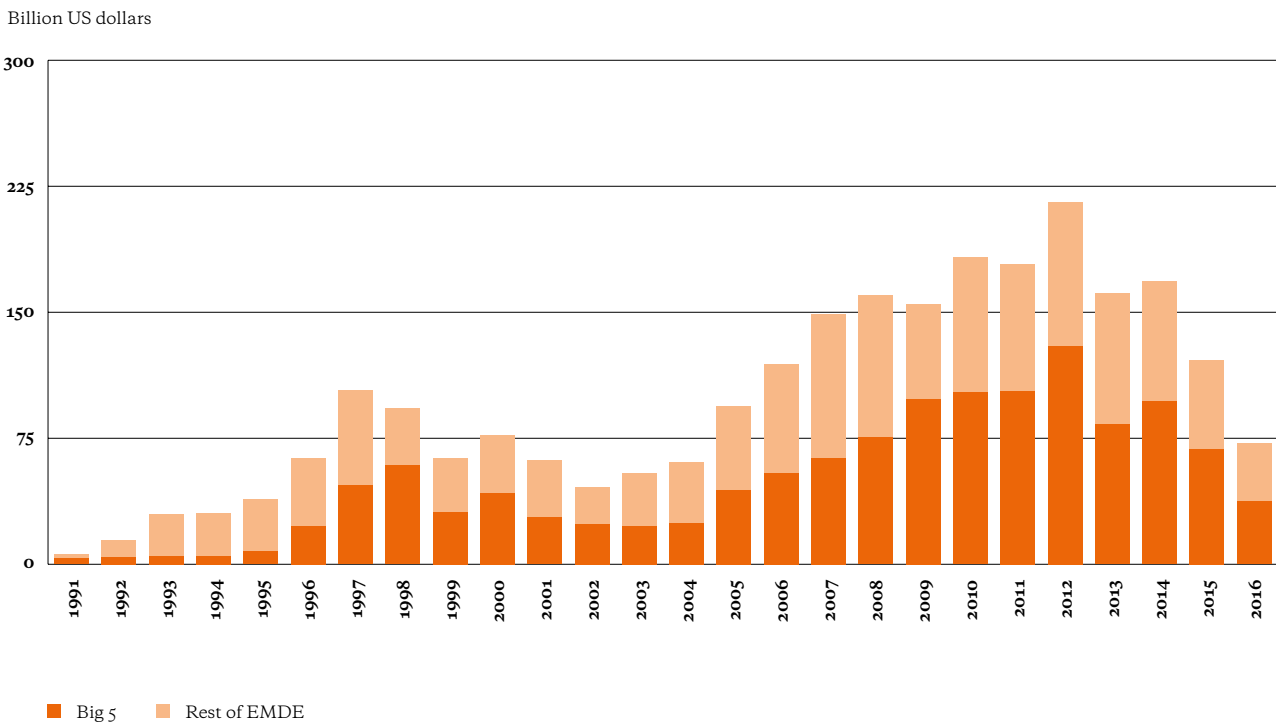


Figure 2: Infrastructure PPPs in the big 5 and Rest of EMDE, 1991–2016 (billion US dollars)
 Source: World Bank 2016, 11. *Nota bene:* these numbers include both domestic projects as well as those with foreign financing

Chapter 1

Mobilizing International Private Finance through PPPs

As noted above, the AAAA assumes that the quantity of government investment is insufficient to reach the SDGs in both developing countries (DCs) and emerging market economies (EMEs). Instead, the AAAA argues that financial frameworks should be amended to induce private sources to finance projects that promote sustainable development. There has indeed been a large flow of private international finance into EMEs and DCs, but it has been volatile and unevenly distributed across the developing world (c.f. World Bank 2017a). The policy question is whether or how PPPs could help attract those funds into financing sustainable infrastructure and in more countries.

An array of policy tools - ranging from domestic reforms to make the economy more investor-friendly, to free trade agreements (FTAs) to bilateral investment treaties (BITs) - have sought to make countries more attractive to investors in general. It is not clear to what extent they have been effective. Investors seem to be focused, as always, on profitability and risk, to which end sustained economic growth of the host economy seems the primary factor. In addition, short-term investment is deemed a way to capture strong earnings while reducing the investor's exposure to various risks, including exchange-rate changes as well as declines in investment earnings. PPPs, in contrast, would lock in investor funds for a project, albeit with public guarantees of one sort or another to reduce the risk of loss, while holding out the prospect of profits if the project succeeds over time.

PPPs have existed in various forms for decades. Governments have frequently outsourced the partial provision of services or contracts to private partners through various co-financing and risk-sharing schemes. The modern form of PPPs, with more complicated financial arrangements and deeper private sector provision of services, arose in the 1980s. These new PPPs were envisioned to entirely replace government services by harnessing the innovative capacity and operational flexibility of the private sector. Proponents have argued that utilizing the private sector in this way would reduce the overall financial burden on public budgets. The United Kingdom under Margaret Thatcher provided the first large-scale laboratory for PPPs for these very reasons. A desire to reduce public expenditures, combined with strict public spending limits, raised the attractiveness of PPPs to the government. Consequently, the UK implemented dozens of projects, called private finance initiatives (PFIs), in sectors from infrastructure to healthcare.

Defining PPPs

While the concept of a PPP is relatively straightforward, one of the biggest and most persistent challenges with PPPs has been devising a universal definition. According to the World Bank, a public-private partnership is “a long-term contract between a private party and a government entity, for providing a public asset or service, in which the private party bears significant risk and management responsibility, and remuneration is linked to performance” (World Bank Group 2014a, 14). Other scholars have developed variations of this definition. Forrer et al. (2010) note that PPPs are also defined by shared decision-making in areas that have traditionally been funded entirely by the public sector. Engel et al. (2008) find a distinction in that PPPs bundle multiple investment and service provisions in a single, long-term contract. Lewis (2002) further argues that there is an implication that there is a “cooperative investment of resources and therefore joint risk-taking, sharing of authority and benefits for all partners.”

In practice, however, PPPs have exhibited a significant amount of variation. PPPs vary in three broad categories - the project and sector in which they invest, which functions the private actor is responsible for, and how the private actor is financially compensated. Functions of the private sector can constitute a wide range of activities, including designing a new project, constructing new projects and refurbishing old ones, financing the investment, maintaining the project, and operating the finished product for a specified amount of time. A single PPP project can encompass one or all of these functions, giving rise to substantial variation. This breadth in operationalization has also resulted in a myriad of terms. In addition to PPPs, other related names have included private finance initiatives (PFIs), private finance projects, private sector contracting, public-private relationship, public alliance, and non-profit partnership. All of these terms refer, however, to the arrangement that the public and private sectors share risk and that compensation is dependent at least partially on performance. It also, unfortunately, leads to analytical confusion.

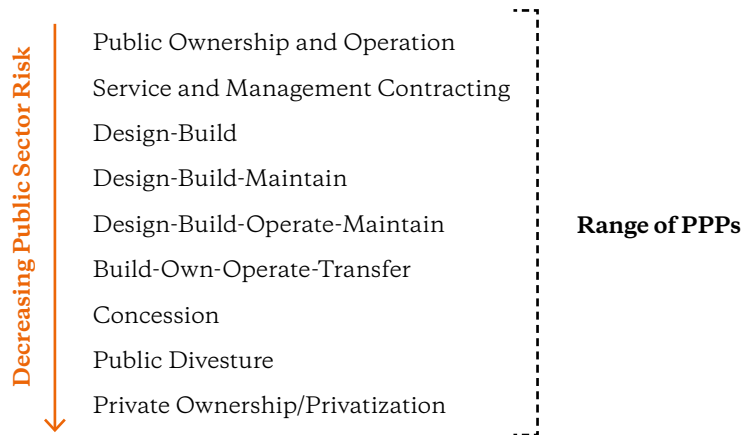
With regards to the responsibilities given to the private sector, on the one hand, some PPPs are nearly indistinguishable from government procurement contracts. Under these arrangements, the private sector has no ownership over the asset and provides a temporary service. The private sector may also upgrade or manage existing assets, a type of project classified as so-called “brownfield

investments”. On the other end of the spectrum, some PPPs have entirely replaced public services with full operation and ownership through a private entity and can border on full privatization. The private actors may be entitled to the operating revenues. Under these arrangements, the private sector frequently engages in new or so-called “greenfield investments”.

