Designing the African Development Bank’s PPP Framework

Whitepaper for Discussion
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Abbreviations

ADB : Asian Development Bank
ADP : African Development Fund
AFDB : African Development Bank
AIIB : Asian Infrastructure Investment Bank
ALSF : African Legal Support Facility
BIFL : Bangladesh Infrastructure Finance Fund Limited
BPC : Bank Country Procurement Assessment
CIS : Commonwealth of Independent States
CPIA : Country Policy and Institutional Assessment
CRD : Country Readiness Diagnostic
EBRD : European Bank for Reconstruction and Development
EIB : European Investment Bank
FAPA : Fund for African Private Sector Assistance
GDP : Gross Domestic Product
IADB : Inter-American Development Bank
ICA : Infrastructure Consortium for Africa
ICT : Information and Communication Technology
IDEV : Independent Development Evaluation Department (of AFDB)
IFC : International Finance Corporation
IIIFCL : India Infrastructure Finance Company Limited
IPP : Independent Power Producer
IPPF : Infrastructure Project Preparation Facility
MIC : Middle Income Countries
NEPAD : New Partnership for Africa’s Development
OPPP : Office of PPP
PEVP : Vice Presidency for Power, Energy, Climate and Green Growth
PPF : Project Preparation Facility
PPI : Private Participation in Infrastructure
PPP : Public-Private Partnership
RMC : Regional Member Country
SEFA : Sustainable Energy Fund for Africa
SMI : PT Sarana Multi Infrastruktur
SPV : Special Purpose Vehicle
TAF : Technical Assistance Facility
UNCITRAL : United Nations Commission on International Trade Law
USD : United States Dollar
WBG : World Bank Group
Context

Critical need for investments in infrastructure...

The infrastructure gap in African countries, especially in transport, electricity, and water supply acts as an impediment to their economic growth and development. The gaps impact not only the economic situation of the citizens of Africa, but also its global competitiveness. It is estimated that poor infrastructure shaves off 2% of the per capita GDP growth rates.

The African Development Bank ("AFDB" or "the Bank") estimates that African countries need to invest USD 130-170 billion by 2025 to meet their present and future infrastructure requirements. The Bank estimates that there will be gap of USD 68-108 Billion in financing of the investment requirement, based on the total amount of financing commitments made by all donors to absorb the infrastructure deficit.

National governments are the main source of financing for investments in infrastructure but are subject to national fiscal and economic constraints. The total investment in infrastructure in 2018, according to ICA, was around USD 100.8 Billion, but still fell short of the USD 130-170 Billion investment need estimated by the Bank. Investment from private sources has been increasing in the last five years, from USD 2.9 Billion in 2014 to USD 11.8 Billion in 2018, but still falls far below the levels required to bridge the infrastructure investment gap.

…and improvement in public service delivery.

Complicating the challenge of financing the infrastructure gap is the inefficiencies in operations of the infrastructure that already exists. Africa’s power and water utilities present very high inefficiencies in distribution losses, under-collection of revenues, and overstaffing. In addition, it is estimated that on an average about 30% of the infrastructure assets of a typical African country needs rehabilitation and upgradation, because of decades of inefficient and underfunded maintenance. The inefficiencies paradoxically lead to both higher tariffs for services and at the same under-recovery of cost of providing services. The gains from resolving these inefficiencies, though costly, would contribute positively to bridging the infrastructure gap.

Public-Private Partnerships can be a viable alternative...

Public-Private Partnerships (PPPs) offer a solution to both the challenges impeding development and upgradation of infrastructure in Africa – increased investments, and increased efficiencies. PPPs leverage private sources of finance for delivery of public assets and services, while providing opportunities to optimize the quality of such services. PPPs deliver value for money for governments by leveraging private innovation to provide public services more efficiently. PPPs deliver value by ensuring competitive discovery of prices, providing opportunities to optimize lifecycle costs, and allocating the responsibilities and risks to the party best positioned to manage them.

PPPs can be an alternative source of finance for infrastructure investments in African countries, while potentially also delivering higher quality and efficiency in public assets and services.

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1 Source: African Economic Outlook 2018, AFDB Group
2 Ibid.
3 Source: Africa’s Infrastructure: A Time for Transformation, ICA 2015
...but are African countries ready?

African countries realize the value of PPPs, both as an alternate source of finance and as an approach for more efficient provision of higher quality public assets and services. The growing interest is evidenced by the fact that several countries have already laid the enabling frameworks for PPPs in the form of PPP legislations or regulations and PPP units. Based on the African Legal Support Facility (ALSF) PPP Country Profiles, 33 out of 54 African countries have already put in place a PPP Law or Policy and a PPP Unit, with a further six countries putting in place a PPP Law or Policy only.

However, the actual deal flow has been fairly limited so far. In terms of value, PPP projects in Sub-Saharan Africa were only about 5% of the total PPP investment globally during the period 1999 to 2019. The PPP market in Africa is also a concentration of deals in a handful of countries. Five countries – South Africa, Morocco, Nigeria, Egypt, and Ghana – account for a little more than 50% of all PPPs in Africa by value.