The diagram below (see Figure 3) illustrates the breadth of possible operationalization’s of a PPP. If imagined as a linear spectrum between full public risk assumption and full private risk assumption, PPPs theoretically comprise the entirety of possible arrangements between these two extremes. At one end, PPPs distribute very little risk to the private sector, and, as previously mentioned, are virtually indistinguishable from contracting agreements with private actors. Under these arrangements, private actors have limited responsibilities and limited revenues, and contracts are typically shorter term. These can include service contracts, which are based on a one to three year time horizon and a one-time fee, and management contracts, which are for longer-term and have recurring fees. Yet with both, the public sector is still responsible for the majority of capital costs while the private sector performs a contractual service. The private actor assumes little to no risk.

Imagining that a government wants to shift from public provision to a PPP, one can see the government transferring risk to the private partner that it otherwise would bear. As the transfer of risk to the private sector marginally increases, so does the amount of responsibility delegated to the private sector. At low levels of risk transfer, private partners can be tasked with designing and building transportation projects, yet they have no operational or ownership rights to the completed project. Moving up the degree of risk transfer scale, private firms may then be delegated operational and maintenance responsibilities. These can include lease contracts, in which the private actor is financially responsible for addition costs. Towards the higher end of private risk assumption, private actors may build, own, and operate the project for a predetermined length of time. The private actor may be required to transfer the project at a specified date back to a public entity (under a build-own-operate-transfer, or BOOT, agreement), or it may be granted concessional rights, engage in joint ventures with the government, or, at the very extreme, may be afforded de facto full ownership. Under these arrangements, the private sector fronts the capital costs, and operates and maintains the project in the long-term (Asian Development Bank 2008).

Full Public Risk Assumption



Full Private Risk Assumption

Figure 3: Risk Assumption Spectrum and Public-Private Partnerships

Source: Deloitte 2006; Roehrich et al. 2014; World Bank Institute 2012

Private investors in illiquid assets, like infrastructure, tend to be risk-averse, or at least more so than their public counterparts. In order to incentivize private actors to assume more risk, the government will increase the amount of financial compensation that a private actor receives from its investment. Payment in PPPs is usually dependent on project performance in order to keep the interests of the private actor aligned with the public mission. However, this can be achieved through a variety of ways. For one, PPPs can generate revenue through “user pays” schemes, where fees are paid by the final consumer, such as toll roads or ship docking fees. In a “government pays” arrangement, the government is the only purchaser and its payments can be distributed either as contractually defined or output-based (World Bank Group 2014a, 19). However, there are numerous ways to modify and combine these financial incentives. These can include management contracts, turnkey projects, and financial leasing.

This generic conceptualization of a PPP, however, does not take into account other implicit guarantees that the public sector may provide a private actor. For instance, the public sector may guarantee the loan that a private actor issues. Under normal circumstances this does not increase the cost to the public sector, but during economic downturns or a default by the private partner, this arrangement can substantially increase the financial liabilities to the government. The public sector may also be financially responsible for construction overruns or delays. In the long term, the public sector may be responsible for all contingent liabilities, which can include unforeseen maintenance costs and, more commonly, continued subsidization of socially-beneficial services that are unfunded by the private operators. In the case of a subsidized toll road, for instance, the government may deem the tolls charged too high to generate public good benefits, and will provide additional subsidies to lower the cost. All of these measures should be included in evaluations of PPP projects, in addition to the standard risk sharing assessment. Problematically for the government, they can also negate any of the initial cost savings with long-term liabilities.

Chapter 2

Public-Private Partnerships Today

Today, PPPs are no longer limited to public services in the developed world and now constitute an important fixture of international development strategy. From 2007 to 2011, PPPs as defined by the World Bank amounted to approximately USD 79 billion spread across investments in 134 developing countries. PPPs also accounted for around 15-20 percent of total infrastructure spending in developing countries (World Bank Group 2015a). From 2012 to 2014, investments in PPPs grew to an average of USD 124 billion in new projects per year, though in 2015 declined slightly to USD 111.6 billion. Even though new funding is substantial, PPPs remained concentrated in a relatively small number of countries. For instance, between 2011 and 2015, Laos accounted for one third of total PPP funding in infrastructure in low-income countries eligible to draw from the International Development Association (IDA) of the World Bank Group (World Bank Group 2016b). In 2015, Turkey alone comprised 40 percent of global PPP financing in infrastructure. Even though the total amount of funding declined in three countries, Brazil, India, and China, they still accounted for 131 of the total 300 PPP projects in infrastructure in 2015 (World Bank Group 2015b). Within developed countries, PPPs are present but not prevalent; in a 2010 survey of 22 member countries of the Organization for Economic Cooperation and Development (OECD), only four (Australia, Chile, Mexico, and South Korea) used PPPs for more than 10 percent of total infrastructure spending (Burger/Hawkesworth 2011).

As noted previously, the scope of PPPs can be broad. Examples of existing PPP projects include trash disposal systems, prisons, information technology services, stadiums, and pipelines. However, the vast majority of PPPs in developing countries have historically been concentrated in the infrastructure and energy sectors. According to the World Bank, from 2012 to 2015 PPPs in IDA countries focused exclusively on energy, transportation, and water and sewage projects; even then, a vast majority (86 percent) of the projects were in the energy sector, principally in hydroelectric and wind power generation (World Bank Group 2016b). Transportation projects have focused on highways, seaports, and airports. According to the same World Bank report, the vast majority of these IDA PPP projects were “greenfield investments” (86 percent), a rate higher than in non-IDA countries (68 percent). There is also variation in funding structures. Within the World Bank PPI database, which only examines infrastructure projects, approximately 53 percent of total investment for IDA PPPs was raised through multilateral development banks, with another 43

percent from private investments. Only four percent came from public sources, such as public banks or government budgets (World Bank Group 2016b). Moreover, commercial partners were more likely to obtain equity rather than debt. While commercial banks only sourced 27 percent of total debt, they held 73 percent of the equity in the PPP projects; most of the debt was in the form of borrowings from the multilateral or bilateral development banks.

In recent years, more investment has been targeted at non-traditional sectors for developing countries, such as healthcare and education. In the healthcare sector, the World Bank has promoted PPPs as a way to fund vaccinations, hospital construction and maintenance, and food fortification in the developing world (World Bank Group 2013a). However, given the social objectives for healthcare, some PPPs have encountered significant cost overruns and disappointing outcomes. Oxfam criticized one healthcare PPP in Lesotho for costing three times as much as the old public hospital (Marriott 2015). Additionally, the World Bank has supported PPPs in education, both in the construction of new schools and in the operation of existing educational services. Proponents have argued that PPPs in education introduce competition in the education market while reducing the government risk (Patrinos/Barrera-Osorio/Guáqueta 2009). There has also been a rapid increase in the number of PPP projects earmarked for renewable energy projects. In 2015, investment in renewable energy increased to USD 9.4 billion, and focused on PPP investments in solar, wind, hydro, and geothermal energy. Renewables accounted for 63 percent of all energy investments via PPP projects in the World Bank database (World Bank Group 2015b).

Even though PPPs have grown quickly, it is also important to keep them in perspective. As noted above, PPPs still only comprise a small amount of total investment in any one economy. PPPs are also not evenly distributed throughout the world. For instance, in the first half of 2016, Latin America and the Caribbean attracted 43 percent of the total global infrastructure investment in PPPs; the Middle East and North Africa and Sub-Saharan Africa each accounted for only four percent (World Bank Group 2016c). Investments are further concentrated in only a few projects in a few sectors. Despite some experimentation in the health and education sector, nearly all PPP investment goes to infrastructure, energy, transportation, and utility sectors. Therefore, while PPPs have certainly increased the participation of the private sector and raised the profile of development banks in the process, PPPs remain a relatively small – albeit growing – amount of total investment.

Chapter 3

Advantages and Disadvantages of PPPs

In theory, PPPs are envisioned to synthesize the advantages of both the public and private sector. The public sector, with its large budget and government-backing, is able to provide secure, long-term financing for large-scale projects. In addition, since the government is also tasked with objectives that prioritize socially-beneficial projects and public goods, such as infrastructure and social programs, the public sector can invest in projects that may not be profitable. On the other hand, the private sector is considered more efficient. According to the Asian Development Bank, “the private sector’s role in the partnership is to make use of its expertise in commerce, management, operations, and innovation to run the business efficiently” (Asian Development Bank 2008, 1). A PPP endeavors to combine these two sets of advantages. Consequently, the World Bank has heralded PPPs as an important tool for economic development, particularly in developing countries, as “PPP’s can help overcome these constraints by mobilizing private sector finance and helping improve project preparation, execution, and management” (World Bank Group 2015a, vi).

Advantages

Proponents have cited numerous reasons for supporting PPPs. These can be divided into five broad points:

- 1. Compensates for the public funding shortfall:** The developing world lacks adequate investment. According to the World Bank, existing investment shortfalls in infrastructure in developing countries amounts to USD 1 trillion per year through 2020 (World Bank Group 2013b, 4). A McKinsey report estimates that USD 57 billion in global infrastructure investment will be necessary just to keep up with projected global GDP growth (McKinsey Global Institute 2013). In many developing countries, governments lack the ability to provide the large amount of upfront capital necessary to make investments in key infrastructure and social projects. Governments may also be unable to borrow money on international capital markets because of weak credit ratings and underdeveloped financial sectors. In operation, governments may be ineffective in delivery and lack the financing and ability to ensure long-term maintenance. Instead of using public funds for projects, PPPs can help distribute the financial burden to the private sector in exchange for the
- 2. Incentivizes private investment:** As detailed in the previous section, attracting private capital, especially to developing countries, has been a growing emphasis of the international development community. However, despite the existing strategies of tax reductions, freer international private capital flows, and stronger legal frameworks, the growth of foreign private financing of long-term investment has not achieved its envisioned goals. PPPs present a possible solution. By allowing private actors to gain long-term security via the public sector through non-traditional financing methods - such as through secured long-term operations contracts or fiscal guarantees - private investors are incentivized to undertake investment projects. This should theoretically attract more private investment to projects that would otherwise remain unfunded. International development banks are particularly enthusiastic about incentivizing private financing. As the World Bank argued, the public sector, through mechanisms like PPPs, can serve “a catalytic role in attracting private sector financing” (World Bank Group 2013b, ix). The 2015 Addis Ababa resolution also specifically cited PPPs as an important strategy to achieving development financing targets.
- 3. Increases operational efficiency:** One of the greatest challenges for new investment is understanding the best strategy to implement the investment. It is often assumed that public sector actors have fewer incentives to reduce costs in implementation and operation of projects. By utilizing the profit incentive of private firms, PPPs allow the government to provide important public goods at a lower cost. As the ADB describes, private actors “enter into an investment or contracting opportunity with the clear goal of maximizing profits,

granting of concessionary services or asset ownership. While these PPPs will ultimately provide the desired investment, the cost of the project will remain off the government budget. That is, the government is not required to either list the PPP as a liability on government balance sheet, nor does it have to use budgeted funds. In this way, PPPs can be off-balance sheet public investments. To international development banks, which also lack the financial resources to close the total investment gap, PPPs may be seen as an effective contribution to solve the public funding shortfall in developing countries.

which are generated, in large part, by increased efficiency in investment and operations. If the PPP is structured to let the operator pursue this goal, the efficiency of the infrastructure services will likely be enhanced” (Asian Development Bank 2008, 4). Contracting with private firms with better on-the-ground knowledge can increase project efficiency and, more importantly, encourage more innovative solutions while minimizing inefficiency (World Bank Group 2014c, 3). Finally, with long-term time horizons, private investors are incentivized to have a whole-lifecycle approach. A potential hazard of short-term service contracting with private actors is that the private actor will not bear the costs of poor quality construction. However, if the private actor is responsible for both the implementation and operation of the PPP, they are incentivized to have higher quality implementation in order to reduce overall long-term costs (El-Haram et al. 2002).

4. Transfers risk to the private sector: While the public sector may provide a limited number of financing guarantees, the objective of a PPP is to at least partially transfer the risk of the project to the private sector. This has a dual impact. First, the government is supposedly less liable for future contingencies, thereby reducing the financial burden to the public. This is realized both in the short-term, since the public sector does not have to provide the upfront investment, as well as in operationalization where first losses normally accrue to the private sector. Second, by assuming partial risk, the private sector is incentivized to produce the project in a profitable manner. Risk transfer ensures that incentives are aligned. In exchange for risk, the private sector receives greater financial compensation. They can either secure long-term contracts with the government or they are able to retain a share of the profits from the operation of the project. So long as the private sector shares the risk during the implementation and operation of the PPP, then higher quality services may be produced at a lower financial cost than the public sector option. It also allows the government to provide these services without adding them directly to their balance sheets.

5. Increases technological transfer and innovation: Private actors often have deeper, more specialized knowledge than their government counterparts. By

providing joint investment opportunities, some have argued that PPPs contribute to technological transfer from the private to the public sector that ultimately lead to secondary efficiency gains within the public sector. Proponents argue that this is particularly effective in the provision of services, such as in the health-care, education, and management sectors. In a similar vein, private actors may be more innovative than their public counterparts, largely because of their profit motives. This can result in a more efficient deployment of public sector resources. Efficiency gains in project implementation and operation should lead to a decrease in the financial cost, optimizing the utilization of private funds.

Disadvantages

Despite their purported advantages, PPPs have not always been as successful as its promoters claim. A significant body of literature has found that PPPs often do not meet expectations on delivery of planned services and, under certain conditions, can actually lead to worse development outcomes. The problems with PPPs are detailed below.

1. Crowding out investment: One danger in a public-private partnership is if the government subsidizes a private firm with public financing that would have been invested anyway. This effectively amounts to a direct wealth transfer from the public to the private sector, with no additional benefit to society. This problem is exacerbated when the PPP project either originates from a private interest or when the government directly negotiates with a private actor without tendering a competitive bidding process. Therefore the implementation of PPPs can crowd out private investment. Since the government can financially guarantee a project, the cost and the risk of undertaking a PPP is artificially decreased, disincentivizing other private actors from investing in the project. By driving out other private actors, competition is reduced and social gains could be further limited. There has been evidence that has suggested that PPPs can reduce aggregate public investment. According to a study by Rhee and Lee (2007), the South Korean government’s promotion of PPPs has replaced government spending, but not increased aggregate spending on infrastructure.

Moreover, there is a risk that private interests could leverage the government's financial backing to earn higher rates of return on their investments. That is, the government accepts a portion of the risks of the investment, yet the private sector is able to profit and capture the upside of investments. Furthermore, if the private actor is allowed to earn profits at a higher rate than the financial cost of the government loan, then private firms are able to earn additional profits on investments than would otherwise be profitable. However, it is usually difficult *ex ante* to determine the appropriate rates of return on investments.

2. Increased implementation and monitoring costs:

Despite the objective to reduce the overall cost of projects, there is evidence that PPPs can, in some cases, actually cost more than if the government had implemented the project itself. This is due to a number of factors. For one, governments may be poor selectors of PPP projects and armed with flawed analysis (World Bank Group 2014a, 18). In addition, private contractors are likely to incorporate market risks into the initial bidding price, reducing savings. Research from major international organizations has found that PPPs can on average cost 25 percent more than their public counterparts (Hall 2014). It should be noted however that the evidence is mixed. According to the UK's National Audit Office in 2003 and 2008, PPPs were found to be more likely on-budget and on-time than their public project counterparts. Similar findings were found with PPP projects in Australia in 2007 and 2008 (World Bank Group 2014a, 43). Since PPP contracts transfer some risk from the government to the contractor, the risk premium is simply included in the original price to hedge against unexpected costs. The World Bank explicitly notes that "development, bidding and ongoing costs in PPP projects are likely to be greater than for traditional government procurement processes" (World Bank Group (2017b)). The IMF (Public-Private Partnerships, 2004, 14) has also noted that governments often overestimate risk: "It is also possible that the government overprices risk and overcompensates the private sector for taking it on, which would raise the cost of PPPs relative to direct public investment." (IMF 2004, 14) Taken together, these factors may ultimately increase the cost of PPP project implementation.