The energy sector accounts for 57% of PPPs by value, followed by the transport and ICT sectors accounting for 24% and 16% respectively during 1999 to 2019. Sectors, including water, sewerage, and solid waste management, account for less than 5% of the total value of PPPs during this period.

What are the challenges impeding PPPs in Africa?

The biggest challenge in increasing the level of PPP investments in Africa is the inadequate capacity of the countries in identifying, developing, structuring, and bringing bankable PPPs to the market. Typically, governments in countries with nascent PPP markets have no experience in managing the transaction stage of PPPs. The experience of such governments is typically in structuring and managing public funded infrastructure facilities and services. But structuring and procurement of PPPs is very different from that of traditional government contracts. PPP transactions require specific skills to be available to the government sponsor, in the areas of finance, contracts, engineering and design, environmental and social impacts, and procurement.

Many countries have attempted to put in place the legal, regulatory and implementation frameworks, but in the absence of experiences and required skills, such frameworks have not been able to translate into actual transactions.

The complexity of PPP transactions requires government sponsors to depend on qualified and experienced PPP advisors, even in advanced PPP markets. This need is even more critical in countries with nascent PPP markets as the government sponsors do not have the required experience and internal capacity. For such countries, contracting external transaction advisors is often difficult as there are usually no experienced advisors available in the domestic market or the government sponsor does not have resources to contract the services of an advisor. In many cases, the government does not even have the ability to procure and manage transaction advisors, mainly due to the lack of experience of using such services.

PPPs do not mean that the requirement of public finance will be completely replaced by private finance. Private financing of infrastructure is usually more expensive than the cost of finance for governments. In addition, private investors and Banks may not have the capacity and/or the willingness to completely finance the capital investment for public infrastructure, especially in nascent or emerging PPP markets. Globally, governments have had to contribute to the financing of infrastructure projects implemented through PPPs, across emerging and developed PPP markets. The public contribution comes in various forms, including

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4 Source: Private Participation in Infrastructure Database, World Bank Group (HYPERLINK: https://ppi.worldbank.org/)
5 PPI Database, World Bank Group (2019)
6 Ibid.
construction grants, viability gap grants, availability payments, equity investments, concessional loans, and operational subsidy etc.

The limited financial capacity of the RMC governments to contribute to the financing requirements in PPPs, especially in the Low-Income Countries (LICs) may represent a challenge in getting PPPs to the market. In addition, the levels of poverty in many RMCs may represent a challenge in funding the PPPs through user charges and other sources of revenues that depend on payments by direct or indirect users.

AFDB’s current role

Bank’s mandate

The priorities for the AFDB group are articulated in the form of the High 5 – (1) Light Up and Power Africa (2) Feed Africa (3) Industrialize Africa (4) Integrate Africa and (5) Improve the Quality of Life for the People of Africa. Most of these priority areas emphasize creating of infrastructure across the sectors of energy, transport, water, sanitation, and agriculture.

The Bank intends to scale up infrastructure financing to the continent significantly – not just through its own lending but also by leveraging its financial resources. The AFDB Strategy for 2013-2022 emphasizes that the Bank will be an increasingly active partner and facilitator for private investment in Africa.

Addressing these gaps in RMCs presents a long-term opportunity for the Bank to enhance the development effectiveness of its overall role in Africa. As described in the preceding chapter, PPPs not only help resolve the gap in infrastructure investments but also enhance the quality and efficiency of infrastructure services by leveraging private finance, efficiency, and innovation. Thus, the same amount of financing by the Bank potentially can deliver additional value to the RMC if it is routed through PPP arrangements as compared to being routed through conventional sovereign financing and delivery of infrastructure.

Bank support across the upstream, midstream, and downstream stages of PPP transactions can help develop the domestic PPP markets in many ways:

- Demonstrating efficiencies and value for money generated through PPPs, based on successful transactions;
- Enhancing the capacity of the RMC governments to implement PPPs;
- Catalyzing the development of domestic markets for PPP investors by ensuring a pipeline of commercially attractive PPP opportunities; and
- Catalyzing the evolution of domestic financial markets and institutions to respond to the requirements of PPPs through their participation as co-financiers to the Bank, and through demonstration of successful PPP transactions

As a development bank, AFDB is mandated to not only provide financing instruments, but also to strengthen the legal, regulatory, and institutional frameworks in RMCs. Strengthening PPP enabling frameworks not only creates the groundwork for enhancing PPP investments in the RMC, but also enhances their ability to manage infrastructure development in general. For instance, the strengthening of procurement regulations for PPP gives the knowledge and experience to an he RMC to strengthen the overall public procurement ecosystem.

Existing portfolio of the Bank

PPPs have not been subject of a Bank-wide overarching strategy but have been addressed widely in the context of corporate and sectorial strategies as well as Country Strategy Papers (CSPs). PPP is considered as a cross cutting issue in most, if not all policies and strategies of the Bank.
The Bank does not have any official classification for PPP projects. Hence it is difficult to identify upstream and downstream operations supporting PPP frameworks or individual PPP transactions in the Bank’s portfolio. As part of the Evaluation of Bank’s Utilization of PPP Mechanism, IDEV identified 65 PPP-related operations during 2006-2017 in 29 RMCs, representing a total net commitment of approximately UA 2.7 billion. These operations covering all regions of the continent, consist of lending (Guarantees, Project loans, Institutional Support loans, Structural Adjustment loans) and non-lending activities (Grants, Economic and Sector Works, and Technical Assistance).