In addition, PPPs often require greater technical capacity than a standard government procurement con-

tract. Since private investors are usually responsible for long-term maintenance and management operations, fewer private actors are willing and able to bid. This can counterintuitively result in a less competitive bidding process that ultimately raises the cost for the public sector (Hall 1998, Roehrich/Caldwell 2012). Since the government cooperates with multiple implementing actors, it can also be costly for the government to monitor its private partners (Lonsdale 2005, Pollack et al. 2011). To make matters worse, oftentimes the public option is not considered during PPP project assessment. The IMF has supported a move to systematically measure PPPs in comparison with the public option, in addition to the competitive bidding process: "When considering the PPP option, the government has to compare the cost of public investment and government provision of services with the cost of services provided by a PPP." (IMF 2004)

3. Obscuring and increasing public debt:

Perhaps more perniciously, PPPs can be a mechanism to hide government expenditures and the public's contingent liabilities. In the past, the donor community and IMF, in particular, has aggressively encouraged developing country governments to reduce public debt burdens. Measures to do so have included the reduction in public expenditures, and the privatization of state-owned enterprises. In practice, these have proven to be socially costly. PPPs have emerged as a new policy tool. Since PPPs are not directly financed by the government, these costs do not appear on official measures of government debt or on the yearly budget. In order to remain within budget deficit targets, developing countries are incentivized to substitute PPPs for public investment for accounting reasons, regardless of potential consequences. Consequently, PPP projects may be selected for reasons other than socially-beneficial reasons, undermining their purported advantages.

Moreover, PPPs can raise the cost of projects vis-à-vis a public option because sometimes contingent liabilities become actual liabilities. The World Bank has explicitly acknowledged this problem: "PPPs may appear to relieve funding problems more than it is actually the case, as the government's fiscal commitments to PPPs can be unclear. This can lead to governments accepting higher fiscal commitments and risk under PPPs than would be consistent with prudent public financial management" (World Bank Group 2014a, 32).

Examples have included long-term revenue guarantees for toll roads and electricity payments in Colombia and in South Korea, exchange rate exposure on public roads in Mexico, and an equity injection into the UK's recently privatized air traffic services (World Bank Group 2014a, 37). As a result, many NGOs have declared PPPs to be insufficient solutions to solving public sector investment problems.

4. Emphasis of private interests: While PPPs may endeavor to synthesize the interests of the public and private sectors, their objectives may ultimately remain at odds. Many scholars have noted that it is difficult to fully align the objectives of the private sector with the public sector. For example, during project negotiation, private firms are tempted to overbid for projects, particularly when there is a lack of competition, even though the government wants to maximize social benefit (Hall 2014). In implementation, private actors are incentivized to reduce costs in the short-term rather than long-term. The divergence is particularly acute after project implementation. Numerous studies have found that during the operational phase of PPPs, private actors will increase the cost of contracted service because of their monopoly power. For instance, a comprehensive study on French water PPPs concluded that municipalities with PPPs paid 16.6 percent more in water costs than those with government-provided services (Chong et al. 2006). Ensuring that incentives align for both actors has proven extraordinarily difficult when considering that future risks are often unknown.

5. Lack of PPP assessment measures: While PPPs may be purportedly beneficial, there is a surprising lack of empirical research that demonstrates precisely when and how PPPs are most effective. This is largely the consequence of the incomparability of PPP projects - there is substantial variation in the project scope, sector, risk sharing arrangement, legal framework, private sector compensation, and financial instruments. Even though existing World Bank assessments have concluded that PPPs are effective around two thirds of the time, they also note that extrapolating these results to PPPs more generally is difficult. This is because of the selection bias of projects, since the World Bank and its member the International Finance Corporation (IFC) principally choose relatively safe projects with sufficient data base (World Bank Group 2015a, 140).

In other words, PPP assessments are conducted on an ad-hoc basis by various institutions, and little is systematically known about the causes of PPP success or failure. A 2013 Dutch government report found that the empirical evidence from PPP evaluations is sparse and can only provide weak evidence for project effectiveness. No evidence was available on issues of environmental protection and project cost-effectiveness (Ministry of Foreign Affairs of the Netherlands 2013).

Moreover, the basis for evaluating PPP performance has predominantly focused on bankability aspects, namely value for money calculations and cash flows analysis. The value for money calculations, which specifically assess the private option vis-à-vis the public option, has been advocated by nearly all international development financial institutions (Burger/Hawkesworth 2011). However, this assessment omits more qualitative aspects like total social benefit, quality of service, financial risk distribution, and transparency measures. While focusing on financial aspects is certainly important, these assessment criteria may encourage PPPs to adhere to private measures of success rather than public ones. Development banks are aware of this problem - and have developed corresponding guidelines (European Commission 2004) - this has still yet to result in a common assessment framework or a paradigm shift away from purely financial considerations.

In sum, the contours of the PPP debate are complicated and largely unclear. On the one hand, there has been some evidence that PPPs can encourage sources of private financing which would otherwise not have been invested and can provide improvements to project efficiency. This has been the official position of the Group of 20 and most international financial organizations. On the other hand, the systematic benefits of PPPs are unknown and the temptation of private capture of public services has the potential to increase costs and decrease output. As much research has shown, from both civil society organizations and the international development banks, there are numerous pitfalls that can negate the benefits of PPPs.

Chapter 4

Development Bank Promotion of PPPs

Critical to the proliferation of PPPs has been the support of multilateral and bilateral development banks. PPPs began as a mechanism to reduce a government's financial burden in social programs and infrastructure projects, yet have slowly morphed into an important development tool. The recent 2015 Addis Ababa Agenda has only further solidified the mobilization of private capital as the primary source of funds for economic development. As such, development banks have increasingly participated in developing and overseeing PPP projects around the world. While they will provide their own capital for PPP projects, they have also increasingly served as important coordinators of PPP investments, providing guidelines for PPP implementation, advising governments on regulations, and cataloguing existing projects. Despite this growing influence, little research has examined how development banks affect the implementation and operation of PPP projects. The World Bank has been the most active of the development banks in promoting new PPPs. As of 2015, the World Bank had 26 active PPP projects worth USD 4.1 billion (Hall 2014, 14). The World Bank has also been one of the leading international institutions promoting PPPs. This has included international publications supporting PPPs, such as the G20 Investment and Infrastructure Working Group discussion paper (World Bank Group 2014c), and developing guidelines on governance of PPPs in the water, transportation, and power sectors (World Bank Group 2014a, 31). The IFC, the private sector development arm of the World Bank Group, has been even more active than its development bank counterpart. In 2015, the IFC had 59 active PPP projects that facilitated USD 3 billion in additional private financing. Since 2004, the IFC has reportedly facilitated more than USD 20 billion in private investment (IFC 2017a).

However, unlike the World Bank, the IFC's funding is mainly lent to the private actors rather than the government partner. The IFC has reported that its PPP projects have been successful (IFC 2017b), but NGOs for example in Indonesia, India, Brazil and El Salvador have noted the severe shortcomings of some of its investments (Hall 2014, 27-28).

Direct funding of PPP projects from the World Bank Group occurs only in limited amounts. Restrictions on budgets and complicated procurement requirements render the process complicated and limiting. Instead, the World Bank Group has emphasized a strategy that transfers knowledge for new PPP projects. Both the World

Bank and the IFC have developed model agreements and implementation guidelines. Particular to the infrastructure sector, the World Bank Group has also developed two specified centres (World Bank Group 2014b). One is the Public-Private Partnership in Infrastructure Resource Center for Contracts, Laws and Regulations (PPPIRC), which provides "legal materials which can assist in the planning, design and legal structuring of any infrastructure project" (World Bank Group 2017). This helps countries write new PPP proposals based on existing or past PPP projects to ensure that they are implemented appropriately, as well as helping both governments and private actors with sector-specific information. The PPPIRC also provides extensive information regarding the PPP legal frameworks of each country.