The Bank’s upstream support to RMCs in the context of PPPs consisted of 24 lending and non-lending operations, representing a total net commitment of UA 665 million. In this respect, the Bank deployed instruments such as structural adjustment and institutional support programs with PPP components to prepare enabling policy and regulatory environments for PPPs in RMCs.

The Bank’s downstream financing involved 41 PPP transactions with financing (debt and equity participation) representing a total net commitment of approximately UA 2 billion. This support went mainly to the power and transport sectors, which respectively contributed 64% and 30% of the total value of the Bank’s downstream support to PPPs. The Bank also financed guarantees in 13 of these 41 downstream transactions, for a total amount of UA 140 Million.

**Unique value proposition of the Bank**

The competitive strength of the Bank derives from its deep knowledge of the African context. This knowledge comes from its experience of undertaking more than 4,707 operations to date, in almost every African country. This knowledge also comes from its physical presence of the Bank in more than 40 countries in Africa.

The Bank has largely concentrated on supporting PPPs in electricity generation (both conventional and renewables) and road sector till now, with close to 75% of the PPP experience of Bank concentrated in these two sectors. At the same time, the Bank has experience of almost every other infrastructure sector such as water supply, environment, health, and urban development in its ‘non-PPP’ portfolio. The vast experience of the Bank in these sectors in Africa gives it a potential competitive strength as compared to other development Banks.

The Bank has an in-depth understanding of the African context, not only because of its extensive operations undertaken since 1976, but also due to its initiatives like the Country Policy and Institutional Assessment (CPIA), Bank Country Procurement Assessment (BPCA) and review of country prospects and portfolios as part of the Country Strategy Papers (CSPs). In fact, the IDEV Evaluation of the use of PPP Mechanism by the Bank 2006-2017 quotes RMC governments and private project sponsors explicitly recognizing the Bank’s knowledge of the African context as its key strength.

While the PPP experience of the Bank has been limited, it has still participated in some of the largest and successful PPPs in the continent, including the Dakar Diamniado Toll Highway (Senegal), Lake Turkana Wind Power Project (Kenya), Ouarzate NOORo I and II Solar Power Projects (Morocco) and Ithezi-thezi Hydropower Project. Bank’s experience in such and other projects gives it an insight into the key risks and success factors for implementation of large and complicated PPP deals in Africa.

**Lessons from the IDEV evaluation of the Bank’s use of PPP mechanisms (2006-2017)**

IDEV undertook an independent development evaluation of the Bank’s use of PPP mechanisms in 2019. This evaluation assessed the extent to which the Bank’s PPP interventions achieved targeted development results and were well managed by the Bank. The evaluation attempted to identify factors that enable and/ or hinder successful implementation and achievement of development results and to harvest lessons from experience.
to inform the Bank’s use of its PPP mechanism. The key findings from the evaluation are summarized in the following paragraphs.

1. **Bank’s strategy for PPPs**: The Bank has neither an overarching and formal strategy, nor operational guidelines and directives for PPPs. It has generally addressed PPPs within its corporate and sectoral strategies, and country strategy papers (CSPs), which consider PPPs mostly as a cross-cutting issue.

2. **Bank’s internal mechanisms for PPPs**: The Bank has no formal coordination mechanisms directed toward PPPs, facilitating concerted efforts across its departments, nor a central PPP unit. Instead, it has a decentralized matrix approach. This means that several units within the Bank handle PPP activities, with occasional overlaps, and without the necessary coordination.

3. **Development impact of PPPs**: The Bank’s PPP interventions are largely relevant and effective, with the benefits likely to be sustained. However, both financial and non-financial additionality of the Bank is limited, mainly because of the late stage of the Bank’s involvement, typically after the structuring and procurement stages.

4. **Transformative impact**: The Bank has been involved in some of the most transformative and pioneering PPP projects in the region. The Bank’s downstream interventions established some of the first successful demonstrations of PPP models in some sectors and RMCs.

5. **Achievement of outcomes**: Most of the downstream interventions (88 percent of the sample interventions) achieved their targeted outcomes and impact satisfactorily. As the Bank’s PPP interventions were targeted toward large economic infrastructure projects, they improved access to infrastructure facilities and services, and indirectly access to social services.

**The PPP Framework**

**Need for a strategic framework**

The Bank has been providing support to its RMCs in the development and implementation of PPPs for several years and continues to do so. This support is in the absence of a Bank-wide strategic framework and approach for PPPs. To address development challenges in infrastructure and other important social sectors, the Bank seeks to upscale its support and financing for PPP investment by its RMCs.

As the IDEV PPP evaluation concluded, most of the elements that are needed for a strategic Bank-wide programme for supporting PPP development in RMCs are already present in the organisation.