In addition, there is the Public-Private Infrastructure Advisory Facility (PPIAF). Created in 1999, the PPIAF promotes new PPPs in the infrastructure sector, encourages the adoption of PPP-friendly laws in developing countries, designs new PPP projects, and provides assessment and evaluation services for completed projects. The PPIAF specifically notes its knowledge diffusion role: "PPIAF focuses on the development of new knowledge through research and helps to make existing knowledge more accessible to policy makers and other stakeholders. The offerings aim to identify solutions to infrastructure challenges and disseminate the best practices and lessons learned through PPIAF's technical-assistance activities to our clients, donors, and the broader development community" (PPIAF 2017a). Together with the PPPIRC and the other activities of the World Bank and IFC, the World Bank Group has been perhaps the most important supporter of PPPs.

Other multilateral development banks have also strongly supported PPP projects. Within Europe, the European Investment Bank (EIB) has some of the most well developed PPP programs, though, unlike the World Bank, their projects have nearly exclusively focused on investments within the European Union, plus Turkey and Israel. In 2015, the EIB itself provided EUR 1.2 billion in financing for 13 projects, eight of which were in the United Kingdom (EPEC 2016a). To support projects not directly financed by the EIB, it founded in 2011 the European PPP Expertise Centre (EPEC), which has been tasked with the mission to "strengthen the ability of the public sector to engage in PPP transactions" (EPEC 2016b). EPEC has provided a members-only platform for EU countries to share experiences from PPP projects and

ensure best practices. In addition, EPEC has published a number of documents relating to issues in PPP implementation, including guidelines for how PPPs should be implemented (EPEC 2015a) and (EPEC 2014), how they should be assessed (EPEC 2015b), and how they should be treated within national statistics and state aid regulations (EPEC 2016c). The European Bank for Reconstruction and Development (EBRD) has also strongly supported PPP development over the past 20 years. Like the World Bank and EIB, the EBRD has largely avoided direct investment in favor of advisory services. The EBRD's Legal Transition Programme (LTP) has advised countries on PPP assessments and concession frameworks, technical assistance and legal reform projects, international PP standard setting, and outreach with other international organizations (EBRD 2017). The other large regional development banks have also all created advisory services for PPP implementation, including the Inter-American Development Bank, the Asian Development Bank (Asian Development Bank 2008), Islamic Development Bank, and the African Development Bank. However, as the World Bank acknowledges, the synergies between the multilateral development banks has been limited because of the lack of policy harmonization (IEG 2017).

To a lesser extent, national development banks have also provided financing for PPP projects. The KfW (Kreditanstalt für Wiederaufbau), the German national promotional bank, has implemented a few projects at the municipal level in Germany with generally positive success (KfW 2015). The German government has also supported joint investments with the private sector through the develoPPP.de program, implemented by DEG (a subsidiary of KfW), as well as GIZ (Gesellschaft für Internationale Zusammenarbeit). Since the program was launched in 1999, there have been more than 1,500 projects, two thirds of which were in East Asia, South Asia, or Sub-Saharan Africa, across numerous sectors. Moreover, while the German government has provided EUR 330 million, it has also attracted EUR 558 million in private participation (BMZ 2017).

As noted before, the majority of development bank activities focuses on advisory services rather than direct investment. In order to finance these programs, development banks often create special funds to administer their technical assistance projects. The Public-Private Infrastructure Advisory Facility (PPIAF), for instance, has a Program Council that defines the strategic direction of technical assistance programs and works closely with the

independent Technical Advisory Panel on ex-post evaluations. It also ensures that funding from 15 donor agencies continues to be provided (PPIAF 2017b). PPIAF also supports the World Bank's PPPIRC (PPP-Infrastructure Resource Center). There are also a host of other funds. Similarly, in its 2020 strategic vision for PPPs, the Asian Development Bank has advocated the creation of project development funds (PDFs) to create an enabling environment (Asian Development Bank 2012). Finally, the EIB has implemented the MED 5P Initiative (Public-Private Partnership Project Preparation in the Southern and Eastern Mediterranean) to support technical assistance programs "to unblock a number of PPP projects in Egypt, Jordan, Lebanon, Morocco and Tunisia" (EIB 2014, 4).

Chapter 5

Development Bank Influence in the PPP Lifecycle

Three stages may be identified in the lifecycle of PPPs - initiation, implementation (construction), and operation. Development banks have been involved in each of them, a relationship that could benefit from greater scrutiny.

Stage 1: Initiation

The first stage of a PPP is its initiation - which projects are selected? Who are the chosen public and private partners? And perhaps most importantly, who decides? The biggest risk at this stage is that projects are selected for reasons other than maximizing social welfare. Private actors often have close connections to government, and the potential for corruption is high in underdeveloped countries. Moreover, complex bidding conditions or lengthy contract requirements often eliminate potential bidders, and therefore competition, which could potentially undermine cost-savings. This can only serve to exacerbate the risk that projects are selected based on the interests of the private sector rather than the public good.

In order to mitigate these risks, development banks have created a series of initiation frameworks to safeguard proper initiation. For example, in 2014, the World Bank developed a comprehensive checklist for potential PPP projects that emphasized improvements in governance. The World Bank thus now insists that these PPPs have widespread domestic political support, particularly from high-ranking officials, to ensure that projects are selected fairly and transparently.

The World Bank has also been active in the promotion of PPP frameworks, which are legislated rules and regulations that “lay out a process for approval, procurement and regulation of projects through construction and approval stages and specify which public authorities can sign the PPP agreements” (World Bank Group 2014b, 5). The World Bank’s previous experiences with PPPs suggested that establishing a framework that specifically governs PPPs resulted in better outcomes. Therefore, the Bank has strongly advocated for domestic reforms in the legal system. However, the World Bank has been hesitant to provide specific systematic recommendations for domestic changes. For example, while they raise the idea that private actors engaged in PPP projects should be able to legally challenge the government through a dispute resolution mechanism, they do not officially endorse the measure. Other development banks have provided similar advice to ensure that PPPs are promoted and

function within a legal framework, but without providing direct recommendations on domestic reforms.

Development banks have also acknowledged the possibility of unequal negotiations of PPPs. In order to counter this, development banks have engaged in early-stage capacity building. For instance, the World Bank has developed a comprehensive document on the types and advantages of different PPP arrangements to help “policymakers and their advisers to better understand some of the most important and difficult issues related to the design, award, implementation, monitoring, and modification of concessions” (World Bank Group 2014b, 7). The risks of discrepancies in negotiating capacity were also addressed at the Addis Ababa conference. According to discussions, experts argued that PPPs “should be drawn up as robust contractual relationships under strong public-private partnership laws”. In addition, they noted that the state should still play a strong advisory role: “A dedicated public-private partnership unit should be established to oversee the negotiation and implementation of such partnerships” (UN 2014b, 4/5).

The increased attention to building up government capacity prior to the planning stages is a direct consequence of the poor results of PPPs from the 1990s and early 2000s. Projects were often ad hoc and governments lacked the experience necessary to guard against private sector influence and future contingent liabilities. However, the role of development banks has shifted. Instead of directly financing PPPs, most development banks have increasingly shifted to providing advisory and technical services. Development banks have also begun to serve a coordinating role, linking private investors with potential public investments. This has certainly helped developing country governments - there are more projects now, and development banks have increased the bargaining position of governments by arming them with model PPP contracts and specific information. However, since development banks are often not directly participating in the negotiation process, governments are frequently not better equipped to gain more favorable contracts. Under these circumstances, PPPs are direct agreements between the government and private actors, and development banks are not ultimately responsible for the content of the final PPP agreement. Only when development banks themselves provide capital for a specific PPP do they directly participate in negotiations and absorb project risk. Moreover, given that supporting PPP initiation is relatively low-risk, funding has been increasingly ear-

marked for the promotion of new PPP projects. There is a risk that in order to reduce risk and criticism of their investments, development banks begin to push for even more PPPs.