In the absence of a strategic framework, the use of these elements has been transactional and on an individual basis, without being coordinated or synchronized with other elements. A concise, specific, and clear framework and guidelines for PPPs would therefore lead to

- Integrated support to RMCs, combining individual offerings of the Bank based on needs of individual RMCs;
- Better leveraging of the Bank’s offerings;
- Consistent and standardized offerings; and
- Clear communication of offerings to RMCs and development partners.

**Purpose of the PPP Framework**

The Bank’s PPP Framework intends to promote a common understanding on PPPs, within and outside the Bank and to articulate the Bank’s role and priorities for supporting PPPs in RMCs. The purpose of the PPP Framework is to define the Bank’s strategic priorities in supporting PPPs and PPP markets in Africa, and at the
same time specify the support that it can provide to RMCs to develop their PPP markets. This PPP Framework complements other long-term policies and strategies of the Bank.

The PPP Framework is required due to the increasing requests made to the Bank by RMCs to support PPPs, and the Bank’s intentions to play a leading role in supporting development of infrastructure through PPPs as an alternative to publicly financed, operated and maintained infrastructure.

Consequently, the PPP Framework is directed towards the objective of mobilizing private finance, innovation, management capacity and efficiency for resolving infrastructure gaps in African countries. The Framework seeks to fulfill this objective by

• Providing a clear strategic direction to the Bank’s support to PPPs in RMCs;
• Integrating all operations and activities within the Bank supporting PPPs in RMCs;
• Optimally organizing the resources within the Bank for supporting PPPs in RMCs; and
• Clearly communicating the different forms of support that Bank can provide to support PPPs in RMCs.

Underlying principles of the PPP Framework

The PPP Framework is being developed based on underlying, general principles that share the Bank’s strategic priorities in supporting PPP development in the RMCs. These principles include the following:

• The Bank will consider the option of PPP implementation in every infrastructure project that is being considered or evaluated for Bank operations. Only if the project in its entirety is not appropriate for PPPs, in its original form or with modifications that do not alter the outcome of the project, the Bank will consider other alternative implementation mechanisms.

• Notwithstanding the above principle, the Bank will promote the use of PPPs in only those infrastructure projects where PPPs are most appropriate.

• The Bank will focus on delivery of infrastructure and public services as the ultimate outcome of its support to RMCs. The Bank will support the strengthening of PPP enabling frameworks, and capacity of RMCs to develop PPPs as the means to achieve the end result of implemented PPP deals.

• The Bank will endeavor to make systemic impacts in RMCs, through its support on PPPs, even when the support is for individual projects. Systemic impact refers to long term, sustainable improvements in the PPP enabling framework, capacity of the RMC government to develop PPPs in the future, strengthening of the project financing market, strengthening of the private sector, promotion of sovereign and sub-sovereign PPPs, and promotion of national community of PPP advisors and experts.

• The Bank will offer support to RMCs across the complete PPP lifecycle. Ideally, the Bank will endeavor to support every individual PPP to the end of its lifecycle, irrespective of where the Bank’s involvement begins.

• The Bank will take a leadership role, among other lenders and development partners in PPP projects in Africa that it is supporting, subject to applicable Bank policies and regulations.

• The Bank will promote the participation of African businesses and investors in PPPs, as much as possible, where it does not affect the quality of implementation or delivery of PPPs.

• The Bank will endeavor to create a community of PPP experts and practitioners in Africa by promoting the involvement of African experts and advisors as much as possible, disseminating PPP knowledge and experience widely and developing platforms for exchange and sharing of PPP knowledge.
Pillars of PPP Framework

The Bank intends to support PPP development in RMCs through the following three strategic pillars:

<table>
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<tr>
<th>Pillar 1: Strengthening PPP enabling environment</th>
<th>Pillar 2: Project preparation and transaction advisory</th>
<th>Pillar 3: Financing of PPP projects</th>
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<tr>
<td>Support RMCs to develop PPP laws, policies, and regulations, establish PPP institutions, and strengthen public sector capacity to identify, develop and implement PPPs</td>
<td>Support RMCs to prepare, develop, structure, and procure individual PPP projects</td>
<td>Support financing of PPP projects through debt, equity, and risk mitigation instruments, and both sovereign and non-sovereign operations</td>
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These strategic pillars of Bank support are explained in the following sections of this document.

Pillar 1: Strengthening PPP enabling environment

Need for strengthening PPP enabling environments

According to Procuring Infrastructure PPPs 2018, 68% of countries in Sub-Saharan Africa have standalone PPP laws, which is comparable to the global average. Based on the information available on Private Participation in Infrastructure (PPI) Database and the PPP Knowledge Lab, 33 African countries have a PPP Law or Policy and a PPP unit in place. However, having a PPP law and/or PPP unit does not translate into a healthy PPP deal flow. There are 14 African countries with both a PPP Law and Unit that have fewer than five PPP projects recorded in the PPI database.

This indicates a wider need in these markets beyond the PPP law/policy and units. The RMCs need support in operationalising frameworks for infrastructure planning, budgeting, contracting and project management. In parallel, the regulatory frameworks governing private investment, project finance and access to financial markets are also required.

In addition, some sectors require sector wide reform before PPPs could be implemented. Examples are power sector and water supply sector which require unbundling and corporatisation before opportunities for private investment can be identified, structured, and procured.