Stage 2: Implementation

After the project has been selected, then the PPP must be implemented, i.e., the road must be constructed, the port built, the electric wires strung. This stage raises a new set of questions – how will the projects be carried out? How will the construction risk be shared between the private and public sectors? How will the impact assessments be conducted, and how will procurement procedures function? As with any development project, there is significant risk of cost and time overruns, as well as negative impacts on the environment, labour, and local populations. Implementation, particularly in large-scale infrastructure or energy projects, is often disruptive, and without proper surveillance it can engender bad outcomes.

Of these three stages, the implementation stage is perhaps the one best addressed by development banks. The World Bank, in developing its checklist for PPP projects, has provided detailed questions about project execution. These include topics in internal and external capacity for implementation, procurement procedures, and contract management (World Bank Group 2014b). Like the initiation stage, development banks have also established some technical and advisory services to reduce government risk exposure during project implementation – such as guarding against cost overruns – or providing substantial legal advice to ensure private actors abide by the contracts. More recently, the World Bank has also promoted enhanced transparency measures, and in 2016 circulated a framework for the public disclosure of information in PPP projects (World Bank Group 2016d). In addition, existing international standards for public projects still apply for PPPs. Standards of the Development Assistance Committee of OECD, for instance, are still used by its members to evaluate projects and their implementation.

Yet despite these guidelines, critics of development banks have highlighted that implementation measures have not always produced desired results. Most importantly, development banks do not closely monitor PPPs when they are not an invested actor. In such cases, by making the PPP contract one solely between the private

sector and the government, international regulations frequently do not apply. For example, there are limited – if any – disclosure requirements on such PPPs; these depend exclusively on the regulations of the country. Procurement, assessment, and management measures for PPPs are similarly non-transparent and inconsistent. Moreover, even if these results were public, there are still no international standards for project procurement and management for PPPs. To be sure, the World Bank and other development banks have made efforts to encourage adherence to international best-practices; yet without a stake in the investment, these recommendations can be easily ignored. PPPs that do not involve multilateral banks (or bilateral donors) present a significant challenge for CSOs during project implementation. The lack of direct development bank participation removes a critical point of contact between civil society and the investor. Given the differentiated nature of individual PPPs anyway, as well as the absence of CSO access to information, it is more difficult to systematically monitor projects across countries and sectors.

Stage 3: Operation

After construction has been completed, there are a variety of ways that PPPs may be operated. This raises a final set of questions – who should have operating and ownership rights over the completed project? How will the private sector be compensated in the long-term? Who will be responsible for unforeseen costs in operation and maintenance? Early PPP projects were notoriously bad for taking advantage of government partners. Often private enterprises were granted long-term contracts or ownership at higher cost than if they government had provided the service itself. Private actors were also known to raise the cost of services to rates higher than previous agreed to or would reduce service. Poor contracting also made governments responsible for financial cost. Guaranteed revenue schemes, for instance, were particularly costly for governments.

Since then, development banks have tried to improve issues of long-term ownership and operations of PPPs. Advisory services from development banks provide information on how concessions could be structured, and methods to mitigate future costs using case studies from previous PPPs (EBRD 2017). The World Bank has also provided some guidelines for possible ways to measure

the effectiveness of specific sectors, such as education-related projects (Patrinos/Barrera-Osorio/Guáqueta 2009). Outside of advising, the World Bank Group has also been good at providing self-evaluations: All of the IFC's investments in PPPs, the Multilateral Investment Guarantee Agency (MIGA) guarantee projects, and World Bank direct loans are subjected to regular monitoring. According to these reports, a majority of investments have been rated satisfactory or better (83 percent for IFC projects and 66 percent for World Bank ones), yet these heavily rely on business performance rather than social performance indicators (World Bank Group 2015a, 63).

However, development banks have dedicated significantly fewer resources to helping countries monitor PPPs, particularly in the long-run. The World Bank's PPP checklist does not mention ways to ensure effective long-term project management aside from adding clauses in the initial contract. Neither the PPPIRC nor the PPIAF have programs in place to help governments fund evaluation programs, so governments have fewer resources at their disposal. As the World Bank's Independent Evaluation Group (IEG) reported in 2014, this is an area that requires improvement if PPPs are to be expanded in the future, as "arrangements are needed to monitor the performance of PPPs throughout major parts of their lifespan." The IEG report also notes that existing evaluation criteria do not adequately address broader measures of success: "PPP's need to be measured in a more multifaceted manner to shed more light on important aspects of public service delivery, for instance, access, pro-poor aspects, and quality of service delivery. But such data are rare." The World Bank management has fully agreed with this assessment. In a recent report, the World Bank acknowledged that it will "identify a process through which a suite of principles can be created to guide and inform task teams seeking to monitor the performance of PPP operations. Additional work on impact evaluation placing PPPs against other models of service delivery may have to be explored for a fuller understanding of potential impacts" (World Bank Group 2015a, xxvi).

Yet while development banks have certainly improved the amount of attention they give to ownership and operation issues, not every PPP falls within their area of interest. The World Bank Group, for instance, only monitors and evaluates the projects in which it has invested, not necessarily all of the projects on which it has advised. This is a similar practice for the other development banks as well. Consequently, not only is there

a lack of systematic data within the World Bank, there is no comparability in assessments across all PPPs. This creates severe difficulties when trying to evaluate the strengths and weaknesses of various aspects of PPP projects. The development banks also take no official position on ownership structures, allowing the governments to decide what the best way for them is.

Chapter 6

Conclusions and Recommendations

This report has examined the origins, definitions, and implementations of public-private partnerships, with particular emphasis on the role of development banks in the recent promotion of PPPs. While the number of public-private partnerships has expanded sharply in recent years, less research has focused on the impact these PPPs have had on the international development landscape and the ways that development banks have engendered these changes. As the global development objectives become increasingly tied to the mobilization of private financial resources, and the goals of the 2015 Addis Ababa meeting are brought to fruition, it is likely that PPPs will continue to expand in both number and scope, despite the numerous problems of PPP efficacy. In the absence of a complete reversal of the trend towards private financial promotion by the donor community, CSOs should develop both a strategy and technical capacity to assess PPPs. Going forward, what is the best way to ensure that PPPs generate the greatest amount of public benefit? How can civil society organizations steer PPPs into financially sounder and more socially responsible investments? We offer five recommendations.

1. Define public-private partnerships (PPPs) and their appropriate role in society:

As mentioned previously, PPPs encompass a wide range of arrangements from contracted private engagement in large, state-owned projects all the way to de facto privatization. The definitional imprecision, however, also confuses the ability to monitor and evaluate PPPs. Without a standard framework for comparison, systematic analysis is more difficult than it would otherwise be. In order to counter this, CSOs could analyze existing initiatives and cooperate to create a common working definition and typology for PPPs that incorporate different levels of private involvement, different varieties of public assumption of private risk, and different PPP designs appropriate to different sectors. Adding structure to the PPP framework will help increase comparability among disparate PPP projects. This will also assist efforts determining the merits of each new PPP. This information can be shared with the relevant government bureaucracies. It will also assist CSOs to selectively pressure development banks into supporting or opposing new PPP projects.

PPPs often obfuscate the actual role of the private actors in public investments. Consequently, the lack of systematic information makes it difficult to determine the extent to which the private sector is replacing the public one. After developing a common definition and

typology for PPPs, CSOs could better judge which PPPs are the most socially beneficial in which circumstances, and which projects could be better implemented by a purely public project. A significant amount of academic work has found that PPPs can be more expensive than if the government were to implement the project itself (Hall 2014), but there has been no effort to systematically analyze when and under what conditions PPPs may be more beneficial to society. Development banks have already recognized the need to compare PPPs to a fully public sector option, and CSOs could help governments develop these assessments to ensure they operate in the public interest. CSOs could therefore provide an important counterweight to PPP advocates, including development banks.