It is evident that the RMCs need support beyond PPP laws and setting up of PPP units. The challenge is in identification of the specific areas or enablers where they need support of the Bank, as each RMCs presents a unique set of needs. This challenge would influence the entry point and design of the Bank operations.

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8 Source: Procuring Infrastructure Public-Private Partnerships 2018, World Bank Group
10 [www.pppknowledgelab.org](http://www.pppknowledgelab.org), The World Bank Group
Current approach of the Bank

As there is no official ‘PPP category’ of Bank operations, including upstream operations that make it difficult to identify the Bank portfolio. In addition, many large programs in areas such as strengthening public finance frameworks or procurement systems have PPP components, but these are difficult to isolate.

Bank operations for support to PPP frameworks have largely focussed on promulgation of PPP policies and laws and setting up of PPP units. In a few RMCs, the Bank has started to support the operationalising of PPP units, through development of guidelines and strengthening capacities of the units. The Bank has recently started to integrate project identification as part of ISPs and PBOs. However, there is still a need for integrating such support with downstream operations of the Bank, including project preparation support, and eventually financing of PPPs. For instance, while the Bank identifies potential lending operations and lists potential ISPs and PBOs as part of individual country strategies, there is limited integration between the two lists. PBOs and ISPs can be targeted towards strengthening the framework and make the country (or sector) ready to implement a project, that can be financed by the Bank.

The operations of the Bank in each country are designed based on the requirements of that country. However, there is no standardised diagnosis tool / approach of the Bank that can help identify the key gaps in the PPP enabling framework in a country as a basis for the design of operations. While designing such operations, the focus also needs to shift to the end outcome of development of PPP markets and catalysing deal flow, rather than developing a comprehensive PPP framework as an outcome in itself.

Lessons from peer institutions

- Most peer MDBs provide support for the development of legal, regulatory, and institutional frameworks for PPPs. The exception is AIIB which has taken a deliberate decision to focus on financing projects only, at the present stage of its operations.
- WBG and IADB have encountered challenges of inadequate coordination and integrations across upstream, midstream, and downstream operations supporting PPPs in their member countries. This is like the situation of the Bank at present.

The WBG resolved this challenge by institutionalising standard approaches – like the Country Readiness Diagnostic for PPPs (CRD for PPPs) tool which identifies the bottlenecks for PPPs across the complete value chain of development in a member country and forms the basis for coordinated support across the Bank. The WBG also created institutions and mechanisms specifically for supporting PPPs at different stages of development.

- The EBRD and WBG have standardised frameworks for diagnostic assessment of country level PPP environments. The EBRD has a focussed exercise every five years to assess the strength of country level PPP policy, legal, regulatory, and institutional frameworks in all member countries. WBG and ADB have integrated the review of PPP frameworks and markets in their country strategy processes, forcing the country offices to identify the support that may be needed by the RMCs for implementing PPP programs. The review and diagnostics form the basis for the design of their upstream operations.

Strategy for Pillar 1 Support to RMCs

The Bank will support the establishment of PPP legal, regulatory, and institutional frameworks in RMCs, with a focus on creating conditions favourable for catalysing identification, development, and implementation of PPP projects in the RMC. The focus would be on development of implementing regulations, detailing of government mechanisms for approvals, financial support, and PPP procurement, and establishing contract management systems and processes. Some of the specific strategies that the Bank is considering include the following:
• The Bank intends to develop a standardised diagnostic tool, integrated with the process for individual country strategies. The findings from the diagnostic will form the basis for identification of possible ISPs and PBOs.

• The Bank intends to focus specifically on those gaps and challenges that are impeding PPP projects. The Bank will consciously avoid strengthening PPP frameworks as an end in itself.

• The Bank will integrate project identification and early stage project screening within its Pillar 1 operations as much as possible.

At the same time, the Bank will support strengthening of public sector and private sector capacities to undertake PPPs in the RMCs. This capacity building support will be focused on operationalization of regulatory frameworks, project identification, feasibility assessment, approvals, procurement, management of fiscal impacts, and contract management.

The Bank will specifically focus on strengthening of institutional capacities to identify potential PPP projects. This support might involve the Bank directly guiding the RMCs to screen projects already identified by the RMCs and sub-sovereign government entities. The Bank will endeavour to integrate project identification and/or preliminary screening of potential PPPs in most Pillar 1 operations.

Finally, the Bank will endeavour to research, analyse and disseminate information on PPPs to increase the awareness and understanding of PPPs, including in the areas of best practices in PPP implementation, innovative PPP models, guidance on key decisions and toolkits for use in project implementation.

The Bank will collaborate with institutions which are already active in assessment of PPP enabling frameworks in Africa and globally, for example Africa Legal Support Facility (Country PPP Snapshots), WBG (Procuring PPPs Report) and Global Infrastructure (Infra Compass) to develop the standard methodology for the diagnostic assessment, and identification of areas for support. The Bank will collaborate with peer institutions to coordinate areas of support, with the intention of complementing respective programs and avoiding overlaps. The Bank will also leverage on existing capacity building methodologies, like the APMG PPP certification for strengthening capacities in individual RMCs.