2. **Prioritize national leadership in PPPs:** If PPPs are to support national economic and social development objectives, then it is crucial that the PPPs remain embedded within both the national and local sphere. Synergies should be sought between national and local organizations as national groups often have greater financial resources and political access, while local ones offer a depth of contextual knowledge. All national and local groups, including in the communities to be affected, should play key roles in the three aforementioned stages of PPPs: initiation, implementation, and operation. At initiation, CSOs should ensure that the projects targeted for PPPs are selected by the relevant national and local stakeholders rather than by the private partner or international institutional actors. Domestic actors should identify projects that would benefit from a PPP prior to selecting a private partner, not the other way around. Not only does this reduce the opportunities for corporations to influence economic development projects, but it also ensures that projects are selected based on their societal impact. In the event that there are unsolicited proposals for a PPP from a private actor, the World Bank has recommended that they undergo rigorous analysis and face competition from other possible partners (World Bank Group 2014a). CSOs can ensure these guidelines are adhered to. During implementation, when possible, CSOs should encourage the utilization of local contracting parties so that the multiplier effects from large-scale investment remain within the country. The World Bank guidelines on PPPs already have codified the use of local suppliers and watchdogs in PPPs; CSOs must ensure that these are upheld.

Finally, CSOs should ensure that local actors retain influence over the operations of the PPP after construction is completed. One of the most problematic aspects of PPPs has been that the private sector benefitted from public support during the initiation and implementation phases, only to later operate the PPP according to private, profit-oriented goals. CSOs can play an important role in ameliorating this problem. This can be achieved in two ways. First, CSOs can advocate during the partnership design stage by promoting local ownership of the PPP, whereby after completion the public sector assumes full operational control of the project, though the opportunities for this arrangement are likely to be limited. Second, CSOs can ensure that a more clearly-defined contract between the public and private sectors is drafted and then implemented that prevents the submerging of societal objectives by private interests. For instance, these contracts could detail the limits of public liabilities for future downside risks, restrict the total amount of public funds that can be provided for operational costs, stipulate long-term contract pricing agreements that prevent price erosion, or require a certain portion of the operation be targeted towards public sector-defined objectives. As mentioned earlier, completely covering all potential future liabilities is nearly impossible. However, CSOs should work to minimize the contingent liabilities to the public sector through better defined contracts that incorporate local stakeholders prior to the initiation and implementation of the PPP and the content of those contracts should be publicly available.

3. Empower local CSOs: Monitoring and enforcement of PPPs is notorious difficult. Normally, the responsibility to enforce best-practice standards falls on countries themselves rather than the private actor or international development partner. To be certain, development banks have drafted guidelines for international best practices in transparency and social responsibility for their own investments, though since they usually only serve in a supervisory role over PPPs, they remain as such – guidelines. The unintended consequence of greater CSO pressure on international development institutions has incentivized these development banks to avoid directly investing in a project for fear of heavy criticism. As such, the strengthening of development bank regulations is less effective and the ability of CSOs to impact PPPs through these institutions can be highly circumscribed.

Instead, international CSOs could support local CSOs in their efforts to monitor PPPs at each stage of the process. International CSOs lack the capacity to individually assess each PPP and, more importantly, this strategy would not necessarily be effective. Since PPPs are often unique one-time investments between various local or national actors, global CSOs lack the local knowledge and connections to effectively impact the trajectory of the PPP. They also are less likely to have intimate on-the-ground knowledge of the project and relevant local actors. Instead, global CSOs should assist local CSOs. At project initiation, local CSOs can ensure that projects are selected based on social benefit rather than private interests. During implementation, local CSOs could monitor the private actor and ensure it adheres to the predetermined environmental and labour regulations. After completion, local CSOs can ensure that private actors are upholding the contract, serving as a long-term watchdog on behalf of the people. Critical to this strategy is the transfer of knowledge and resources from international CSOs, which possess the financial ability and broader understanding of how PPPs have been implemented elsewhere.

4. Enhance public sector capacity: The leveraging of the advantages of the public and the private sectors assumes that both parties have roughly equal capacity in negotiation, operational experience, and technical knowledge. Under these conditions, PPPs can achieve their intended goal of matching public objectives and financing with private operational efficiency and knowledge. However, capacity parity is rare in practice. Often the private sector is privy to knowledge that the government lacks, or has better teams of negotiators and lawyers to draft contracts that favor the private sector. This can allow the private actor to receive preferential agreements that aid private interests rather than the public good. The academic literature on PPPs has consistently cited the lack of government capacity as a major hindrance to successful implementation of PPPs.

In order to balance the scales, CSOs could provide assistance to developing the capacity of the public sector, particularly in countries that lack strong bureaucracies. Private actors, when backed by the government, have an incentive to leverage more than they would otherwise because creditors know they are at least partly protected from losses. In order to reduce this risk, limits can be placed on the debt-to-

equity ratios of PPPs. Since CSOs often have intimate knowledge of projects around the globe, sharing this information with the public sector could help them make informed decisions on the successes and failures of PPPs, or, more fundamentally, whether a given PPP project is even beneficial. The knowledge-sharing also reduces the burden of the government.

More technically, CSOs could provide legal assistance in negotiation and contract writing. As mentioned earlier, governments frequently lack the legal expertise to develop contracts that mitigate contingent liabilities for the public sector and ensure that PPPs over the long run continue to prioritize socially-beneficial objectives. Given the relative infrequency and uniqueness of PPP projects, governments are unlikely to develop in-house departments, though a few countries have. The World Bank has created a database of PPP programs, though CSOs could verify the findings and provide their own parallel analysis for distribution to country governments, particularly given the nontransparent nature of governments to openly provide this information.

5. Create standards that are harmonized and include non-financial measurements: Over the years, there have been many efforts to harmonize the implementation and evaluation of PPPs. In 2003, for instance, the European Commission issued guidelines for PPP project selection and administration based upon the EU's own experience with public-private partnerships (European Commission 2003). The advantage of a harmonized system is well-documented; in addition to improved development outcomes, a standardized protocol also engenders comparability in PPPs across time, space, and sector. Nevertheless, while there are guidelines for PPPs, a fully standardized system has thus far remained elusive because of the highly decentralized nature of PPPs. For instance, while the World Bank has published a set of guidelines that recommends best practices for PPP implementation, governments and private actors are under no obligation to follow them, especially when the World Bank plays only a coordinating role. More problematically, there are no guidelines as to how PPPs should be managed in the long-term. For instance, there are no internationally agreed upon reporting requirements, no common assessment protocols, and no social impact measures.

CSOs can help mitigate these problems by further encouraging the harmonization of these practices. For one,

CSOs can lobby the Group of 20, development banks and the United Nations to create a common set of standardized guidelines for PPP appraisal, monitoring, and assessment. Recent work relating to the 2015 Addis Ababa Action Agenda shows encouraging signs for greater harmonization of PPP management, and currently there is work being done to draft guidelines (UN 2016). This provides a good opportunity for CSOs to have their concerns heard and, more importantly, allow CSOs to shape the future of PPP guidelines. Of particular importance is creating an international standard to force better disclosure on the operations of PPPs and prevent the ability of private actors to opaquely obtain public funds.

Finally, CSOs should also argue for the inclusion of non-financial measurements in guidelines for PPP appraisal, monitoring, and assessment. Oftentimes assessments of PPPs only account for financial aspects of projects while ignoring the broader social impact. This can incentivize PPPs to focus on measures of profitability or return on investment, outcomes that are particularly favorable to the interests of private enterprise. Therefore, CSOs should provide guidance on how to incorporate non-financial aspects like environmental or social concerns into the guidelines and assessment standards for PPPs (c.f. Aizawa 2016). Including these measures would not only create a broader and more inclusive conceptualization of PPPs, but it would also help ensure that PPP projects are not captured by private interests and instead work for the greater public good.

In conclusion, PPPs may offer the international development community a potentially powerful mechanism to catalyze private investment in the provision of public services. It is likely that given the enormous need for financing, PPPs are almost certainly going to be an important tool for development. Development banks have taken a particularly active role in this promotion, and have reiterated their support for finding innovative ways to extend PPPs to different sectors. As noted throughout this report, while PPPs at least theoretically have benefits, in practice they have been beset with a host of problems. CSOs should be aware of these problems, and actively engage to help the public decide whether or not a particular PPP project is ultimately likely to be beneficial. In doing so, CSOs can ensure that PPPs leverage the private sector for the greater good.