Pillar 2: Project preparation and transaction advisory

Need for support for project preparation and transaction advisory

PPPs are complex arrangements and involve long term contractual commitments by the government. PPP projects require substantial due diligence and preparatory work from the government sponsor, before the project can be structured and an appropriate procurement followed, leading to the selection of the private sector partner.

To undertake project preparation activities, the government sponsor must have access to inhouse or external PPP expertise in areas such as engineering, technology, finance, industry, and contracts. The government must have the necessary budget to pay for the deployed internal human resources or the external expertise (through hired experts and consultants). At key stages of project preparation, the government must also make go/ no-go decisions, based on informed understanding of the project feasibility and risks.

Governments undertaking PPP projects ideally need to set up a dedicated project and transaction management team for individual projects, covering these areas of expertise, either through their own staff or by hiring transaction advisors and consultants. Large and complicated PPP transactions require larger and exclusively deployed teams, while smaller projects may be managed by a smaller team, or as part of a portfolio being managed by a single team.
The complexity of PPP transactions requires government sponsors to depend on qualified and experienced PPP advisors, even in advanced PPP markets. This need is even more critical in countries with nascent PPP markets as the government sponsors do not have the required experience and internal capacity. For such countries, contracting external transaction advisors is often difficult as there are usually no experienced advisors available in the domestic market or the government sponsor does not have resources to contract the services of an advisor. In many cases, the government does not even have the ability to procure and manage transaction advisors, mainly due to the lack of experience of using such services.

External support, through MDBs, has shown to be effective in developing countries. The external technical assistance in handholding project preparation, arranging for consultants and advisors, developing and guiding the use of decision and approval protocols is effective not only for the preparation of the first few PPPs, but also as useful precedents for future PPPs over the next few years.

**Current approach of the Bank**

The sector complexes of the Bank – Private Sector, Infrastructure and Industrialisation and Power, Energy, Climate and Green Growth – have PPP experts in their teams. The PPP experts provide support to the country offices in developing the financial structures of projects in RMCs. This form of support is not standard but based on requirements of individual operations.

The Bank provides support in structuring the financing mix for projects when it is the lead financing institution. This support is in the form of optimising the finance drawn from various sources, including concessional finance and climate finance. However, in many such instances, the involvement of the Bank is largely when the project’s preparation, PPP structuring and procurement stages are completed.

In addition, ALSF (an independently funded and administered facility hosted by the Bank) provides support to RMCs in negotiations of contracts with the private sector, including for PPPs. ALSF provides legal support to RMCs to ensure that the public interest and finances are protected, and the risk allocation is optimum in contracts with the private sector.

Additionally, The Bank provides funds for project preparation through its technical assistance windows, trust funds and project preparation facilities, while the procurement is conducted by the RMC based on its own procurement procedures or based on the Bank procurement procedures. The notable facilities include the African Development Fund project preparation facility (ADF PPF), Middle Income Countries Technical Assistance Fund (MIC TAF), NEPAD Infrastructure Project Preparation Facility (NEPAD IPPF), Sustainable Energy Fund for Africa (SEFA) and Fund for African Private Sector Assistance (FAPA).

Previously, the Bank established Regional PPP Hubs (2013-14) with the expectation that they would coordinate with the country offices and provide upstream support to RMCs, develop project pipelines and then work with the private sector / public sector operations to implement the transactions. However, the Regional Hubs were subsequently discontinued due to various reasons.

The Bank’s Vice Presidency for Power, Energy, Climate and Green Growth (PEVP) has been supporting the development of Independent Power Producer (IPP) arrangements in RMC, leveraging on private sector participation. This includes supporting preparatory studies and developing financing structures for complex projects.

Finally, the Bank has supported the establishment of specialized project development vehicles like the Africa50 and Kukuza Project Development Company. Both these facilities play an active role in structuring of selected transactions involving private investments in infrastructure.

Given the deep knowledge of the Bank across countries and sectors, and the various project preparation facilities, the Bank has a solid foundation to assist RMCs in PPP project preparation and transaction advisory. The wide range of RMCs presents a challenge for the Bank. The Bank needs to cater to large, active PPP
markets and at the same time to countries with almost no experience or institutional capacity to implement PPPs. As a result, a single standardised approach may not be effective across the continent. The current approach of the Bank is largely centralised and is individualistic.

**Lessons from peer institutions**

- Most peers have PPP focussed project preparation facilities. Even the newer regionally focussed Banks, like the IsDB and the AIIB have such facilities. Project preparation support of most peers range from feasibility studies up to full transaction support to financial close of deals. However, ADB and the World Bank group, which have the most extensive and active approaches for supporting PPPs, also support earlier stages of project identification, development of project pipelines, and prefeasibility of potential PPP projects.
- ADB and World Bank have active PPP project preparation and transaction advisory offerings in the form of Office of PPP (OPPP) and IFC Advisory, respectively. These entities have been effective in catalysing pilot PPPs, and complex PPP transactions in challenging and nascent PPP markets.
- ADB has effectively used a mix of approaches for supporting project development and PPP transaction structuring in its developing member countries. It has helped establish country level PPP project development funds in countries including India and the Philippines, while at the same time it is providing advisory support on a project level through OPPP on selected deals.
- Many of the facilities offered by the peer institutions are fee based / reimbursable / recoverable. The intent is to make the facilities financially sustainable. There are examples of some facilities being partly effective in recycling the initial funds. In most such facilities, the cost of project preparation is recovered from the successful bidder at the end of the procurement process or from the RMC government agency if the project preparation is terminated before procurement is completed/ procurement is unsuccessful.

**Strategy for Pillar 2 Support to RMCs**

The Bank would support RMCs in developing and structuring bankable PPP projects that can be taken to the market. Support in this Pillar 2 would enable RMCs to leverage private finance, efficiency, and innovation to deliver public infrastructure. The support provided by the Bank under Pillar 2 will cover two stages-(a) Project Preparation and (b) Transaction Management.

The Bank’s support under Pillar 2 would materialize in the form of PPP specific project development financing fulfilling the need of RMC governments for funds to undertake PPP project development and transaction structuring.

The Bank may also support PPP project preparation and transaction structuring by offering PPP preparation and transaction advisory services, deploying its own experts, or directly procured experts/ advisors. The following type of projects would ordinarily be eligible for support of the Bank:

- Pathfinder PPPs in RMCs with no or limited PPP experience;
- Pathfinder PPPs in sectors with no PPP precedents;
- Complex PPPs requiring specialized expertise;
- Strategic or transformative PPPs, in terms of potential impact, or replicability across Africa;
- Regional/ multi country PPPs;

When providing Pillar 2 support, the Bank will ensure that there is no conflict of interest in the two competing roles – on one hand, as transaction advisor, and on the other hand, as creditor or investor. The Bank will endeavor to mitigate this by ensuring that the Bank units and staff involved in these two roles are separate, and that their incentive structure reinforces their independence while performing these two roles.
The Bank will be selective in providing support under Pillar 2 for development and structuring of projects which have a high likelihood of being structured as bankable, commercially attractive (to the private sector) PPPs. To this end, the Bank will use a standard screening methodology to identify projects that are prima facie suitable for being implemented as bankable and financially feasible PPPs. At the same time, the Bank will use its expertise to refine the scope and structure of the screened-out projects to strengthen their financial feasibility and bankability. This would be an opportunity for the Bank to develop innovative PPP structures, suitable to the African and regional contexts.

**Pillar 3: Financing of PPPs**

**Need for financing of PPPs**

In PPP transactions, the financing for the project is wholly or partly transferred to the private sector. A key responsibility of the private partner is therefore to arrange adequate finance for the project inter alia through equity and (various forms of) debt, adequate for the construction and implementation of the project. In some cases, the government contracting agency may contribute a part of the financing required in the form of construction grants, equity, or loans.

Arranging sufficient finance at suitable terms (pricing, tenure, etc.) can be a challenge for private companies in PPP projects. Local lenders in early stage markets often do not have the capacity to offer loans of sufficient size and tenure to match the needs of PPP infrastructure projects. PPP and project financing may be new in the market, with lenders not familiar with structuring the financing and pricing risks, and with questions around the creditworthiness of companies and the security of the government counterparties.

In addition, the inability of most infrastructure project debt in Africa to achieve an investment-grade rating is one of the reasons institutional investors, especially those from outside the region, have provided negligible debt and equity financing. Finally, there are few refinancing opportunities available in many African countries, that can lower the cost of finance after construction.

Institution like the Bank play an important role in addressing some of these financing challenges and help to attract other financial institutions and Banks to the project. They do this by providing long term, reasonably priced finance themselves, but also by mitigating certain risks for co-financiers and equity investors. The robust due diligence and better ability to manage political risks provide comfort to other lenders and investors. In addition, such institutions often mitigate key projects risks through offering subordinate financing and guarantee products.

The Bank’s role in addressing financing challenges and risks, as explained above, also helps to draw in commercial lenders and private investors. Private investors draw comfort from the presence of an institution like the Bank. The Bank’s presence assures private investors that the transaction meets the stringent transparency and probity requirements of the Bank and therefore involves a fair allocation of risks and returns.

In such context, financial support from Development Banks becomes important for making PPPs possible. This conclusion is underlined by the fact that out of the 269 projects in infrastructure with private participation achieving financial closure from 2009 to 2019 in African countries, 173 (64%) had support from bilateral/multilateral institutions.  

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11 PPI Database, World Bank Group
Current approach of the Bank

As the lead multilateral development finance institution in Africa, the Bank has the mandate to enhance the social and economic well-being of the RMCs. The Bank’s AAA rating allows it to on-lend funds raised in international capital markets to its borrowing countries at favourable terms. Beyond the provision of affordable capital, the Bank offers an attractive, diversified menu of financing options and instruments that allow borrowers to tailor financing to their circumstances.

The Bank’s financial products include loans (including synthetic local currency, and syndicated loans), guarantees, equity and quasi-equity, and risk management products. The Bank’s menu of products has evolved over the last decade as the Bank needed to be more responsive to the evolving requirements of its borrowers.

The Bank does not separately identify financing operations directed towards project financing of PPP projects. That makes it challenging to identify the PPP operations and the instruments used in such lending operations.