Abbreviations

| | |
|--------|---|
| AAAA | Addis Ababa Action Agenda |
| ADB | Asian Development Bank |
| BIT | Bilateral Investment Treaty |
| BOOT | Build-Own-Operate-Transfer |
| CSO | Civil Society Organization |
| DC | Developing Country |
| EBRD | European Bank for Reconstruction and Development |
| EIB | European Investment Bank |
| EME | Emerging Market Economy |
| FDI | Foreign Direct Investment |
| FTA | Free Trade Agreement |
| IDA | International Development Assistance |
| IDB | Inter-American Development Bank |
| IFC | International Finance Corporation |
| IMF | International Monetary Fund |
| GDP | Gross Domestic Product |
| KfW | Kreditanstalt für Wiederaufbau |
| MIGA | Multilateral Investment Guarantee Agency |
| NGO | Non-Governmental Organization |
| OECD | Organization for Economic Cooperation and Development |
| PFI | Private Finance Initiative |
| PPIAF | Public-Private Infrastructure Advisory Facility |
| PPP | Public-Private Partnership |
| PPPIRC | PPP Infrastructure Resource Center |
| SDGs | Sustainable Development Goals |
| SME | Small- and Medium-Sized Enterprise |
| UN | United Nations |
| WB | World Bank |

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Annex

World Bank Chart on International Debt Statistics

All low- and middle-income countries (US\$ billion, unless otherwise indicated)

| | 2000 | 2005 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 |
|-----------------------------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
| Summary external debt data | | | | | | | | |
| External debt stocks | 2,091.2 | 2,532.3 | 4,023.8 | 5,298.6 | 5,871.8 | 6,638.1 | 7,071.2 | 6,669.4 |
| Long-term external debt | 1,732.9 | 1,972.4 | 3,132.9 | 3,573.9 | 4,005.2 | 4,437.5 | 4,753.8 | 4,750.0 |
| Public and publicly guaranteed | 1,271.2 | 1,295.5 | 1,673.5 | 1,798.8 | 2,024.8 | 2,237.0 | 2,382.2 | 2,419.9 |
| Official creditors | 748.5 | 711.6 | 826.8 | 858.2 | 876.6 | 901.5 | 908.8 | 910.7 |
| of which: IMF | 78.4 | 69.4 | 154.5 | 154.4 | 146.1 | 128.4 | 113.8 | 113.7 |
| Private creditors | 522.7 | 583.9 | 846.8 | 940.6 | 1,148.2 | 1,335.5 | 1,473.5 | 1,509.2 |
| of which: Bonds | 331.2 | 414.9 | 558.5 | 617.8 | 787.9 | 862.9 | 975.4 | 1,028.2 |
| Private nonguaranteed | 461.7 | 676.9 | 1,459.4 | 1,775.1 | 1,980.4 | 2,200.6 | 2,371.6 | 2,330.1 |
| of which: Bonds | 97.5 | 140.5 | 236.5 | 280.1 | 323.5 | 390.3 | 449.9 | 463.3 |
| Short-term external debt | 280.0 | 490.6 | 736.4 | 1,570.3 | 1,720.5 | 2,072.2 | 2,203.6 | 1,805.6 |
| interest arrears on long-term | 31.8 | 28.7 | 21.0 | 18.0 | 20.3 | 19.4 | 20.4 | 20.9 |
| Long-term external debt | | | | | | | | |
| Disbursements | 222.4 | 366.6 | 642.2 | 770.4 | 852.3 | 929.0 | 969.0 | 803.1 |
| Public and publicly guaranteed | 136.0 | 148.9 | 293.3 | 262.1 | 318.0 | 370.8 | 379.8 | 314.9 |
| Official creditors | 52.3 | 45.7 | 111.0 | 92.6 | 91.4 | 108.3 | 108.6 | 102.2 |
| Private creditors | 83.7 | 103.2 | 182.3 | 169.5 | 226.6 | 262.6 | 271.2 | 212.7 |
| of which: Bonds | 54.8 | 67.6 | 102.9 | 105.1 | 167.0 | 125.2 | 184.7 | 138.0 |
| Private nonguaranteed | 86.3 | 217.7 | 348.9 | 508.3 | 534.3 | 558.2 | 589.2 | 488.3 |
| of which: Bonds | 12.2 | 41.3 | 56.7 | 100.8 | 105.6 | 131.5 | 114.8 | 102.6 |
| Principal repayments | 197.4 | 272.5 | 382.2 | 400.0 | 406.7 | 478.6 | 549.9 | 593.9 |
| Public and publicly guaranteed | 103.2 | 143.5 | 137.7 | 141.7 | 111.9 | 146.5 | 169.5 | 227.8 |
| Official creditors | 46.9 | 69.3 | 51.3 | 60.5 | 53.7 | 62.7 | 56.2 | 69.2 |
| Private creditors | 56.3 | 74.2 | 86.5 | 81.2 | 58.2 | 83.8 | 113.2 | 158.6 |
| of which: Bonds | 22.0 | 44.0 | 36.8 | 36.4 | 19.0 | 40.8 | 55.8 | 65.7 |
| Private nonguaranteed | 94.2 | 129.0 | 244.5 | 258.3 | 294.8 | 332.2 | 380.4 | 366.1 |
| of which: Bonds | 16.3 | 17.1 | 17.8 | 18.0 | 33.6 | 36.0 | 47.3 | 61.4 |
| Interest payments | 92.0 | 81.9 | 106.4 | 124.1 | 151.7 | 142.1 | 154.2 | 159.6 |
| Public and publicly guaranteed | 63.2 | 60.3 | 51.0 | 56.3 | 81.1 | 65.4 | 71.2 | 78.4 |
| Official creditors | 25.7 | 23.7 | 15.5 | 16.3 | 17.6 | 17.0 | 17.0 | 17.0 |
| Private creditors | 37.5 | 36.6 | 35.5 | 40.0 | 63.4 | 48.4 | 54.2 | 61.4 |
| of which: Bonds | 25.4 | 30.3 | 30.2 | 34.6 | 57.5 | 42.2 | 46.5 | 52.7 |
| Private nonguaranteed | 28.8 | 21.6 | 55.4 | 67.8 | 70.6 | 76.7 | 83.0 | 81.2 |
| of which: Bonds | 8.0 | 8.1 | 12.7 | 18.3 | 16.2 | 21.7 | 24.3 | 25.2 |
| Net financial flows | | | | | | | | |
| Net inflows | 150.5 | 466.6 | 852.1 | 1,815.9 | 1,223.5 | 1,441.3 | 1,159.3 | 379.3 |
| Net debt inflows | 5.2 | 137.5 | 195.0 | 1,207.8 | 585.1 | 785.2 | 542.3 | -184.5 |
| Official creditors | -5.0 | -63.6 | 73.2 | 32.6 | 29.2 | 27.8 | 45.2 | 37.7 |
| of which: World Bank | 8.0 | 2.9 | 22.4 | 6.5 | 12.1 | 14.1 | 16.9 | 19.3 |
| of which: IMF | -10.5 | -40.0 | 13.4 | 0.5 | -8.4 | -17.7 | -7.2 | 4.8 |
| Private creditors | 10.2 | 201.1 | 121.8 | 1,175.2 | 555.8 | 757.3 | 497.1 | -222.2 |
| Long-term | 19.6 | 117.7 | 200.2 | 338.3 | 407.9 | 404.8 | 366.7 | 176.2 |
| Bonds | 28.7 | 47.9 | 105.0 | 151.4 | 220.1 | 179.9 | 196.5 | 113.6 |
| Banks and other private | -9.1 | 69.8 | 95.2 | 186.8 | 187.8 | 224.9 | 170.2 | 62.7 |
| Short-term | -9.3 | 83.4 | -78.4 | 836.9 | 147.9 | 352.5 | 130.4 | -398.4 |
| Net equity inflows | 145.3 | 329.1 | 657.0 | 608.1 | 638.4 | 656.1 | 616.9 | 563.8 |
| Foreign direct investment | 131.1 | 263.0 | 538.8 | 616.2 | 549.4 | 590.8 | 536.1 | 543.0 |
| Portfolio equity | 14.3 | 66.1 | 118.2 | -8.1 | 89.0 | 65.3 | 80.8 | 20.8 |

Source: World Bank 2017c

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