The 2017 PPP Evaluation of the Bank found that it had 41 PPP transactions with financing (debt and equity participation) representing a total net commitment of approximately UA 2 billion in the period 2006 to 2014.

Due to the project financing nature of PPP transactions, non-sovereign loans were the typical instrument used by the Bank in such transactions. In addition, risk and credit guarantees were also used by the Bank. The loans were typically provided to PPP project companies (Special Purpose Vehicles or SPVs) on project finance basis. The Bank has provided financing on the public sector side of PPPs through sovereign loans. The loan to public side was routed to the SPVs in such cases as viability gap grant, government equity or concessional loans.

The Bank’s portfolio of instruments is largely like that of its peers. While the Bank has no PPP specific instruments, it has the complete range of debt, equity and credit enhancement instruments that might be needed to finance PPPs. The Bank also demonstrates expertise in structuring financial packages for complex projects and provide an attractive package for co-finance investors. The Bank has experience in structuring packages of multiple instruments to meet different financing requirements in the same PPP project. Some of these financing packages represent innovative financing structures. However, these financing packages have not been institutionalised or marketed as ‘PPP’ focussed financing packages by the Bank.

The Bank’s presence in any transaction provides confidence to co-lenders and investors that the transaction is well structured and meets the stringent quality at entry requirements of the Bank. In addition, the Bank’s standing as Africa’s premier development financial institution and its relationship with RMCs helps mitigate political risks to a certain extent, providing further comfort to co-lenders and investors.

Lessons from peer institutions

- Most peers have instruments that are broadly comparable to that of the Bank. Peers have made innovative use of some of the financing instruments to offer facilities that meet the unique needs of PPP projects or facilitate systemic development of PPP markets. The WBG provides financing to governments seeking to support specific projects or PPP programs through viability gap funding or financial intermediary loans. For instance, one of the WBG loans was used to set up a viability gap fund in Vietnam.

- Some peers also include sub-national and municipal infrastructure and offer instruments that can be used for financing infrastructure at these levels. For instance, ADB and World Bank have used multi project lending facilities through financial intermediaries (India Infrastructure Finance Company Limited in India, and Bangladesh Infrastructure Finance Fund Limited in Bangladesh).

The IFC Subnational Finance Program of the WBG provides municipal financing directly to municipal and regional governments, and their service entities including for PPPs that provide key subnational infrastructure services.
Some peers (World Bank, EBRD, ADB) have used innovative approaches to crowd in private investment in infrastructure, by mitigating specific risks and improving the bankability of projects. The World Bank and ADB have used multi-project facilities to co-finance along with domestic Bank. The World Bank has mobilised institutional investment through the Managed Co-Lending Facilities. The EBRD has credit enhanced the project bond issuance in Turkey using contingent loans.

**Strategy for Pillar 3 Support to RMCs**

The Bank will encourage RMCs to consider PPP options in all infrastructure projects for which Bank financing support is requested. At the same time, the Bank will consider PPP options for all potential projects identified by its staff as part of the Country Strategy Paper. The Bank will ensure that private solutions will only be promoted where they are economically viable, fiscally and commercially sustainable, transparent regarding the allocation of risks, provide value for money, are environmentally and socially sustainable, and properly address equity and affordability concerns of consumers.

The Bank will continue to take the lead in structuring and financing of PPP projects in Africa and will use its competitive strengths to attract other development finance institutions, domestic lenders, and private investors. The Bank will use its competitive strengths—strong processes for ensuring quality at entry, ability to manage political risks, ability to structure innovative financial packages and use of risk mitigation instruments to do so. The Bank will institutionalize a few of innovative financing packages used by the Bank, as part of its PPP focused offering and disseminate information on such packages to RMCs.

While the Bank will continue its focus on financing PPPs in power and transport sectors, it will endeavor to increase its financing in sectors such as water and sanitation, urban development, urban transport, public health, education, irrigation and agriculture. The Bank will integrate its efforts across the three pillars to identify, structure and finance more PPPs in such sectors. This will help in catalyzing higher levels of private participation in these sectors in the future. In addition, the Bank will widely disseminate its experience and knowledge of financing PPPs in these sectors to encourage RMCs and co-lenders to increase the use of PPPs in such sectors.

The Bank will gradually offer facilities for financing sub-sovereign PPPs in RMCs through multi-project platforms and/or through financial intermediaries. At present, the project pipelines and PPP activities at sub-sovereign level is limited, but the Bank’s gradual involvement in financing PPPs at such levels may have transformative impact in increasing the extent of private investment. The Bank will use grant windows, in combination with commercially priced loans to develop blended products suitable for economically justified, and transformative PPPs, especially in sectors with limited PPP activities and to promote sub-sovereign PPPs.

In instances where the Bank’s involvement in a project involves both Pillar 2 and 3 operations simultaneously or sequentially the Bank will maintain a strict separation of organization structure or groups of staff involved in either of the two operations to mitigate any potential conflict of interest. On the other hand, the Bank will ensure that the departments involved in the origination and management of the Pillar operations have full and timely access to the regional departments’ assessments and advice on RMCs’ policies, institutions, and strategies.
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